

**NEW ISSUE-  
FULL BOOK ENTRY**

Rating: Moody's (expected): Aaa  
See "Rating" herein

*In the opinion of Hawkins Delafield & Wood LLP, Bond Counsel to the Corporation, under existing statutes and court decisions and assuming continuing compliance with certain tax covenants described herein, interest on the 2004 Refunding Series B Bonds (the "2004B Bonds") is excluded from gross income for Federal income tax purposes pursuant to Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), and such interest is not treated as a preference item in calculating the alternative minimum tax imposed on individuals and corporations under the Code; such interest, however, is included in the adjusted current earnings of certain corporations for the purpose of computing the alternative minimum tax imposed on such corporations. In addition in the opinion of Bond Counsel, under existing statutes, interest on the 2004B Bonds is exempt from all taxation by the State of Hawaii or any county or other political subdivision thereof, except for inheritance, transfer and estate taxes and except to the extent such income may be included in the measure of franchise taxes imposed on banks and other financial corporations pursuant to the laws of the State of Hawaii. See "TAX MATTERS" in this Official Statement.*

**\$23,000,000**

**Housing and Community Development Corporation of Hawaii  
Hawaii Rental Housing System Revenue Bonds  
2004 Refunding Series B**

**Dated: Date of Delivery**

**Due: July 1, 2033**

The 2004 Refunding Series B Bonds (the "2004B Bonds") will be issued as Auction Rate Certificates ("ARCs"), will be fully registered bonds in book-entry form only, and will be initially issued and registered in the name of Cede & Co. as nominee for The Depository Trust Company, New York, New York (collectively referred to herein as "DTC"). Purchasers will not receive certificates representing their interest in the 2004B Bonds. Payments of principal of and interest on the Bonds will be made by U.S. Bank National Association, as Trustee, to DTC for subsequent disbursement to DTC Participants (defined herein) who will remit such payments to the beneficial owners of the 2004B Bonds.

The 2004B Bonds will be dated as of their date of delivery and will mature on July 1, 2033, subject to earlier redemption as described herein. Accrued and unpaid interest on the 2004B Bonds will be due and payable on October 20, 2004, and on each succeeding Interest Payment Date (as defined herein) until maturity or earlier redemption. The Auction Rate shall be established from time to time as described herein. The 2004B Bonds will be issued in denominations of \$25,000 or any integral multiple thereof. The 2004B Bonds are subject to redemption on the terms and conditions and at the prices described herein.

THIS OFFICIAL STATEMENT DESCRIBES THE 2004B BONDS ONLY DURING THE PERIOD BEGINNING ON THE CLOSING DATE AND ENDING ON THE DATE ON WHICH THE INTEREST RATE ON THE 2004B BONDS IS ADJUSTED TO THE FIXED RATE.

Simultaneously with the issuance of the 2004B Bonds, the Corporation will issue \$84,055,000\* in aggregate principal amount of its 2004 Refunding Series A Bonds (the "2004A Bonds" and together with the 2004B Bonds, the "2004 Bonds") on a parity with the 2004B Bonds. The 2004 Bonds are being issued by the Corporation for the purpose of refunding certain outstanding bonds of the Corporation which were issued to provide financing for the development of six multi-family rental housing developments of the Corporation. Additional bonds (including the 2004 Bonds, the "Bonds") may be issued on a parity with the 2004 Bonds to finance additional developments in the future or to refund Bonds issued for such purpose.

The scheduled payment of principal of and interest on the 2004B Bonds when due will be guaranteed under an insurance policy to be issued concurrently with the delivery of the 2004B Bonds by FINANCIAL SECURITY ASSURANCE INC.



The 2004B Bonds are general obligations of the Corporation and the principal of and interest thereon are payable from (i) Net Revenues derived by the Corporation from the operation of the Hawaii Rental Housing System Revenue Bond Program, (ii) funds and accounts held under the Indenture (except to the extent described in the Indenture) and (iii) certain other legally available funds, revenues and assets of the Corporation not appropriated for or committed to any other purpose (except to the extent described in the Indenture).

---

**A MATURITY SCHEDULE AND INFORMATION CONCERNING THE ARCS  
APPEARS ON THE INSIDE FRONT COVER**

---

**The Corporation has no taxing power. The Bonds, including the 2004B Bonds, are payable from Net Revenues and other funds and assets pledged under the Indenture. Subject to any agreements heretofore or hereafter made with the holders of any notes or bonds of the Corporation pledging any particular revenues or assets not pledged under the Indenture, the Bonds, including the 2004B Bonds, are general obligations of the Corporation payable from any of the legally available funds, revenues and assets of the Corporation not appropriated for or committed to any other purpose. The State is not obligated to appropriate moneys for payment on the Bonds, including the 2004B Bonds. The Bonds, including the 2004B Bonds, shall not constitute a general or moral obligation of the State of Hawaii or a charge upon the general fund of the State of Hawaii. The full faith and credit of neither the State of Hawaii nor any political subdivision thereof are pledged to the payment of the principal of and interest on the Bonds, including the 2004B Bonds.**

*The 2004B 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 certain other conditions, including the approval of legality by Hawkins Delafield & Wood LLP, New York, New York, Bond Counsel to the Corporation. Certain legal matters will be passed upon for the Underwriter by its counsel, Watanabe Ing Kawashima & Komeiji LLP, Honolulu, Hawaii. It is expected that the 2004B Bonds in definitive form will be available for delivery to The Depository Trust Company in New York, New York on or about October 13, 2004.*

**UBS Financial Services Inc.**

October 7, 2004

**Maturity Schedule**

\$23,000,000 Housing and Community Development Corporation of Hawaii  
Hawaii Rental Housing System Revenue Bonds  
2004 Refunding Series B

Maturity Date:	July 1, 2033
Last Day of Initial Period:	October 19, 2004
First Auction Date:	October 19, 2004
First Interest Payment Date:	October 20, 2004
Auction Term:	Weekly
Auction Day:	Business Day immediately preceding the first day of each Auction Period

A Holder who desires to sell the ARCs on an Auction Date may be required to continue to hold such ARCs after such Auction Date if sufficient Bids to purchase such ARCs are not received, in which case the Auction Rate will be the Maximum Rate, as defined in Appendix G. Furthermore, there may be circumstances where the Auction Procedures are discontinued or the Broker-Dealer may suspend its participation in an auction increasing the risk that a Holder may be required to continue to hold the ARCs. The Corporation has no obligation to purchase the ARCs that a Holder wishes to sell on an Auction Date. Wilmington Trust Company will initially be the Auction Agent and UBS Financial Services Inc. will initially be the Broker-Dealer. See "THE 2004B BONDS –Special Considerations Relating to the 2004B Bonds."

The information contained in this Official Statement has been obtained from the Housing and Community Development Corporation of Hawaii and other sources deemed reliable. No guaranty is made, however, as to the accuracy or completeness of such information. The Underwriter has provided the following sentence for inclusion in this Official Statement. The Underwriter has reviewed the information in this Official Statement in accordance with, and as part of, its responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriter does not guarantee the accuracy or completeness of such information. This Official Statement, which includes the cover page and appendices, does not constitute an offer to sell the 2004B Bonds in any state to any person to whom it is unlawful to make such offer in such state. No dealer, 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 2004B Bonds, and if given or made, such information or representations must not be relied upon. The information contained herein is subject to change without notice and neither the delivery of this Official Statement nor any sale hereunder at any time implies that the information contained herein is correct as of any time subsequent to its date.

Other than with respect to information concerning Financial Security Assurance Inc. ("Financial Security") contained under the caption "Bond Insurance" and Exhibit F "Form of Bond Insurance Policy" herein, none of the information in this 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 2004B Bonds; or (iii) the tax exempt status of the interest on the 2004B Bonds.

THE 2004B BONDS HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, IN RELIANCE UPON AN EXEMPTION CONTAINED IN SUCH ACT. THE 2004B BONDS HAVE NOT BEEN REGISTERED OR QUALIFIED UNDER THE SECURITIES LAWS OF ANY STATE. IN CONNECTION WITH THIS OFFERING THE UNDERWRITER MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE 2004B 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.

**TABLE OF CONTENTS**

<b>INTRODUCTION .....</b>	<b>1</b>	<b>CONTINUING DISCLOSURE .....</b>	<b>19</b>
<b>THE CORPORATION .....</b>	<b>2</b>	<b>TAX MATTERS .....</b>	<b>19</b>
<b>PURPOSE AND POWERS .....</b>	<b>2</b>	<b>CERTAIN ONGOING FEDERAL TAX</b>	
<b>STAFF .....</b>	<b>3</b>	<b>REQUIREMENTS AND COVENANTS .....</b>	<b>20</b>
<b>RENTAL HOUSING PROGRAMS .....</b>	<b>4</b>	<b>CERTAIN COLLATERAL FEDERAL TAX</b>	
<b>HOME OWNERSHIP PROGRAMS .....</b>	<b>5</b>	<b>CONSEQUENCES .....</b>	<b>20</b>
<b>ADMINISTRATION OF FEDERAL PUBLIC</b>		<b>POSSIBLE GOVERNMENT ACTION .....</b>	<b>20</b>
<b>HOUSING UNITS .....</b>	<b>6</b>	<b>LEGALITY OF BONDS FOR INVESTMENT</b>	<b>20</b>
<b>THE PROGRAM .....</b>	<b>7</b>	<b>LITIGATION .....</b>	<b>20</b>
<b>HAWAII RENTAL HOUSING SYSTEM</b>		<b>CERTAIN LEGAL MATTERS .....</b>	<b>24</b>
<b>REVENUE BOND PROGRAM .....</b>	<b>7</b>	<b>RATING .....</b>	<b>24</b>
<b>THE 2004B BONDS .....</b>	<b>10</b>	<b>UNDERWRITING .....</b>	<b>24</b>
<b>GENERAL DESCRIPTION .....</b>	<b>10</b>	<b>CAUTIONARY STATEMENTS REGARDING</b>	
<b>SPECIAL CONSIDERATIONS RELATING TO</b>		<b>FORWARD-LOOKING STATEMENTS IN</b>	
<b>THE 2004B BONDS AS ARCS .....</b>	<b>11</b>	<b>THIS OFFICIAL STATEMENT .....</b>	<b>24</b>
<b>REDEMPTION OF 2004B BONDS .....</b>	<b>11</b>	<b>FINANCIAL STATEMENTS .....</b>	<b>24</b>
<b>BOOK-ENTRY SYSTEM .....</b>	<b>13</b>	<b>MISCELLANEOUS .....</b>	<b>25</b>
<b>SOURCES OF PAYMENT AND SECURITY</b>		Appendix A - Form of Opinion of Bond Counsel	
<b>FOR THE BONDS .....</b>	<b>14</b>	Appendix B - Audited Financial Statements of the	
<b>NET REVENUES .....</b>	<b>14</b>	Rental Housing System Program	
<b>DEBT RESERVE FUND .....</b>	<b>15</b>	Appendix C - Audited Financial Statements of the	
<b>CORPORATION GENERAL OBLIGATION .....</b>	<b>15</b>	State of Hawaii Affordable Rental	
<b>BOND INSURANCE .....</b>	<b>15</b>	Housing Program	
<b>OBLIGATION OF THE CORPORATION .....</b>	<b>15</b>	Appendix D - Summary of Certain Provisions of the	
<b>ADDITIONAL BONDS .....</b>	<b>16</b>	Indenture	
<b>RATE COVENANT .....</b>	<b>16</b>	Appendix E - Form of Continuing Disclosure	
<b>BOND INSURANCE .....</b>	<b>16</b>	Agreement	
<b>BOND INSURANCE POLICY .....</b>	<b>16</b>	Appendix F - Form of Bond Insurance Policy	
<b>FINANCIAL SECURITY ASSURANCE INC. ....</b>	<b>16</b>	Appendix G - Provisions Relating To 2004B Bonds	
<b>SOURCES AND USES OF FUNDS FOR THE</b>		(Auction Rate Certificates)	
<b>2004 BONDS .....</b>	<b>17</b>		
<b>ANNUAL DEBT SERVICE REQUIREMENTS</b>	<b>17</b>		

**(THIS PAGE INTENTIONALLY LEFT BLANK)**

## Official Statement

relating to

\$23,000,000

Housing and Community Development Corporation of Hawaii  
Hawaii Rental Housing System Revenue Bonds  
2004 Refunding Series B

### INTRODUCTION

This Official Statement, including the cover page and appendices hereto (the "Official Statement"), is provided to furnish information with respect to the offer and sale by the Housing and Community Development Corporation of Hawaii (the "Corporation") of its Hawaii Rental Housing System Revenue Bonds, 2004 Refunding Series B (referred to herein as the "2004B Bonds"). Simultaneously with the issuance of the 2004B Bonds, the Corporation will issue \$84,055,000\* in aggregate principal amount of its 2004 Refunding Series A Bonds (the "2004A Bonds" and together with the 2004B Bonds, the "2004 Bonds"). Issuance of each of the 2004B Bonds and the 2004A Bonds will be contingent upon the issuance of the other series of the 2004 Bonds.

The 2004 Bonds are being issued under, pursuant to and in full compliance with the Constitution of the State of Hawaii (the "State") and the statutes of the State, including particularly Part III of Chapter 39, Hawaii Revised Statutes, and Chapter 201G, Hawaii Revised Statutes (collectively, the "Act"), and under and pursuant to a resolution of the Board of Directors of the Corporation, duly adopted on September 16, 2004, and the Trust Indenture, dated as of October 1, 2004, between the Corporation and U.S. Bank National Association, as trustee (the "Trustee"), as supplemented by the First Supplemental Trust Indenture, dated as of October 1, 2004, relating to the 2004 Bonds (collectively, the "Indenture"). All capitalized terms used in this Official Statement that are defined in the Indenture and not otherwise defined herein shall have the respective meanings set forth in the Indenture.

The Corporation, a public body and a body corporate and politic duly organized and existing under the provisions of Chapter 201G, Hawaii Revised Statutes, was established by Act 350, Session Laws of Hawaii, 1997 Regular Session, effective July 1, 1998, for the purpose of consolidating the jurisdiction, functions, powers, duties and authority previously exercised by the Housing Finance and Development Corporation ("HFDC"), the Hawaii Housing Authority (the "Authority") and the Rental Housing Trust Fund of the State. HFDC was itself established in 1987 for the purpose of assuming the housing finance, housing development and residential leasehold functions of the Authority. The Corporation has succeeded to all of the rights and powers previously exercised, and all of the duties and obligations incurred by, HFDC, the Authority and the Rental Housing Trust Fund. The Act provides that nothing therein shall affect the validity or the terms and provisions of any bond theretofore issued by the State, the Authority or HFDC under prior law. Unless the context otherwise indicates, the term "Corporation" shall also be used to refer to the Authority and HFDC in describing or referring to powers originally granted to the Authority or HFDC but transferred to the Corporation or to previous activities of the Authority or HFDC which relate to such transferred functions. In addition to its multi-family programs described below, the Corporation is empowered under the Act to raise funds through the sale of revenue bonds and to make those funds available at affordable interest rates to meet the housing needs of persons and families of low and moderate income living in the State of Hawaii (the "State"). See "THE CORPORATION - Home Ownership Programs."

The Corporation has operated two multi-family rental housing programs, the prior Rental Housing System Program ("RHSP") and the State of Hawaii Affordable Rental Housing Program ("SHARP"), and issued bonds under indentures of the Corporation for the respective programs to finance six housing projects owned by the Corporation (each a "Project"). The Corporation has determined that it is in its best interest to consolidate RHSP and SHARP into a single multi-family rental housing program, the Hawaii Rental Housing System Revenue Bond Program, referred to herein as the "Program". Proceeds of the 2004 Bonds, net of certain expenses incurred in connection with the issuance of the 2004 Bonds, together with certain amounts held under the indentures for RHSP and SHARP, will be applied to refund all six series of bonds (collectively, the "Refunded Bonds") which were previously issued under RHSP and SHARP which are described in more detail below.

<u>Refunded Bonds</u>	<u>Outstanding Principal Amount</u>	<u>Project</u>
RHSP 1989 Series A	\$14,000,000	Honokowai Kauhale Rental Housing Development
RHSP 1990 Series A	31,400,000	Kamakee Vista Rental Housing Development
RHSP 1990 Series B	33,400,000	Pohulani Rental Housing Development
RHSP 1993 Series A	10,050,000	La'ilani Rental Housing Development
SHARP 1993 Series A	29,800,000	Kauhale Kakaako Program Development
SHARP 1995 Series A	<u>6,685,000</u>	Kekuilani Courts Rental Housing Development
<b>Total:</b>	<b><u>\$125,335,000</u></b>	

The 2004B Bonds and the 2004A Bonds are the first two series of bonds to be issued under the Indenture for the Program. The Corporation is authorized to issue additional series of bonds under the Indenture, the proceeds of which will be used for the production of multi-family rental housing units to be included in the Program or to refund all or a portion of bonds outstanding under the Indenture or other indenture. Additional bonds and refunding bonds issued under the Indenture will rank pari passu with the 2004 Bonds. The 2004 Bonds and all such additional bonds and refunding bonds are hereinafter collectively referred to as the "Bonds".

All Bonds will be secured equally and ratably by the Net Revenues and by other funds and assets (except as otherwise expressly provided in the Indenture) pledged thereto under the Indenture and constituting the Trust Estate. In addition, subject to any agreements heretofore or hereafter made with the holders of any notes or bonds of the Corporation pledging any particular revenues or assets not pledged under the Indenture, the Bonds, including the 2004B Bonds, are general obligations of the Corporation payable from any of the legally available funds, revenues and assets of the Corporation not appropriated for or committed to any other purpose or from the proceeds of the municipal bond insurance policy to be issued, simultaneously with the delivery of the 2004B Bonds, by Financial Security Assurance Inc. (the "Insurer"), all as more fully described herein under "BOND INSURANCE" and "SECURITY FOR THE BONDS – Bond Insurance."

**The Corporation has no taxing power. The Bonds, including the 2004B Bonds, are obligations only of the Corporation and shall not constitute a general or moral obligation of the State or a charge upon the general fund of the State, and the full faith and credit of neither the State nor any political subdivision thereof are pledged to the payment of the principal of and interest on the Bonds, including the 2004B Bonds. The Act does not provide that the Corporation may request payment on the Bonds by the State and the State is not obligated to appropriate moneys for such purpose.**

This Official Statement includes a description of the Corporation and its programs, including the Program, the Projects, the 2004B Bonds, the sources of payment and security for the Bonds, including the 2004B Bonds, and a summary of the Indenture. All references herein to the Indenture are qualified in their entirety by reference to the definitive form thereof, which may be obtained from or inspected at the offices of the Corporation, and all references to the Bonds, including the 2004B Bonds, are further qualified by reference to the information with respect to the Bonds, including the 2004B Bonds, contained in the Indenture.

## THE CORPORATION

### Purpose and Powers

The Corporation, a public body and a body corporate and politic organized and existing under Hawaii law, was established in 1998 as successor to the Authority and HFDC. HFDC itself had been established in 1987 to assume the housing finance, housing development and residential leasehold functions of the Authority. At that time, the Authority, a public body and a body corporate and politic in existence since 1935, retained its housing development (including construction and ownership) as well as management functions. Under the Act, the jurisdiction, functions, powers, duties and authority previously conferred upon the Authority and HFDC were transferred to and conferred upon the Corporation and are to be performed and enforced by the Corporation. In addition, the Act provides that all documents executed or entered into by or on behalf of the Authority or HFDC pursuant to provisions made applicable to the Corporation by the Act shall remain in full force and effect.

The Corporation has been granted powers, among others, to acquire real or personal property by purchase or by exercise of the power of eminent domain to provide housing; to study and undertake projects for the clearing, replanning

or reconstruction of areas in which unsafe or unsanitary dwelling or housing conditions exist; to counsel prospective homeowners and other persons and governmental agencies on housing issues and to apply for and receive federal assistance, insurance or guaranties. The Corporation has the power to issue bonds for its purposes and to secure payment thereof by a pledge of specified property of the Corporation.

The Legislature of the State of Hawaii has authorized an aggregate principal amount of \$375,000,000 in revenue bonds for the Corporation's rental housing programs, of which amount to date the Corporation has issued \$170,225,000 of bonds. The Legislature has also authorized the Corporation to issue, with the approval of the Governor, revenue bonds in an aggregate principal amount of \$2,275,000,000 to make funds available for single family housing programs, of which amount to date the Corporation has issued \$1,676,585,000 of bonds for the Single Family Mortgage Purchase Program and \$20,000,000 of bonds for the Home Mortgage Purchase Program described below. The Legislature has also authorized an aggregate principal amount of \$300,000,000 in revenue bonds for privately owned multi-family rental housing projects, of which amount to date the Corporation has issued \$74,713,000 of bonds.

The audited financial statements of the Corporation for the year ended June 30, 2003 (the most recent available audited financial statements for the Corporation) may be reviewed at the Corporation's web site at [www.hcdch.hawaii.gov](http://www.hcdch.hawaii.gov) by selecting "Amended' FY 2003 Independent Auditor's Report" under the heading "HCDCH Reports and Studies." Other information which may be obtained, directly or indirectly, from the Corporation's web site should **not** be relied upon by an investor in making a decision to buy any of the 2004B Bonds. Financial statements of the Corporation for the year ended June 30, 2004, have been completed by the Corporation's staff, but are subject to review and to audit. Prospective purchasers of the 2004 Bonds may request a copy of such unaudited, internal financial statements from the Corporation.

### **Organization**

For administrative purposes only, the Corporation is considered a part of the State's Department of Human Services. The Corporation's Board of Directors consists of nine members, six of whom are public members appointed by the Governor, with at least one each from each of the counties of Honolulu, Hawaii, Maui and Kauai. The Director of Business, Economic Development and Tourism and the Director of Human Resources or their designated representatives, and the Governor's Special Assistant for Housing are ex-officio voting members. The Board of Directors selects from its public members a Chairperson and Vice-Chairperson. All Corporation action must be taken by the affirmative vote of at least five members. There is currently one vacancy on the Board. The members and officers of the Board and the dates of expiration of their respective terms are as follows:

**Charles A. Sted**, Chairperson (Honolulu). President & Chief Executive Officer, Hawaii Pacific Health.  
Term expires June 30, 2005.

**Charles King**, Vice Chairperson (Kauai). President & Owner, King Auto Centers and King Windward Nissan.  
Term expires June 30, 2008.

**Francis L. Jung, Esq.**, Secretary (Hawaii). Senior Partner, Jung & Vassar P.C. Term expires June 30, 2006.

**Travis Thompson**, (Maui). Retired. Formerly Director of Finance, County of Maui. Term expires June 30, 2008.

**Betty Lou Larson** (At Large). Director, Housing Assistance Program, Catholic Charities Elderly Services.  
Term expires June 30, 2006.

**Linda Smith**, Ex-Officio. Senior Policy Advisor, Office of the Governor.

**Lillian B. Koller, Esq.**, Ex-Officio. Director, Department of Human Services.

**Theodore E. Liu**, Ex-Officio. Director, Department of Business, Economic Development and Tourism.

### **Staff**

Principal members of the Corporation's staff with responsibilities for various aspects of the Program are as follows:

**Stephanie Aveiro**, Executive Director, Housing and Community Development Corporation of Hawaii. Ms. Aveiro was appointed to her current position in December, 2003. Prior to this appointment, Ms. Aveiro had been the Special Assistant to Governor Lingle since December, 2002. Previously, Ms. Aveiro served as the Executive Director of the Hawaii Medical Association from 2000 to 2001, and the Director of the County of Maui's Department of Housing and Community Concerns from 1991 to 1998. She received her B.A. degree in Public Administration from the University of Hawaii - West Oahu.

**Darren Ueki**, Finance Manager. Mr. Ueki has served as Finance Manager for the Corporation since January, 2001. Previously, Mr. Ueki served as a Project Resource Specialist for the Corporation since February, 1990. Prior to joining the Corporation, Mr. Ueki was a Program Budget Analyst with the Department of Budget and Finance. He received a B.B.A. degree in Economics from the University of Hawaii.

**Marilyn E.Y. Chock**, Mortgage and Rental Finance Section Chief. Ms. Chock has served as Mortgage and Rental Finance Section Chief since July, 2000. Previously, Ms. Chock served as a Finance Specialist for the Corporation since January, 1986. Prior to joining the Corporation, Ms. Chock worked in the credit department of the University of Hawaii bookstore. She received a B.B.A. degree in Finance from the University of Hawaii.

**Dean M. Sakata**, Finance Specialist. Mr. Sakata has served as a Finance Specialist since December, 2001. Prior to joining the Corporation, Mr. Sakata worked as Vice President at Key Community Development Corporation and at Bank of America. He received an M.B.A. from Portland State University and a B.B.A. degree in Finance from the University of Hawaii.

**Lloyd T. Fukuoka**, Finance Specialist. Mr. Fukuoka has served as a Finance Specialist since November, 1997. Previously, Mr. Fukuoka served as a Loan Specialist for the Corporation since August, 1989. Prior to joining the Corporation, Mr. Fukuoka was a loan underwriter with Pioneer Federal Savings Bank. He received a B.B.A. degree in Management from the University of Hawaii.

**Lisa C. Wond**, Finance Specialist. Ms. Wond has served as a Finance Specialist since July, 1999. Previously, Ms. Wond served as a Land Program Specialist since September, 1985. She received a B.S. degree in Human Development from the University of Hawaii.

The Corporation has been authorized to employ up to 330 permanent positions with an additional authorization to retain 107 personnel on a contractual basis. The Corporation currently maintains approximately 437 positions (permanent and on contract) to manage, operate and maintain its various housing programs and housing projects. The number of employees assigned to each of the housing program areas are: Central Administration/Technical/Support Services: 76 positions; Property Management and Maintenance: 268 positions; Resident Services: 13 positions; Homeless Programs: 11 positions; Housing Development: 44 positions; and Finance: 25 positions.

The Corporation's office is located at 677 Queen Street, Suite 300, Honolulu, Hawaii 96813, and its telephone number is 808-587-0641.

### **Rental Housing Programs**

**General.** In order to assist in the delivery of affordable rental housing throughout the State on a cost-effective basis, the Legislature of the State has authorized the Corporation to issue, with the approval of the Governor, revenue bonds in an aggregate principal amount of \$375,000,000 to finance or refinance rental housing projects developed or acquired by the Corporation. Under this authority the Corporation had established two multi-family rental housing programs the Rental Housing System Program ("RHSP") and the State of Hawaii Affordable Rental Housing Program ("SHARP"). The Corporation has determined that it is in its best interest to consolidate RHSP and SHARP into a single multi-family rental housing program under the name Hawaii Rental Housing System Revenue Bond Program and referred to herein as the "Program". The Program is described below under "THE PROGRAM."

The housing programs described in this Section, other than the Program, have no claim on the assets or the Net Revenues pledged under the Indenture, nor are the revenues generated from these programs pledged to secure payment of the Bonds, including the 2004B Bonds.

**Multi-family Revenue Bond Program.** The Legislature has authorized the Corporation to issue, with the approval of the Governor, revenue bonds in an aggregate principal amount of \$300,000,000 to finance development of privately-owned multi-family rental housing projects. Under this authority, the Corporation operates a rental housing revenue bond program and provides project financing to qualified private developers of eligible multi-family rental housing projects by directly making, or by contracting with mortgage lenders to fund, such loans. The Corporation has issued six series of bonds, including one refunding series, in the total aggregate principal amount of \$74,713,000, of which approximately \$32,000,000 principal amount are presently outstanding, to make loans for construction or acquisition/rehabilitation of multi-family housing developments with a total of 620 units of which 417 are set aside for residents with low or moderate income. Each series of bonds is payable solely from revenues derived from the project financed.

**Rental Assistance Program.** The Rental Assistance Program ("RAP"), together with the Interim Construction Loan Program, is part of the Rental Assistance Revolving Fund. The Corporation uses the RAP to subsidize the rental payments of eligible persons and families. Program subsidies are committed to specific projects for tenants with incomes that do not exceed 80% of the area median income. Funding for the RAP is provided by the principal and investment income from the Rental Assistance Revolving Fund and from origination fees and interest earned on loans which are made under the Interim Construction Loan Program. The RAP has been used by the Corporation to provide assistance to tenants in five of the Projects which constitute the Program. See, "THE PROGRAM - The Projects." As of June 30, 2004 the balance in the Rental Assistance Revolving Fund was approximately \$38 million (unaudited). The total original commitment for the Rental Assistance Program was approximately \$87 million, of which approximately \$48 million remains outstanding. The Corporation believes that it will have sufficient funding to fulfill its obligations under the Rental Assistance Program as such obligations become due.

**Low Income Housing Tax Credit Program.** This program provides incentives, through tax credits, to developers and owners of private rental housing projects where the monthly rents are affordable for tenants with incomes of 60%, or lower, of the area median income. Under this program, the Corporation allocates federal and state income tax credits to the owners of qualified projects who agree to maintain regulated rental rates for a specified period. As of June 30, 2004, the Corporation had allocated credits for the development of 50 projects containing a total of 4,157 dwelling units. Of these units, 3,711 have been constructed and are operational and 446 units are planned or under construction.

**Rental Housing Trust Fund Program.** The Rental Housing Trust Fund Program ("RHTFP") provides "equity gap" low-interest loans or grants to qualified owners and developers constructing affordable rental housing units. Under RHTFP, the Corporation provides financing for capacity building for non-profit organizations, as well as predevelopment, interim/construction and permanent financing for the purpose of constructing new, or rehabilitating existing, affordable rental housing. To date over \$54.3 million of project awards have been issued under RHTFP to thirty projects for the development of 2,270 rental units. RHTFP has also awarded thirty-five capacity building grants and one predevelopment loan. In 2001, the Legislature authorized the Corporation to issue up to \$30 million of revenue bonds for RHTFP.

### **Home Ownership Programs**

**General.** The Legislature has also authorized the Corporation to issue, with the approval of the Governor, revenue bonds in an aggregate principal amount of \$2,275,000,000 to make funds available for single family housing loan programs. The housing programs described in this Section have no claim on the assets or the Net Revenues pledged under the Indenture, nor are the revenues generated from these programs pledged to secure payment of the Bonds, including the 2004B Bonds.

**Single Family Mortgage Purchase Program.** The Single Family Mortgage Purchase Program has been the Corporation's primary program to assist low and moderate income borrowers to finance the purchase of owner-occupied single family residences. Under this program the Corporation has issued bonds having an aggregate principal amount of \$1,676,585,000, of which \$368,290,000 principal amount are presently outstanding. As of June 30, 2004, proceeds of bonds previously issued under this Program have been issued to purchase 9,860 mortgage loans with a total original principal amount of \$1,024,084,735. The Corporation is presently authorized to purchase mortgage loans directly from originating mortgage lenders and to purchase Federal National Mortgage Association ("FNMA") securities backed by mortgage loans originated by participating mortgage lenders in Hawaii.

**Housing Development and Ownership Program.** Under this program the Corporation has the power to acquire land through condemnation; to develop and construct housing projects on its behalf or in partnership with private developers; to provide interim construction loans and other financing to qualified borrowers; and to request exemption from certain local zoning, planning and building ordinances in the development of State housing projects. The prior emphasis of this program was on providing low and moderate income families with the opportunity to purchase homes at a cost within their financial capabilities. The Corporation's current focus under this program is on facilitating the private for-profit and non-profit development or preservation of rental and for-sale units for lower income families and special need groups. As of June 30, 2004, the Corporation has helped to provide 16,749 dwelling units under this program.

This program has been implemented from moneys in the Dwelling Unit Revolving Fund ("DURF") created by the State Legislature in 1970 and funded from the proceeds of general obligation bonds issued from time to time by the State of Hawaii in the aggregate principal amount of \$125,000,000. The Corporation uses DURF to pursue a policy of providing housing for persons and families of low income. The Corporation has carried out this policy by, among other things, selling housing units constructed by the Corporation at prices which reflect no profit and by making developable

land available and making low-interest construction loans to private developers. As of June 30, 2004, the fund equity of DURF was approximately \$150 million (unaudited).

**Broadened Homesite Ownership Program.** Historically, land in the State has been owned in fee simple by a few large landowners. These owners have leased their lands under long term leases. Widespread use of such long term leasing has resulted in a shortage of affordable single family residential land in fee simple. In 1967, the State Legislature granted the Corporation the power to assist lessees of residential land in acquiring fee simple title to their land at a reasonable cost. This program authorizes the Corporation to acquire the leased fee interest in leased land through the use of eminent domain and to reconvey the leased fee interest to the lessees. The United States Supreme Court upheld the constitutionality of this use of the power of eminent domain in Hawaii Housing Authority v. Midkiff, 467 U.S. 229 (1984). As of June 30, 2004, the Corporation had assisted in the conversion of 14,688 residential lots. The Corporation has created a Fee Simple Residential Revolving Fund to assist lessees in financing the purchase of leased fee interests.

**Mortgage Credit Certificate Program.** In November 1990, the Corporation was authorized to issue mortgage credit certificates to eligible mortgage loan borrowers entitling such borrowers to take a direct credit against their federal income tax liability. The credits, which amount to 20% of mortgage loan interest, are intended to assist "first time" moderate income home buyers to qualify for mortgage loans. As of June 30, 2004, the Corporation had traded in \$126,440,000 of single family mortgage revenue bond authority for \$31,610,000 of mortgage credit certificate authority, and had assisted 642 families with mortgage credit certificates.

#### **Administration of Federal Public Housing Units**

One of the functions which the Corporation assumed from the Authority was the administration of the operations of the 5,390 federal public housing units in Hawaii with funds received from the United States Department of Housing and Urban Development ("HUD"). The operation of the federal public housing units is a distinct and separate function from the operation of the Program (and its predecessor programs, RHSP and SHARP) and the funds provided by HUD for the operation of the federal programs are not available to pay the debt service on the 2004B Bonds.

HUD conducts periodic audits of the federal housing programs of the housing agencies with which it works, including the Corporation. Based upon findings from audits conducted of the Corporation, in September, 2002, HUD issued a Corrective Action Order, which cited the Corporation for "irregularities relating to [the Corporation's] performance administering Public and Indian Housing Programs." In particular, HUD expressed concerns about the failure of the Corporation to spend funds provided to it by HUD in a timely manner and on budget items other than those designated.

The Corrective Action Order required that the Corporation fund, at a cost of \$1,200,000, (i) an independent assessment (the "Assessment") of the Corporation's operations, assets, and capabilities to properly administer the federal public housing program and portfolio effectively and (ii) a feasibility study of the entire federal housing portfolio of the Corporation, including a physical needs assessment, five, ten and twenty year plans to address deficiencies and needs and a database of information collected. This work was conducted pursuant to a contract between HUD and IBM Business Consulting Services.

The Assessment, issued in April, 2003, concluded that the Corporation's operation of the federal housing programs suffered from weaknesses in areas of organization, structure, procedural and management and noted some HUD regulatory violations. However, the assessment also noted, "that [the Corporation] had already begun to address some of these issues in constructive and quantifiable ways, such as the reductions in the number of staff vacancies, eviction hearing wait times, and unit vacancies. Based upon our limited review we determined that [the Corporation] also possesses opportunities to address the housing needs of the Hawaii community."

In late 2002, based upon its concerns about the administration of the Federal housing programs, HUD had demanded that the then Executive Director of the Corporation step down and that the entire Board resign. The then Executive Director retired from State service at the end of November, 2002 and, following the election of a new Governor for the State, all of the members of the Board submitted their resignations effective at the end 2002. The Executive Director and Board members listed above were all appointed following the election of the Governor in 2002.

In addition to its periodic audits, HUD established a system for rating the performance of public housing agencies with which it works with throughout the country in managing and operating the federal public housing programs. The system is known as the Public Housing Assessment System or "PHAS" and measures performance under four categories: (i) physical, (ii) financial, (iii) management operations and (iv) resident survey. For the fiscal years (ending September 30) 2000 through 2002, the Corporation had been deemed a "Standard Performer" under PHAS.

However, in June, 2004, HUD notified the Corporation that it had been designated to be an "overall troubled agency" for its fiscal year ending June 30, 2003. The Corporation was not faulted for its policing or upkeep at the federal projects, but HUD was concerned with property management issues, including allowing the use of outdated forms; failure to check for verification of tenant income or citizenship; vacant unit turnaround time; and lease enforcement. With respect to financial reporting, the Corporation was faulted for its failure to submit acceptable audited financial information within the timeframe established by the federal authorities. The Corporation has now furnished to HUD all audited financial information for its fiscal year ending June 30, 2003, and the Corporation has taken action which it believes will prevent delays in the preparation of audited financial information for fiscal year 2004 and thereafter.

As a result of the Corporation being designated as an overall troubled agency, HUD prepared a Memorandum of Agreement ("MOA") which identifies specific and detailed performance targets and strategies for the Corporation to implement to improve its performance under the four categories included in PHAS in the operation of federal housing programs and the areas of weakness noted in the Assessment. Estimated completion dates for the various targets and strategies identified in the MOA range from November 1, 2004 through September 30, 2005. Under the MOA, HUD will provide technical assistance to the Corporation to assist it in achieving the performance targets and the Corporation will provide monthly, quarterly and annual progress reports to HUD. Failure of the Corporation to achieve the targets established by the MOA could lead to additional sanctions being imposed or recommended by HUD and could impact future federal financial awards and assistance. While recognizing it will require a significant effort on its part, and that it has to work within State civil service, procurement, contracting and other requirements, the Corporation agrees with HUD that the performance targets established in the MOA are reasonable and can be achieved. The Corporation has committed to take the necessary action to achieve the performance targets established in the MOA. The Corporation's Board of Directors approved the MOA on September 16, 2004, and delegated authority to its Executive Director to enter into the MOA. The MOA is expected to be executed in the near future.

The Corporation believes that implementation of the MOA will improve its performance in the operation of its federal housing programs. The Corporation does not believe that any of the deficiencies that have been identified in the operation of the federal housing programs have had or will have a material impact on the ability of the Corporation to fulfill its mission to operate its rental housing or home ownership programs, including the Program, which are not part of the federal housing portfolio; to maintain its trust funds; or to pay the debt service due on the Bonds.

Another function within the Corporation is the HUD Section 8 Housing Assistance Payment Program. The Corporation is the Performance Based Contract Administrator for Hawaii for this program. With respect to the Corporation's administration of this program, earlier this year HUD expressed concerns about the Corporation's failure to comply with required HUD procedures. To address this issue, the Corporation has subcontracted with the Bremerton (Washington) Housing Authority to perform the administrative functions of the program. This course of action follows a national trend of hiring specialists to handle the work.

## **THE PROGRAM**

### **Hawaii Rental Housing System Revenue Bond Program**

The Hawaii Rental Housing System Revenue Bond Program (the "Program") is designed to assist in the delivery of affordable rental housing throughout the State on a cost-effective basis. The Program is designed to facilitate the development of multi-family rental housing projects which are owned by the Corporation (either through construction or acquisition) and financed from the proceeds of bonds issued by the Corporation or from other sources available to the Corporation. The 2004 Bonds are the first to be issued under the Indenture following the consolidation of RHSP and SHARP. The Bonds issued for the Program are secured by a lien on, and pledge of all of the Net Revenues and other funds and assets of the Program and are payable (i) from Net Revenues derived by the Corporation from the operation of the Program, (ii) from funds and accounts held under the Indenture (except to the extent described in the Indenture) and (iii) as a general obligation of the Corporation, from any of the legally available funds, revenues and assets of the Corporation not appropriated for or committed to any other purpose (except to the extent described in the Indenture).

The single largest component of Revenues is the rental income received for the rental of the units in the Projects. See, "SOURCES OF PAYMENT AND SECURITY FOR THE BONDS – Net Revenues" and Table 1 below. The Corporation determines the rental rates for the Projects and is currently undertaking a review of the rental rates now in effect and the prevailing commercial rental rates in the market. In making this analysis, the Corporation is gathering information from various sources, including the private contractors which manage the Projects (as described in "The Projects" below). Upon completion of the analysis, the Corporation expects to implement some increases in the rental rates for the Projects so that such rates will better relate to general market conditions.

Under the predecessor programs which have been consolidated into the Program, the Corporation has issued and has outstanding six series of bonds in the original aggregate principal amount of \$152,545,000 of which \$125,335,000 principal amount are presently outstanding. All of such bonds (the "Refunded Bonds") will be refunded with the proceeds of the 2004 Bonds and other funds available under the indentures pursuant to which the Refunded Bonds were issued. Upon the issuance of the 2004 Bonds, the six Projects financed or refinanced with the Refunded Bonds will be included in the Program. All have been completed and are in operation and are briefly described below. For further descriptions of the Projects, see "The Projects" below.

<u>Projects</u>	<u>Description</u>	<u>Original Financing (Year and Amount)</u>	<u>Outstanding Principal Amount</u>
<b>RHSP Projects</b>			
La'ilani	200-unit project in Kailua-Kona, Hawaii	1987 \$14,950,000 (Refunded in 1993)	\$10,050,000 (1993 Bonds)
Honokowai Kauhale	184-unit project in West Maui	1989 \$16,500,000	\$14,000,000
Kamakee Vista	226-unit high-rise residential and commercial mixed use project in the Kakaako District of Honolulu	1990 \$33,500,000	\$31,400,000
Pohulani	262-unit high-rise residential and commercial mixed use project in the Kakaako District of Honolulu	1990 \$35,700,000	\$33,400,000
<b>SHARP Projects</b>			
Kauhale Kakaako	268-unit high-rise residential, light industrial and commercial mixed use project with parking for tenants and the public in the Kakaako District of Honolulu	1993 \$30,700,000	29,800,000
Kekuilani Courts	80 units of residential housing in 10 two-story buildings	1995 \$7,020,000	\$6,685,000

Set forth as Appendices C and D hereto, respectively, are the audited financial statements of RHSP and SHARP for the fiscal years ended June 30, 2002 and 2003, the most recent years for which audited financial information is available. Set forth below in Table 1 are combined summaries of revenues and expenses for RHSP and SHARP and the Corporation's fiscal year 2005 budget for the Program. The information for fiscal years 2000 - 2003 has been re-formatted by the Corporation from the audited financial information of the programs.

**TABLE 1**  
Housing and Community Development Corporation of Hawaii  
Combined RHS and SHARP (Fiscal Years ending June 30)

	<u>2000<sup>1</sup></u>	<u>2001<sup>1</sup></u>	<u>2002<sup>1</sup></u>	<u>2003<sup>1</sup></u>	<u>2004<sup>2</sup></u>	<u>Budget 2005</u>
<b>Revenues</b>						
Rental	\$12,773,921	\$12,919,585	\$12,465,736	\$13,070,304	\$13,223,911	\$12,925,000
Interest Earnings	1,978,722	2,165,325	911,896	509,053	316,328	310,000
Other	<u>770,269</u>	<u>351,394</u>	<u>637,944</u>	<u>633,650</u>	<u>691,665</u>	<u>435,000</u>
Total	\$15,522,912	\$15,436,304	\$14,015,576	\$14,213,007	\$14,231,904	\$13,670,000
<b>Expenses</b>						
Project Expenses	\$4,105,211	\$4,053,016	\$4,425,017	\$4,582,015	\$5,705,219	\$5,300,000
Other Operating Expenses	<u>778,596</u>	<u>547,496</u>	<u>390,603</u>	<u>635,157</u>	<u>409,809</u>	<u>350,000</u>
Total	\$4,883,807	\$4,600,512	\$4,815,620	\$5,217,172	\$6,115,028	\$5,650,000
Net Revenues Available for Debt Service on Bonds	<u>\$10,639,105</u>	<u>\$10,835,792</u>	<u>\$9,199,956</u>	<u>\$8,995,835</u>	<u>\$8,116,876</u>	<u>\$8,020,000</u>

<sup>1</sup> Re-Formatted by Corporation from Audited Financial Statements

<sup>2</sup> Unaudited

## **The Projects**

The Refunded Bonds were issued to construct the Projects which are each briefly described below. No bond proceeds were used to finance the commercial, light industrial or office space or any day-care facilities included in the Projects, except to the extent such facilities are used solely by governmental entities or as permitted by the law in effect at the time the respective financings were completed.

Each of the Projects is owned by the Corporation, operated by a contractor on behalf of the Corporation and has one unit set aside for a resident manager. Hawaii Affordable Properties, Inc., based in Honolulu, operates all of the Projects except Honokowai Kauhale which is operated by Urban Real Estate, also based in Honolulu. The operators are selected based upon responses to "Requests for Proposals" published by the Corporation. For each Project, the operator is paid a monthly management fee (ranging from approximately \$1,700 to approximately \$4,900) and reimbursed for certain costs associated with the operation of the Project (including salaries, benefits and employment taxes of employees assigned to a Project (such as the resident manager and building maintenance personnel), other taxes, accounting fees and liability insurance).

Each of the Projects other than Kekuilani Courts has been accepted into the RAP which provides rental subsidies to families with low or moderate income. See, "THE CORPORATION – Rental Housing Programs – Rental Assistance Program" above. For the Projects in the RAP other than Pohulani, sixty percent (60%) of the units are included in the RAP and the rental subsidy per unit is up to \$175 per month. For Pohulani, which is targeted for elderly couples and individuals, all of the units are included in the RAP and the monthly subsidy per unit is up to \$250. The contracts pursuant to which the rental assistance payments are made were entered into at the times the projects commenced operations and last for approximately thirty years. The remaining commitments under these contracts total approximately \$32 million.

### **La'ilani, Kailua-Kona, Hawaii**

The La'ilani Project was the first development to be financed under the RHSP and was completed in 1988. The Project is located on Manawale'a Street, Kailua-Kona, Hawaii, on approximately 15.5 acres of land, and consists of 25 two-story buildings containing 200 rental units comprised of 32 one-bedroom apartments, 144 two-bedroom apartments and 24 three-bedroom apartments. The buildings are constructed on slab-on-grade with wood frames, and all units are equipped with a range, hood fan, refrigerator, smoke detector and wall-to-wall carpeting. Parking and laundry facilities are also provided. Occupancy during the twelve month period ending June 30, 2004 was 96.48%.

### **Honokowai Kauhale, Maui**

The Honokowai Kauhale Rental Housing Development (the "Honokowai Project"), completed in 1990, consists of 23 two-story buildings located at Honokowai, Maui, Hawaii, on approximately 11.9 acres, containing 184 affordable rental units comprised of 42 one-bedroom apartments, 112 two-bedroom apartments and 30 three-bedroom apartments. Each of the buildings is constructed on concrete slabs with wood frames. All apartment units are equipped with a range, hood fan, refrigerator, smoke detector and wall-to-wall carpeting. Parking and laundry facilities are also provided. The Honokowai Project is constructed on land leased by the Corporation from the Department of Land and Natural Resources of the State of Hawaii. Occupancy during the twelve month period ending June 30, 2004 was 96.72%.

### **Kamakee Vista, Honolulu, Oahu**

The Kamakee Vista Rental Housing Development (the "Kamakee Project"), completed in 1991, is located in the Kakaako District of Honolulu, Oahu, Hawaii, an area near the central business district of Honolulu. The Kamakee Project consists of a twenty-eight story building containing 226 affordable rental units comprised of 90 one-bedroom apartments and 136 two-bedroom apartments. In addition, 28,800 square feet of commercial/office space, a day-care facility and 288 parking spaces are also included. Each apartment unit is equipped with a refrigerator, range with hood, carpets, drapes and ceiling fans. Laundry facilities and a landscaped recreation deck with barbecue areas have also been provided. This Kamakee Vista Project is constructed on land leased by the Corporation from the Hawaii Community Development Authority, a public corporate body. Occupancy during the twelve month period ending June 30, 2004 was 97.93%.

### **Pohulani, Honolulu, Oahu**

The Pohulani Rental Housing Development (the "Pohulani Project"), completed in 1992, also located in the Kakaako District of Honolulu, consists of a twenty-five story building containing 262 affordable rental units targeted for elderly couples and individuals, comprised of 128 studio apartments and 134 one-bedroom

apartments. In addition, commercial/office space, retail space and 191 covered parking spaces are also included. Each apartment unit is equipped with a refrigerator, range with hood, carpets, drapes and emergency call system. Amenities include a landscaped recreation deck containing a lap pool, jogging path, barbecue area, garden plots, multi-purpose room, central laundry facilities and secured entrance lobby. The Pohulani Project is constructed on land owned by the Corporation in fee simple. Occupancy during the twelve month period ending June 30, 2004 was 97.49%.

#### **Kauhale Kakaako, Honolulu, Oahu**

The Kauhale Kakaako Rental Housing Development, also located in the Kakaako District of Honolulu, is a 268 unit multi-family rental housing development project completed in December, 1993. This project has 116 one-bedroom and 152 two-bedroom units and is located on 71,614 square feet of land. This Project consists of a 29-story high-rise tower and a five-story parking structure. It includes 268 affordable rental apartment units with balconies, approximately 13,522 square feet of light industrial space, 200 square feet of commercial space for a convenience store and 698 parking stalls for tenants integrated with 500 stalls dedicated for public parking on a shared basis. Occupancy during the twelve month period ending June 30, 2004 was 99.97%.

#### **Kekuilani Courts, Honolulu, Oahu**

The Kekuilani Courts Rental Housing Development is located on approximately 4,728 acres of land in the Villages of Kapolei, on the southwest coast of the island of Oahu, Hawaii. This Project consists of 10 two-story buildings, each comprised of 8 two-bedroom, one-bath units. The Project provides 80 affordable rental apartments. Each apartment provides 760 square feet of living area, plus a lanai. A total of 160 parking stalls are available. Other amenities include a separate, free-standing community center (with kitchen facilities), a tot lot, barbecue areas, and centralized laundry facilities. Occupancy during the twelve month period ending June 30, 2004 was 94.52%.

### **THE 2004B BONDS**

#### **General Description**

The 2004B Bonds will be issued as Auction Rate Certificates ("ARCs") and will be issued as fully registered bonds in denominations of \$25,000 or any integral multiple thereof. The 2004B Bonds will be dated their date of delivery and bear interest from that date until the Initial Auction Date at the initial rate established in connection with the initial offering and thereafter at the Applicable ARCs Rate established for the 2004B Bonds as set forth in the Indenture and summarized in "Appendix G - Provisions Relating To 2004B Bonds (Auction Rate Certificates)." UBS Financial Services Inc. will serve as the Broker-Dealer and Market Agent for the 2004B Bonds and the Auction Agent will be Wilmington Trust Company.

The Auction Period for the 2004B Bonds will generally be the 7-day period commencing on a Wednesday and ending on, and including, a Tuesday (subject to modification in the event of holidays or in the event that the 2004B Bonds are subject to redemption or at maturity). The Initial Auction Period will be from the date of delivery of the Series 2004B Bonds through October 19, 2004. The Auction Date is the Business Day immediately preceding the first day of each Auction Period. The initial Auction Date will be October 19, 2004.

The initial Interest Payment Date will be October 20, 2004. Thereafter interest will be paid on the day following the end of each Auction Period, and upon the redemption date or the stated maturity date of the 2004B Bonds. Except for an Interest Payment Date occurring on a redemption date or the stated maturity date, interest will be paid on the following Business Day if such day is not a Business Day. The Record Date for the payment of interest is the date preceding the Interest Payment Date which is the greater of two Business Days or one Business Day plus the number of Business Days by which the Auction Date precedes the first day of the next succeeding Auction Period. See "Appendix G - Provisions Relating To 2004B Bonds (Auction Rate Certificates)." The Auction Period is not subject to adjustment.

For a further description of ARCs and the terms applicable to the Series 2004B Bonds, See "Appendix G - Provisions Relating To 2004B Bonds (Auction Rate Certificates)."

The 2004B Bonds, when issued, will be registered in the name of Cede & Co., as nominee for The Depository Trust Company, New York, New York ("DTC"). DTC will act as securities depository for the Bonds. Individual purchases of the 2004B Bonds will be made in book-entry form only (the "Book-Entry System"), in the principal amount of \$25,000 or integral multiples thereof. Purchasers will not receive certificates representing their interest in the 2004B Bonds. Principal of and premium, if any, and interest on the 2004B Bonds will be paid by the Trustee 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 2004B Bonds, as described herein. See "THE BONDS - Book-Entry System," below.

### **Special Considerations Relating to the 2004B Bonds as ARCs**

The Indenture and the Auction Agreement provide that the Auction Agent may resign from its duties as Auction Agent by giving at least 90 days' notice, or 30 days' notice if it has not been paid, to the Corporation, Market Agent, Insurer and the Trustee. In the event of a resignation because the Auction Agent has not been paid, there is no requirement that a replacement Auction Agent be in place at the effective date of such resignation. The Broker-Dealer Agreement provides that the Broker-Dealer thereunder may resign upon 30 days' notice to the Auction Agent, the Corporation and the Insurer or may suspend its obligations immediately under certain circumstances, and does not require, as a condition to the effectiveness of such resignation or suspension, that a replacement Broker-Dealer be in place. For any Auction Period during which there is no duly appointed Auction Agent, or during which there is not duly appointed Broker-Dealer, it will not be possible to hold Auctions, with the result that the interest rate on the 2004B Bonds will be determined as set forth in the definition of Auction Rate in Appendix G - Provisions Relating to the ARCs.

The Broker-Dealer Agreement will provide that a Broker-Dealer may submit an Order in Auctions for its own account. If a Broker-Dealer submits an Order for its own account in any Auction, it might have an advantage over other Bidders in that it would have knowledge of orders placed through it in that Auction; such Broker-Dealer, however, would not have knowledge of Orders submitted by other Broker-Dealers (if any) in that Auction. As a result of bidding by a Broker-Dealer in an Auction, the Auction Rate may be lower than the rate that would have prevailed had the Broker-Dealer not bid. A Broker-Dealer may also bid in an Auction in order to prevent what would otherwise be (a) a failed Auction, (b) an "all-hold" Auction, or (c) the implementation of an Auction Rate that the Broker-Dealer believes, in its sole judgment, does not reflect the market for such securities at the time of the Auction. In the Broker-Dealer Agreement, all Broker-Dealers will agree to handle customer orders in accordance with their respective duties under applicable securities laws and rules.

According to published news reports, the Securities and Exchange Commission (the "Commission") has requested information from a number of broker-dealers regarding certain of their practices in connection with auction rate securities, such as the practices described in the preceding paragraph. The Broker-Dealer has advised the Corporation that it, as a participant in the auction rate securities markets, has received a letter from the Commission requesting that it voluntarily conduct an investigation regarding certain of its practices and procedures in connection with those markets. The Broker-Dealer is cooperating with the Commission in providing the requested information. No assurance can be given as to whether the results of this process will affect the market for the 2004B Bonds or the auctions therefor.

### **Redemption of 2004B Bonds**

#### Optional Redemption

The 2004B Bonds shall be subject to redemption prior to maturity, at the option of the Corporation, as a whole or in part at any time, in such order as the Corporation shall determine, at a redemption price equal to the principal amount thereof, plus accrued interest thereon to the date fixed for redemption, without premium.

#### Sinking Fund Redemption

The 2004B Bonds are also subject to redemption in part by lot prior to their scheduled maturity at a redemption price equal to the principal amount thereof, without premium, plus accrued interest to the date of redemption, in amounts sufficient to redeem (or pay at maturity) on January 1 and July 1 of each year the principal amount of such Bonds specified for each of the years schedule shown below:

Mandatory Sinking Fund Payments

<u>Payment Dates</u>	<u>Principal Amount</u>	<u>Payment Dates</u>	<u>Principal Amount</u>
January 1, 2005	\$ 0	July 1, 2019	\$400,000
July 1, 2005	250,000	January 1, 2020	400,000
January 1, 2006	250,000	July 1, 2020	400,000
July 1, 2006	250,000	January 1, 2021	400,000
January 1, 2007	275,000	July 1, 2021	425,000
July 1, 2007	275,000	January 1, 2022	425,000
January 1, 2008	275,000	July 1, 2022	425,000
July 1, 2008	275,000	January 1, 2023	450,000
January 1, 2009	275,000	July 1, 2023	450,000
July 1, 2009	275,000	January 1, 2024	450,000
January 1, 2010	300,000	July 1, 2024	450,000
July 1, 2010	300,000	January 1, 2025	475,000
January 1, 2011	300,000	July 1, 2025	475,000
July 1, 2011	300,000	January 1, 2026	475,000
January 1, 2012	300,000	July 1, 2026	475,000
July 1, 2012	300,000	January 1, 2027	500,000
January 1, 2013	325,000	July 1, 2027	500,000
July 1, 2013	325,000	January 1, 2028	500,000
January 1, 2014	325,000	July 1, 2028	525,000
July 1, 2014	325,000	January 1, 2029	525,000
January 1, 2015	350,000	July 1, 2029	525,000
July 1, 2015	350,000	January 1, 2030	550,000
January 1, 2016	350,000	July 1, 2030	550,000
July 1, 2016	350,000	January 1, 2031	550,000
January 1, 2017	375,000	July 1, 2031	575,000
July 1, 2017	375,000	January 1, 2032	575,000
January 1, 2018	375,000	July 1, 2032	575,000
July 1, 2018	375,000	January 1, 2033	600,000
January 1, 2019	375,000	July 1, 2033 <sup>#</sup>	600,000

<sup>#</sup> Stated maturity

Notice of Redemption; Procedure for Selection

Notice of the redemption of each 2004B Bond shall be mailed by the Trustee or if the Trustee shall so direct, by the Broker-Dealer, at least once not less than fifteen (15) nor more than forty-five (45) days prior to the dated fixed for the redemption thereof, by first class mail, postage prepaid, to DTC as the registered owner of the 2004B Bonds. The failure of DTC to receive such notice by mail or any defect in such notice will not affect the sufficiency of the proceedings for the redemption of 2004B Bonds.

Any notice of redemption may state that it is conditional upon receipt by the Trustee of moneys sufficient to pay the redemption price of such 2004B Bond or upon the satisfaction of any other condition, or that it may be rescinded upon the occurrence of any other event. Any conditional notice so given may be rescinded at any time before payment of such redemption price if any such condition so specified is not satisfied or if any such other event occurs. The Trustee shall give notice of any such condition to the affected registered owners of 2004B Bonds as promptly as practicable upon the failure of such condition or the occurrence of such other event.

## **Book-Entry System**

*Information on DTC and 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 Corporation 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 Corporation or the Underwriter.

DTC will act as securities depository for the 2004B Bonds. The 2004B 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 2004B Bonds, each in the aggregate principal amount of such maturity, 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 provision 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, LLC, 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 2004B Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the 2004B Bonds on DTC's records. The ownership interest of each actual purchaser of each 2004 Bond (for the purposes of the discussion under "Book-Entry System," "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 ownership interests in the 2004B 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 ownership interests in 2004B Bonds, except in the event that use of the Book-Entry System for the 2004B Bonds is discontinued.

To facilitate subsequent transfers, all 2004B Bonds deposited by Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co. The deposit of 2004B 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 2004B Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such 2004B 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.

Redemption notices shall be sent to Cede & Co. If less than all of the 2004B Bonds are being redeemed, DTC's practice is to determine by lot the amount of the ownership interest of each Direct Participant in such maturity to be redeemed.

*Voting Rights.* Neither DTC nor Cede & Co. will consent or vote with respect to 2004B Bonds. Under its usual procedures, DTC mails an Omnibus Proxy to the Corporation or the Registrar 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 2004B 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 2004B Bonds will be made to DTC. DTC's practice is to credit Direct Participants' accounts on the payment 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 payment 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 Corporation, 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 Corporation, 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.* DTC may discontinue providing its services as securities depository with respect to the 2004B Bonds at any time by giving reasonable notice to the Corporation. Under such circumstances, in the event that a successor securities depository is not obtained, bond certificates are required to be printed and delivered.

The Corporation 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.

*Use of Certain Terms in other Sections of the Official Statement.* In reviewing this Official Statement it should be understood that while the 2004B Bonds are in the book-entry system, references in other sections of this Official Statement to owners should be read to include the person for which the Participant acquires an interest in the 2004B Bonds, but: (i) all rights of ownership must be exercised through DTC and the system of book-entry; and (ii) notices that are to be given to owners by the Corporation or the Trustee 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.

The Corporation and the Underwriter will have no responsibility or obligation to Direct Participants, to Indirect Participants or to Beneficial Owners nor do they give assurances with respect to (i) the accuracy of any records maintained by DTC, any Direct Participants or Indirect Participants, or (ii) the payment by DTC, any Direct Participants or any Indirect Participants of any amount in respect of principal or redemption price of or interest on the 2004B Bonds, or (iii) any notice which is permitted or required to be given to owners under the Indenture (except such notice as is required to be given by the Corporation or the Trustee to DTC), or (iv) the selection by DTC of any Participant to receive payment in the event of a partial redemption of the 2004B Bonds, or (v) any consent given or other action taken by DTC as owner of the 2004B Bonds, or (vi) any other event or purpose. Neither the Corporation nor the Underwriter is responsible or liable for the failure of DTC or any Direct Participant or Indirect Participant to make any payments or to give any notice to a Beneficial Owner with respect to the 2004B Bonds or any error or delay relating thereto.

## **SOURCES OF PAYMENT AND SECURITY FOR THE BONDS**

The Indenture provides the sources of payment and security for the Bonds, including the 2004B Bonds. Certain provisions of the Indenture are described below. See, also, Appendix D - Summary of Certain Provisions of the Indenture. There will not be any mortgage on any of the Projects or other property of the Corporation to secure the Corporation's obligation to make debt service payments with respect to the Bonds.

### **Net Revenues**

The Bonds, including the 2004B Bonds, are payable from and secured by the Net Revenues derived from the Program and all amounts in funds and accounts established under the Indenture (other than the Rebate Fund) as security for payment of the Bonds; provided, however that amounts on deposit in any Escrow Fund derived from the proceeds of sale of any series of Bonds shall be pledged as provided in the supplemental indenture providing for the issuance of the Bonds of such series. "Net Revenues" is defined by the Indenture to mean, for any period, the Revenues during such period less the Operation and Maintenance Costs during such period. "Revenues" is defined to mean all revenues, income, rents, fees, charges and receipts derived by the Corporation from or attributable to the ownership and operation of the Program, including the applicable portion of any federal, state or local rent subsidy payment, all amounts derived from investment of moneys held under the Indenture and required to be paid into the Revenue Fund, proceeds derived by the Corporation from the disposition of property and proceeds of insurance and condemnation awards, in each case arising out of the Corporation's ownership of the Program and deposited in the Revenue Fund, and any amounts specifically pledged or designated by the Corporation and deposited in the Revenue Fund as provided in a supplemental indenture. See, also, "Corporation General Obligation" below and Appendix D - Summary of Certain Provisions of the Indenture.

## **Debt Reserve Fund**

The Indenture provides for the establishment by the Trustee of a Debt Reserve Fund from the proceeds of the sale of 2004 Bonds or by deposit of a surety bond, insurance policy or letter of credit in an amount equal to the Debt Reserve Requirement. The Debt Reserve Requirement is for the 2004B Bonds is an amount equal to ten percent (10%) of the initial public offering price of the 2004B Bonds. The Debt Reserve Requirement for the 2004A Bonds is, as of the date of calculation, an amount equal to the maximum Aggregate Debt Service for all 2004A Bonds Outstanding as computed for any Bond Year.

Under the Indenture, amounts credited to the Debt Reserve Fund shall be used to pay, when due, Principal Installments and accrued interest on the Bonds to the extent necessary to remedy a deficiency in the Debt Service Fund.

The Indenture provides that the Debt Reserve Requirement applicable to the 2004B Bonds shall initially be \$2,300,000 and the Corporation expects to satisfy the Debt Reserve Requirement by deposit of a surety bond or insurance policy issued by the Insurer. See "BOND INSURANCE."

## **Corporation General Obligation**

The Indenture provides that, in addition to the Trust Estate, and subject to any agreements heretofore or hereafter made with the holders of any notes or bonds of the Corporation pledging any particular revenues or assets not pledged under the Indenture, the Bonds, including the 2004B Bonds, are general obligations of the Corporation payable from any of the legally available funds, revenues and assets of the Corporation not appropriated for or committed to any other purpose. The Indenture does not restrict the ability of the Corporation to use, appropriate or commit funds, revenues or assets not pledged under the Indenture for any other purpose for which they may be used.

Currently, the principal source of such other security is the Dwelling Unit Revolving Fund ("DURF"), which is described above under "THE CORPORATION -- Home Ownership Programs - Housing Development and Ownership Program." DURF has a balance, as of June 30, 2004, of approximately \$150 million (unaudited), but is pledged as security for certain other obligations of the Corporation and the amounts therein are also available for the use of the program for which it was created. The Corporation is not required to maintain any minimum balance in DURF and the cash balance can vary significantly. In addition, amounts in DURF are subject to transfers mandated by the legislature. The legislature has mandated such transfers in the past and may so in the future. The transfers which have occurred are as follows (in \$ millions): 1995 - \$18.4; 1998 - \$6.4; 2002 - \$12.0; 2003 - \$15.0; and 2004 - \$10.0. Therefore, there can be no assurance that amounts will be available therein if needed in connection with the Bonds, including the 2004B Bonds, and the current respective balance in DURF should not be viewed as indicative of amounts that may be available at any time.

## **Bond Insurance**

Payment of the principal of and interest on the 2004B Bonds when due will be insured by the Insurer. See "BOND INSURANCE" and Appendix F - Form of Bond Insurance Policy.

Under the Indenture, the Insurer must consent to any amendment of the Indenture and the Insurer shall be deemed to be the sole holder of the 2004 Bonds, including the 2004B Bonds, for the purpose of exercising any voting right or privilege or giving any consent or direction or taking any other action that the holders of the 2004 Bonds, including the 2004B Bonds, are entitled to take pursuant to the provisions of the Indenture relating to the Trustee and events of default and remedies. See Appendix D - Summary of Certain Provisions of the Indenture-- Events of Default and Remedies of Owners of the Bonds. In addition, the 2004B Bonds may not be accelerated without the consent of the Insurer and in the event that the 2004B Bonds are accelerated, the Insurer may elect, in its sole discretion, to pay accelerated principal and interest accrued on the 2004B Bonds to the date of acceleration (to the extent unpaid by the Corporation) and the Trustee is required to accept such amounts.

## **Obligation of the Corporation**

The Bonds are obligations of the Corporation and shall not constitute a general or moral obligation of the State or a charge upon the general fund of the State, and the full faith and credit of neither the State nor any county or political subdivision thereof are pledged to the payment of the principal of and interest on the Bonds. The Act does not provide that the Corporation may request payment on the Bonds by the State and the State is not obligated to appropriate moneys for such purpose.

The covenants and agreements set forth in the Indenture to be performed by the Corporation are for the equal and proportionate benefit, security and protection of all owners of the Bonds, and all Bonds rank pari passu under the Indenture except as otherwise provided in the Indenture.

### **Additional Bonds**

The Indenture permits the issuance of additional parity Bonds to provide funds for the Corporation's acquisition, construction and rehabilitation of Program Developments ("Additional Bonds") and to refund Outstanding Bonds issued under the Indenture ("Refunding Bonds"). See Appendix D - Summary of Certain Provisions of the Indenture--Additional Bonds and Refunding Bonds. In addition, the Corporation may issue other evidences of indebtedness payable out of and secured by amounts in the General Reserve Fund maintained under the Indenture so long as the pledge of such amounts to such indebtedness shall be subordinate in all respects to the pledge of such amounts created for the benefit of the Bonds by the Indenture.

### **Rate Covenant**

The Corporation has covenanted in the Indenture that if then permitted by law, the Corporation will, at all times while any of the Bonds shall be Outstanding, establish, fix, prescribe, maintain and collect rates, rents, fees and charges for the use and occupancy of Program Developments so as to provide (i) Net Revenues which, together with other lawfully available funds, shall be sufficient, in each Bond Year, to provide an amount equal to 1.25 times the Aggregate Debt Service on Outstanding Bonds for such Bond Year and (ii) Net Revenues which shall be sufficient, in each Bond Year, to provide an amount equal to 1.10 times the Aggregate Debt Service on Outstanding Bonds for such Bond Year.

The Corporation must review its rates, rents, fees and charges at least annually and revise the same as necessary to comply with the foregoing rate covenant.

The failure by the Corporation to comply with the rate covenant shall not be deemed a default if (A) the Corporation presents a plan to the Trustee to remedy such failure within ninety (90) days from the date of notification of such failure by the Trustee and the Corporation implements such plan and pursues the same diligently until the failure is corrected or (B) upon the failure of the Corporation to present such plan within such ninety (90) days from the date of notification, (i) the Housing Consultant, upon request by the Trustee, presents such plan within sixty (60) days thereafter and the Corporation implements such plan provided by the Housing Consultant and pursues the same diligently until the failure is corrected or (ii) a Housing Consultant's certificate is delivered to the Trustee stating that the schedule of rates, rents, fees and charges which will comply with such covenant is impracticable at such time and the Corporation establishes a schedule of rates, rents, fees and charges, as recommended by the Housing Consultant, which permits the Corporation to comply as nearly as practicable with such rate covenant.

## **BOND INSURANCE**

### **Bond Insurance Policy**

Concurrently with the issuance of the Bonds, Financial Security Assurance Inc. ("Financial Security") will issue its Municipal Bond Insurance Policy for the 2004 Bonds, including the 2004B Bonds (the "Policy"). The Policy guarantees the scheduled payment of principal of and interest on the 2004B Bonds when due as set forth in the form of the Policy included as Appendix F 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 financial guaranty 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, and of Dexia Credit Local, a direct wholly-owned subsidiary of Dexia, S.A. Dexia, S.A., through its bank subsidiaries, is primarily engaged in the business of public finance, banking and asset management in France, Belgium and other European countries. No shareholder of Holdings or Financial Security is liable for the obligations of Financial Security.

At June 30, 2004, Financial Security's total policyholders' surplus and contingency reserves were approximately \$2,212,545,000 and its total unearned premium reserve was approximately \$1,501,280,000 in accordance with statutory accounting practices. At June 30, 2004, Financial Security's total shareholders' equity was approximately \$2,438,206,000

and its total net unearned premium reserve was approximately \$1,255,708,000 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 2004B 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 2004B 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 2004B Bonds or the advisability of investing in the 2004B 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 Corporation the information presented under this caption for inclusion in the Official Statement.

### **SOURCES AND USES OF FUNDS FOR THE 2004 BONDS**

**(Includes 2004A Bonds and 2004B Bonds)**

**Sources**

Principal Amount of 2004A Bonds	\$ 84,055,000
Principal Amount of 2004B Bonds	23,000,000
Funds Held Under RHSP Indenture*	12,746,705
Funds Held Under SHARP Indenture*	8,660,498
<b>Total Sources</b>	<u><u>\$128,462,203</u></u>

**Uses of Funds**

Deposit to Escrow to Current Refund:	
RHSP Bonds	\$ 90,065,484
SHARP 1993 Series A Bonds	30,102,885
Deposit to Escrow to Advance Refund SHARP 1995 Series A Bonds	7,120,082
Municipal Bond Insurance Premiums for 2004 Bonds	95,428
Debt Reserve Fund Surety Bond Premiums for 2004 Bonds	150,269
Cost of Issuance**	928,055
<b>Total Uses of Funds</b>	<u><u>\$128,462,203</u></u>

\* It is expected that approximately \$23 million of other funds held under each of the RHSP and SHARP indentures will be transferred to the Indenture.

\*\* Includes underwriters' discount and other costs of issuance for the 2004 Bonds.

### **ANNUAL DEBT SERVICE REQUIREMENTS**

Total debt service requirements of the Program are listed in the following Table 2. Because issuance of each of the 2004B Bonds and the 2004A Bonds will be contingent upon the issuance of the other series of the 2004 Bonds, the table assumes the issuance of each series of the 2004 Bonds and the refunding of all the Refunded Bonds. The 2004B Bonds will be issued as Auction Rate Certificates with interest paid as described above. See "THE 2004B BONDS – General Description." For the purposes of Table 2, it is assumed that interest on the 2004B Bonds will be paid semi-annually based upon a 360-day year composed of twelve 30-day months with an assumed interest rate of 3.16% per annum (which is the Certified Interest Rate under the Indenture; see Appendix D – Summary of Certain Provisions of the Indenture – Certain Definitions).

**TABLE 2**

**Total Annual Debt Service\***  
**Housing and Community Development Corporation of Hawaii**  
**\$107,055,000 Hawaii Rental Housing System Revenue Bonds, including**  
**\$84,055,000 of 2004A Bonds and \$23,000,000 of 2004B Bonds**

Date	2004A Bonds		2004B Bonds		Total Annual Debt Service
	Principal	Interest	Principal	Interest	
1/1/2005	\$760,000	\$766,645.75	\$0	\$157,473.33	\$1,684,119.08
7/1/2005	840,000	1,763,482.50	250,000	363,400.00	-
1/1/2006	850,000	1,756,342.50	250,000	359,450.00	6,432,675.00
7/1/2006	855,000	1,748,267.50	250,000	355,500.00	-
1/1/2007	865,000	1,739,290.00	275,000	351,550.00	6,439,607.50
7/1/2007	875,000	1,729,558.75	275,000	347,205.00	-
1/1/2008	885,000	1,719,277.50	275,000	342,860.00	6,448,901.25
7/1/2008	895,000	1,708,215.00	275,000	338,515.00	-
1/1/2009	910,000	1,696,580.00	275,000	334,170.00	6,432,480.00
7/1/2009	920,000	1,683,385.00	275,000	329,825.00	-
1/1/2010	935,000	1,669,585.00	300,000	325,480.00	6,438,275.00
7/1/2010	950,000	1,654,625.00	300,000	320,740.00	-
1/1/2011	965,000	1,638,950.00	300,000	316,000.00	6,445,315.00
7/1/2011	985,000	1,622,545.00	300,000	311,260.00	-
1/1/2012	1,000,000	1,605,553.75	300,000	306,520.00	6,430,878.75
7/1/2012	1,020,000	1,587,553.75	300,000	301,780.00	-
1/1/2013	1,035,000	1,569,193.75	325,000	297,040.00	6,435,567.50
7/1/2013	1,055,000	1,550,046.25	325,000	291,905.00	-
1/1/2014	1,075,000	1,530,528.75	325,000	286,770.00	6,439,250.00
7/1/2014	1,095,000	1,510,103.75	325,000	281,635.00	-
1/1/2015	1,115,000	1,489,298.75	350,000	276,500.00	6,442,537.50
7/1/2015	1,140,000	1,467,556.25	350,000	270,970.00	-
1/1/2016	1,160,000	1,445,326.25	350,000	265,440.00	6,449,292.50
7/1/2016	1,185,000	1,420,676.25	350,000	259,910.00	-
1/1/2017	1,210,000	1,395,495.00	375,000	254,380.00	6,450,461.25
7/1/2017	1,235,000	1,369,782.50	375,000	248,455.00	-
1/1/2018	1,260,000	1,343,538.75	375,000	242,530.00	6,449,306.25
7/1/2018	1,290,000	1,316,763.75	375,000	236,605.00	-
1/1/2019	1,315,000	1,289,351.25	375,000	230,680.00	6,428,400.00
7/1/2019	1,345,000	1,261,407.50	400,000	224,755.00	-
1/1/2020	1,370,000	1,232,826.25	400,000	218,435.00	6,452,423.75
7/1/2020	1,400,000	1,203,713.75	400,000	212,115.00	-
1/1/2021	1,430,000	1,173,963.75	400,000	205,795.00	6,425,587.50
7/1/2021	1,465,000	1,141,073.75	425,000	199,475.00	-
1/1/2022	1,500,000	1,107,378.75	425,000	192,760.00	6,455,687.50
7/1/2022	1,530,000	1,072,878.75	425,000	186,045.00	-
1/1/2023	1,565,000	1,037,688.75	450,000	179,330.00	6,445,942.50
7/1/2023	1,605,000	1,001,693.75	450,000	172,220.00	-
1/1/2024	1,640,000	964,778.75	450,000	165,110.00	6,448,802.50
7/1/2024	1,680,000	927,058.75	450,000	158,000.00	-
1/1/2025	1,715,000	888,418.75	475,000	150,890.00	6,444,367.50
7/1/2025	1,755,000	848,973.75	475,000	143,385.00	-
1/1/2026	1,795,000	808,608.75	475,000	135,880.00	6,436,847.50
7/1/2026	1,840,000	766,875.00	475,000	128,375.00	-
1/1/2027	1,880,000	724,095.00	500,000	120,870.00	6,435,215.00
7/1/2027	1,925,000	680,385.00	500,000	112,970.00	-
1/1/2028	1,970,000	635,628.75	500,000	105,070.00	6,429,053.75
7/1/2028	2,015,000	589,826.25	525,000	97,170.00	-
1/1/2029	2,060,000	542,977.50	525,000	88,875.00	6,443,848.75
7/1/2029	2,110,000	495,082.50	525,000	80,580.00	-
1/1/2030	2,160,000	446,025.00	550,000	72,285.00	6,438,972.50
7/1/2030	2,210,000	394,725.00	550,000	63,595.00	-
1/1/2031	2,265,000	342,237.50	550,000	54,905.00	6,430,462.50
7/1/2031	2,315,000	288,443.75	575,000	46,215.00	-
1/1/2032	2,370,000	233,462.50	575,000	37,130.00	6,440,251.25
7/1/2032	2,430,000	177,175.00	575,000	28,045.00	-
1/1/2033	2,485,000	119,462.50	600,000	18,960.00	6,433,642.50
7/1/2033	2,545,000	60,443.75	600,000	9,480.00	-
1/1/2034	-	-	-	-	3,214,923.75
<b>Totals:</b>	<b>\$84,055,000</b>	<b>\$65,954,827</b>	<b>\$23,000,000</b>	<b>\$12,213,268</b>	

\* Based upon fiscal years ended June 30. Interest on the 2004A Bonds is actual; interest on the 2004B Bonds is assumed to be paid semi-annually based upon a 360-day year composed of twelve 30-day months with an assumed interest rate of 3.16%.

## CONTINUING DISCLOSURE

The Corporation has covenanted for the benefit of the Holders and Beneficial Owners of the 2004B Bonds to provide certain financial information and operating data relating to the Corporation not later than nine months following the end of the Corporation's fiscal year, commencing with a report for the Corporation's fiscal year ending June 30, 2004 (the "Annual Bond Disclosure Report"), and to provide notices of the occurrence of certain enumerated events, if material. The Annual Bond Disclosure Report will be filed with each Nationally Recognized Municipal Securities Information Repository and with the State Repository, if any. The notices of material events will be filed with the Municipal Securities Rulemaking Board and with the State Repository, if any. The specific nature of the information to be contained in the Annual Bond Disclosure Report and the notices of material events is set forth in Appendix E - Form of Continuing Disclosure Undertaking. These covenants have been made in order to assist the Underwriter in complying with SEC Rule 15c2-12(b) (5).

The Corporation has made similar undertakings with respect to other bonds issued by it. In certain instances described below, the Corporation did not file its annual bond disclosure report in a timely manner. The Corporation has addressed the causes for such failures and is currently in compliance with the continuing disclosure requirements for all bonds for which it has an obligation to file an annual bond disclosure report. The Corporation believes that the actions it has taken will prevent any such delayed filings in the future.

The annual reports for bonds issued under the Corporation's Single Family Mortgage Purchase Program, including the 1997 Series A, 1997 Series B, 1998 Series A, 1998 Series B and 1998 Series C, for the fiscal years ending June 30, 1997, and June 30, 1999, which should have been filed, respectively, prior to the end of March, 1998, and March, 2000, were filed by October 7, 1998, and April 27, 2000, respectively. All required annual reports for fiscal year 2000 and thereafter have been filed in a timely manner.

The annual reports for the Refunded Bonds issued for SHARP for fiscal years 1996 through 2002 and the annual reports for bonds issued in 1995 by the Corporation on behalf of the University of Hawaii for its Faculty Housing project for fiscal years 1995 through 2002 were inadvertently not filed as required on a timely basis. All of such annual reports for the SHARP bonds and for the University bonds were filed in July, 2003. The required annual report for the SHARP bonds for fiscal year 2003 was filed in a timely manner. For fiscal year 2003, the University was delayed in providing information about the University to the Corporation. As a result, filing of the annual report for the University bonds for fiscal year 2003 was delayed and was not filed until June 10, 2004.

The Corporation has not failed to comply in any other respect with any previous undertaking pursuant to Rule 15c2-12 and, as noted above, the Corporation believes that the actions it has taken will prevent any such delayed filings in the future.

## TAX MATTERS

In the opinion of Hawkins Delafield & Wood LLP, Bond Counsel to the Corporation, under existing statutes and court decisions and assuming continuing compliance with certain tax covenants described herein, interest on the 2004B Bonds is excluded from gross income for Federal income tax purposes pursuant to Section 103 of the Internal Revenue Code of 1986, as amended (the "Code") and such interest is not treated as a preference item in calculating the alternative minimum tax imposed on individuals and corporations under the Code; such interest, however, is included in the adjusted current earnings of certain corporations for purpose of computing the alternative minimum tax imposed on such corporations. In rendering its opinion, Bond Counsel has relied on certain representations, certifications of fact, and statements of reasonable expectations made by the Corporation in connection with the 2004 Bonds, and Bond Counsel has assumed compliance by the Corporation with certain ongoing covenants to comply with applicable requirements of the Code to assure the exclusion of interest on the 2004 Bonds from gross income under Section 103 of the Code.

In addition, in the opinion of Bond Counsel, under existing statutes, interest on the 2004B Bonds is exempt from all taxation by the State of Hawaii or any county or any political subdivision thereof, except inheritance, transfer, and estate taxes and except to the extent such income may be included in the measure of franchise tax imposed on banks and other financial corporations pursuant to the laws of the State of Hawaii.

Bond Counsel expresses no opinion regarding any other Federal or state tax consequences with respect to the 2004B Bonds. Bond Counsel renders its opinion under existing statutes and court decisions as of the issue date, and assumes no obligation to update its opinion after the issue date to reflect any future action, fact or circumstance, or change in law or interpretation, or otherwise. Bond Counsel expresses no opinion on the effect of any action hereafter

taken or not taken in reliance upon an opinion of other counsel on the exclusion from gross income for Federal income tax purposes of interest on the 2004B Bonds, or under state and local tax law.

#### **Certain Ongoing Federal Tax Requirements and Covenants**

The Code establishes certain ongoing requirements that must be met subsequent to the issuance and delivery of the 2004 Bonds in order that interest on the 2004B Bonds be and remain excluded from gross income under Section 103 of the Code. These requirements include, but are not limited to, requirements relating to use and expenditure of gross proceeds of the 2004 Bonds, yield and other restrictions on investments of gross proceeds, and the arbitrage rebate requirement that certain excess earnings on gross proceeds be rebated to the Federal government. Noncompliance with such requirements may cause interest on the 2004B Bonds to become included in gross income for Federal income tax purposes retroactive to their issue date, irrespective of the date on which such noncompliance occurs or is discovered. The Corporation has covenanted to comply with certain applicable requirements of the Code to assure the exclusion of interest on the 2004B Bonds from gross income under Section 103 of the Code.

#### **Certain Collateral Federal Tax Consequences**

The following is a brief discussion of certain collateral Federal income tax matters with respect to the 2004B Bonds. It does not purport to address all aspects of Federal taxation that may be relevant to a particular owner of a 2004 Bond. Prospective investors, particularly those who may be subject to special rules, are advised to consult their own tax advisors regarding the Federal tax consequences of owning and disposing of the 2004B Bonds.

Prospective owners of the 2004B Bonds should be aware that the ownership of such obligations may result in collateral Federal income tax consequences to various categories of persons, such as corporations (including S corporations and foreign corporations), financial institutions, property and casualty and life insurance companies, individual recipients of Social Security and railroad retirement benefits, individuals otherwise eligible for the earned income tax credit, and taxpayers deemed to have incurred or continued indebtedness to purchase or carry obligations the interest on which is not included in gross income for Federal income tax purposes. Interest on the 2004B Bonds may be taken into account in determining the tax liability of foreign corporations subject to the branch profits tax imposed by Section 884 of the Code.

#### **Possible Government Action**

Legislation affecting municipal bonds is regularly under consideration by the United States Congress. In addition, the Internal Revenue Service has established an expanded audit program for tax-exempt bonds. There can be no assurance that legislation enacted or proposed or an audit initiated by the Internal Revenue Service involving either the 2004B Bonds or other tax-exempt bonds will not have an adverse effect on the tax-exempt status or market price of the 2004B Bonds.

### **LEGALITY OF BONDS FOR INVESTMENT**

Under the Act, the State and all of its public officers, municipal corporations, political subdivisions, and public bodies, all banks, bankers, trust companies, savings banks and institutions, including savings and loan associations, all investment companies, insurance companies, insurance associations, and other persons carrying on an insurance business in the State and all personal representatives, guardians, trustees and other fiduciaries in the State may legally invest any moneys or funds belonging to them or within their control and available for investment under other provisions of law, in any bonds or other obligations issued by the Corporation, and the 2004B Bonds and other obligations of the Corporation shall be authorized security for all public deposits and shall be fully negotiable in the State.

### **LITIGATION**

There is no litigation of any nature now pending or threatened restraining or enjoining the issuance, sale, execution or delivery of the 2004 Bonds or the application of the proceeds thereof to the refunding of the Refunded Bonds, or in any way contesting or affecting the validity of the 2004 Bonds or any proceedings of the Corporation taken with respect to the issuance or sale thereof, or the pledge or application of any revenues or other moneys or security provided for the payment of the 2004 Bonds, or the existence or powers of the Corporation.

## Office of Hawaiian Affairs and Ceded Lands

Certain developments of the Corporation, but not those constituting Projects within the Program, are located on "Ceded Lands" (as described below) which are the subject of certain litigation involving the Corporation. These cases, *OHA v. Housing Finance and Development Corporation* and *OHA v. Hawaii Housing Authority*, are described below. However, to provide the context in which this litigation exists, and to provide information on claims made that a portion of the revenue earned with respect to such developments is required to be transferred outside the Corporation, it is necessary to provide background relating to other litigation concerning ceded lands.

In 1898 the former Republic of Hawaii transferred certain lands to the United States. Upon Hawaii's admission to the Union in 1959, the United States reconveyed title to those lands (collectively, the "Ceded Lands") to the State of Hawaii (the "State") to be held as a public trust for five purposes: (1) public education; (2) betterment of the conditions of native Hawaiians; (3) development of farm and home ownership; (4) making public improvements; and (5) provision of land for public use. In 1978, the State Constitution was amended expressly to provide that the Ceded Lands were to be held as a public trust for native Hawaiians and the general public, and to establish the Office of Hawaiian Affairs ("OHA") to administer and manage the proceeds and income derived from a pro rata portion of the Ceded Lands to better the conditions of native Hawaiians.

In 1979, the State legislature (the "Legislature") adopted HRS Chapter 10 ("Chapter 10"), which, as amended in 1980, specified, among other things, that OHA expend 20% of all funds derived by the State from the Ceded Lands for the betterment of native Hawaiians.

In 1987, in *Trustees of the Office of Hawaiian Affairs v. Yamasaki*, 69 Haw. 154 (1987) ("*Yamasaki*"), the Hawaii Supreme Court concluded that Chapter 10 was insufficiently clear regarding the amount of monies OHA was entitled to receive from the public trust lands.

In 1990, in response to *Yamasaki*, the Legislature adopted Act 304, Session Laws of Hawaii 1990, which (i) defined "public land trust" and "revenue," (ii) reiterated that 20% of the now defined "revenue" derived from the "public land trust" was to be expended by OHA for the betterment of native Hawaiians, and (iii) established a process for OHA and the Director of Finance of the State jointly to determine the amount of monies which the State would pay OHA to retroactively settle all of OHA's claims for the period June 16, 1980 through June 30, 1991. Since fiscal year 1992 and until the first quarter of fiscal year 2002, the State, through its departments and agencies, paid 20% of "revenues" to OHA on a quarterly basis.

In 1993, the Legislature enacted Act 35, Session Laws of Hawaii 1993, appropriating \$136.5 million to pay the amount determined to be OHA's claims, with interest, for the period June 16, 1980 through June 30, 1991.

On January 14, 1994, OHA and its Board of Trustees (the "Plaintiffs") filed suit against the State (*OHA, et al. v. State of Hawaii, et al.*, Civil No. 94-0205-01 (1st Cir.) ("*OHA I*")), claiming that the amount paid to OHA was inadequate and alleging that the State had failed to properly account for and fully pay the pro rata share of proceeds and income derived from the public land trust. Among other things, the Plaintiffs sought an accounting of all proceeds and income, funds and revenue derived from the public land trust since 1978, and restitution or damages amounting to 20% of the proceeds and income derived from the public land trust, as well as interest thereon. In its answer to OHA's complaint, the State denied all of the Plaintiffs' substantive allegations, and asserted its sovereign immunity from suit and other jurisdictional and claim-barring defenses.

The Plaintiffs thereafter filed four motions for partial summary judgment as to the State's liability to pay OHA 20% of monies it receives from (i) the Department of Transportation Airports Division's in-bound duty free airport concession (including receipts from the concessionaire's off-airport sales operations), (ii) the State-owned and operated Hilo Hospital, (iii) the State's public rental housing projects and affordable housing developments, and (iv) interest income, including investment earnings (collectively, the "Sources"). In response, the State filed a motion to dismiss on the basis of sovereign immunity and opposed Plaintiffs' four motions on the merits and raised several affirmative defenses.

On October 24, 1996, the circuit court filed an order denying the State's motion to dismiss and rejecting its affirmative defenses. Also on October 24, 1996, the circuit court filed an order granting Plaintiffs' four motions for partial summary judgment with respect to the State's liability to pay OHA 20% of the monies it receives from each of the Sources, and deferred establishing amounts owed from those Sources for further proceedings or trial. The State's motion for leave to file an interlocutory appeal from both the order denying its motion to dismiss and the order granting

Plaintiffs' four partial summary judgments was granted and all proceedings in the suit were stayed pending the Hawaii Supreme Court's disposition of the State's appeal.

On September 12, 2001, the Hawaii Supreme Court concluded *OHA I* by holding in *OHA v. State of Hawaii*, 96 Haw. 388 (2001) that Act 304 was effectively repealed by its own terms, and that there was no judicially manageable standard, i.e., a legal standard, by which to determine whether OHA was entitled to the revenues it sought from the Sources because the repeal of Act 304 revived the law which the court in *Yamasaki* had previously concluded was insufficiently clear to establish how much OHA was entitled to receive from the Ceded Lands. The Supreme Court dismissed *OHA I* for lack of justiciability, that is, that the case was not appropriate for review by the Court, noting that it was up to the Legislature to enact legislation to give effect to the right of native Hawaiians to benefit from the Ceded Lands under the State Constitution. Immediately thereafter, agencies ceased paying OHA any receipts from the Ceded Lands.

The Legislature took no action during the 2002, 2003 and 2004 legislative sessions to establish a new mechanism for establishing how much OHA was entitled to receive from the Ceded Lands. On January 10, 2003, and pending legislative action to establish such a mechanism, the Governor issued Executive Order No. 03-03 directing state agencies to resume transferring 20% of receipts from leases, licenses and permits indisputably paid for the use of improved or unimproved parcels of Ceded Lands to OHA, if federal or state law did not preclude all or any portion of the receipt from being used to better the conditions of native Hawaiians, and the transfer of all or any portion of the receipt to OHA would not cause the agency to renege on a preexisting pledge, rate covenant, or other preexisting obligation to holders of revenue bonds or other indebtedness of the State or the agency. During the 2003 legislative session, the Legislature appropriated moneys from the various funds into which the Ceded Lands receipts had been deposited after the decision in *OHA I* was issued and agencies ceased making payments to OHA, and directed the agencies to pay them to OHA.

OHA continues to pursue its claims for a portion of the revenues from the Sources and other Ceded Lands that it made in *OHA I*. On July 21, 2003, OHA filed a new lawsuit, *OHA et al. v. State of Hawaii, et al.*, Civil No. 03-1-1505-07 ("*OHA II*"). There follows additional background information pertinent to *OHA II*. In September 1996, the Office of the Inspector General of the U.S. Department of Transportation ("DOT") issued a report (the "IG Report") concluding that from 1992 to 1995, the Hawaii Department of Transportation's payment to OHA of \$28.2 million was a diversion of airport revenues in violation of applicable federal law as OHA provided no airport services in return. The Attorney General of Hawaii disagreed with the IG Report's conclusion, stating in November 1996 that the payments to OHA were simply an operating cost of the airports, and thus not a diversion of airport revenues in violation of federal law. In April 1997, the Acting Administrator of the FAA concurred in writing (the "FAA Memorandum") with the IG Report and opposed the Hawaii Attorney General's position. In support of its appeal of the circuit court's *OHA I* decision to the Hawaii Supreme Court, but differing with the original position of the Attorney General, the State noted in its May 1997 amended opening brief that "unless the federal government's position [set forth in the IG Report] changes, Act 304 prohibits the State from paying OHA airport-related revenues." In its June, 1997, reply brief, the State stated that the "DOT Inspector General's determination shows that the federal government is on its way to finding such payments illegal and requiring the State to reimburse past payments of airport-related revenues to OHA." In October, 1997 the Department of Transportation and Related Agencies Appropriation Act, 1998, PL 105-66, 1997 HR 2169 (the "DOT Appropriation Act") was enacted into federal law. Section 340 of the DOT Appropriation Act ("Section 340") essentially provides that in exchange for there being no further payments of airport revenues for claims related to Ceded Lands, any such payments received prior to April 1, 1996 need not be repaid. The Hawaii Attorney General submitted the enactment of Section 340 to the Hawaii Supreme Court in December 1997, "for the Court's use" in conjunction with the *OHA I* appeal, whereupon the Court requested the parties to submit supplemental briefs to address whether Section 340 affected the Court's interpretation of Act 304. The State, in its March 1998 supplemental brief, stated, *inter alia*, that paying OHA a pro rata share of airport monies violated federal law, and that there was no live, ripe controversy regarding those payments because Section 340 relieved the State and OHA of any obligation to return improper past payments.

Despite the adverse *OHA I* decision, the Plaintiffs in *OHA II* sued the State for alleged breaches of fiduciary duties as purported trustee of the Ceded Lands public trust, alleging violations of Act 304, Chapter 10, and Article XII, Sections 4, 5 and 6 of the Hawaii Constitution, violations of the Contract Clause of the U.S. Constitution, and misrepresentation and non-disclosure, by the following alleged acts (but not limited to these acts): (1) failing to oppose the positions set forth in the FAA Memorandum; (2) resolving its dispute with the FAA by obtaining a forgiveness of the prior \$28.2 million payment in exchange for a promise not to make future airport revenue payments to OHA and not to appeal the positions set forth in the FAA Memorandum; (3) breaching the trust duty of impartiality by not opposing the

positions set forth in the FAA Memorandum in order to use them as a sword in *OHA I*, (4) failing to timely advise OHA that the State was not going to continue to oppose the positions set forth in the FAA Memorandum or IG Report, and that it was planning to settle with the federal government, in order to provide OHA with a fair opportunity to take measures to step into the State's position to oppose the FAA; and (5) failing to obtain instructions from the Court on how to proceed given the State's conflict between defending the State against OHA in *OHA I*, and having a duty to oppose the positions set forth in the FAA Memorandum.

OHA further asserted that these alleged "breaches, errors and omissions" were substantial factors that resulted in the passing of the Section 340 and the issuance of the Hawaii Supreme Court's opinion in *OHA I*. Plaintiffs claimed that, accordingly, the State is liable to OHA for damages including, but not limited to: (1) the damages alleged by OHA in *OHA I*, and (2) amounts payable under Act 304 that have not been paid, including but not limited to, airport landing fees. Plaintiffs also sought declaratory and injunctive relief ordering the State to reinstate Act 304, pay airport-related revenues to OHA from sources other than airport revenues (and enjoining the State and its agents, employees, and officials from opposing any of the above), and sought appointment of an independent trustee to temporarily replace the State as trustee of the native Hawaiian public trust with respect to matters relating to reinstatement of Act 304 and the payment of airport-related revenues to OHA from sources other than airport revenues. The State filed a motion to dismiss OHA's complaint in *OHA II* which the court granted in an order filed on December 26, 2003. The Court entered a final judgment on May 19, 2004, encompassing the order dismissing the complaint and several procedural orders. On June 8, 2004, OHA filed a notice of appeal from the portions of the May 19, 2004, judgment dismissing its complaint in *OHA II*, denying leave to amend the complaint and denying a request for bifurcation of OHA's claims for liability and damages. On June 9, 2004, the State of Hawaii filed a notice of cross appeal from two discovery rulings set forth in the judgment.

The State intends to vigorously defend against all of OHA's claims. It is currently unable to predict with reasonable certainty the magnitude of its potential liability for such claims, if any. The Attorney General is of the view that the claims asserted by OHA in *OHA II* are meritless. Resolution of all of OHA's claims could have a material adverse effect on the State's financial condition.

#### Actions Related To Ceded Lands Specifically Involving The Corporation

In a second lawsuit, OHA and four individuals filed complaints for declaratory and injunctive relief on November 4, 1994, and November 9, 1994 (*OHA v. Housing Finance and Development Corporation et al.*, Civil No. 94-4207-11 (1st Cir.)) to enjoin the State from alienating any Ceded Lands and extinguishing any rights Hawaiians may have in Ceded Lands that may be alienated. Alternatively, OHA sought a declaration that the amounts the Housing Finance and Development Corporation (now the Corporation) and the State paid to OHA for Ceded Lands the Corporation planned to use to develop and sell housing units pursuant to Act 318, 1992 Session Laws of Hawaii, were insufficient. Act 318 established a separate process for valuing the Ceded Lands the Corporation used for its two housing developments at Kealakehe and Lahaina, and quantifying the amounts of income and proceeds from the Ceded Lands that the Corporation and State were required to pay to OHA for conveying and using the parcels for the Corporation's two projects.

In December, 2002, following a trial on the issues, the trial court confirmed the State's authority to sell Ceded Lands, denied the declaratory ruling that the sale of Ceded Lands did not directly or indirectly release or limit Hawaiians' claims to those lands which the plaintiffs requested, and ordered that judgment be entered in the State's and Corporation's favor as to Counts I, II, and III of the Amended Complaint. The plaintiffs moved for and were granted leave to file immediate appeals from the court's rulings to the Hawaii Supreme Court. Those appeals are now pending. Trial to determine the sufficiency of the proceeds paid to OHA by the Corporation and the State from the sale of the particular parcels of Ceded Lands at issue has not been scheduled.

In a third lawsuit, OHA filed suit against the Hawaii Housing Authority (the "HHA" and now the Corporation), the executive director of the HHA, the board members of the HHA and the Director of Finance on July 27, 1995 (*OHA v. HHA, et al.*, Civil No. 95-2682-07 (1st Cir.)) to secure additional compensation and an itemized accounting of the sums previously paid to OHA for five specifically identified parcels of Ceded Lands which were transferred to the HHA for its use to develop, construct and manage additional affordable public rental housing units under HRS Chapter 201G. On January 11, 2000, all proceedings in this suit were stayed pending the Hawaii Supreme Court's decision in the State's appeal in *OHA I*. OHA disagrees that the repeal and revival of the pre-*Yamasaki* law by the Hawaii Supreme Court's September 12, 2001 decision in *OHA I* should also require dismissal of the claims OHA makes in *OHA v. HHA*, and the case remains pending.

## **CERTAIN LEGAL MATTERS**

All legal matters incident to the authorization, issuance and delivery of the 2004B Bonds are subject to the approval of Hawkins Delafield & Wood LLP, New York, New York, Bond Counsel. The form of the opinion Bond Counsel proposes to render is set forth in Appendix A hereto. Copies of the approving opinion of Bond Counsel will be available at the time of delivery of the 2004B Bonds. 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, Watanabe Ing Kawashima & Komeiji LLP, Honolulu, Hawaii.

## **RATING**

Moody's Investors Service (Moody's") is expected to assign a rating of "Aaa" to the 2004B Bonds based on the issuance of the Policy by the Insurer. Such rating reflects only the views of such organization. Any explanation of the significance of the rating given by Moody's may only be obtained from such rating agency. There is no assurance that such rating will continue for any given period of time or that it will not be revised downward or withdrawn entirely by such rating agency if, in its judgment, circumstances so warrant. Any such downward revision or withdrawal of such rating may have an adverse effect on the market price of the 2004B Bonds.

## **UNDERWRITING**

The 2004B Bonds are being purchased by UBS Financial Services Inc. (the "Underwriter") at an aggregate price of \$22,835,325.56. The Contract of Purchase provides that the Underwriter will purchase all the 2004B Bonds if any of the 2004 Bonds are purchased, and that the obligations to make such purchases are subject to certain terms and conditions set forth in the Contract of Purchase for the 2004B Bonds, including issuance of the 2004A Bonds, the approval of certain legal matters by counsel and certain other conditions.

## **CAUTIONARY STATEMENTS REGARDING FORWARD-LOOKING STATEMENTS IN THIS OFFICIAL STATEMENT**

Certain statements included or incorporated by reference in this Official Statement constitute "forward-looking statements." Such statements are generally identifiable by the terminology used such as "plan," "expect," "estimate," "budget" or similar words.

The achievement of certain results or other expectations contained in such forward looking statements involve known and unknown risks, uncertainties and other factors which may cause actual results, performances or achievements described to be materially different from any future results, performances or achievements expressed or implied by such forward looking statements. The Corporation does not plan to issue any updates or revisions to those forward looking statements if and when changes to its expectations, or events, conditions or circumstances on which such statements are based, occur, unless such updates or revisions are made in the course of fulfilling its continuing disclosure obligation.

## **FINANCIAL STATEMENTS**

The combined financial statements of the Corporation referenced above and the financial statements of RHSP and of SHARP, included, respectively, as Appendices B and C to this Official Statement, are in each case for the year ended June 30, 2003, and have been audited by independent certified public accountants, to the extent and for the period indicated in their reports thereon.

The audited financial statements of the Corporation and the Program for future years will be available upon request from the Corporation.

## MISCELLANEOUS

Any statements made in this Official Statement involving matters of opinion or estimates, whether or not expressly so stated, are set forth as such and not as representations of fact, and no representations are made that any of the estimates will be realized.

The references to the Indenture and other documents referred to herein are brief summaries of certain provisions thereof. Such summaries do not purport to be complete and reference is made to such documents for full and complete statements of such provisions.

The execution and delivery of this Official Statement has been duly authorized by the Corporation.

HOUSING AND COMMUNITY DEVELOPMENT  
CORPORATION OF HAWAII

By /s/ Darren Ueki  
Darren Ueki, Acting Executive Director

**(THIS PAGE INTENTIONALLY LEFT BLANK)**

FORM OF OPINION OF BOND COUNSEL

[Date Of Closing]

Housing and Community Development  
Corporation of Hawaii  
677 Queen Street, Suite 300  
Honolulu, Hawaii 96813

Dear Board of Directors:

HOUSING AND COMMUNITY DEVELOPMENT CORPORATION OF HAWAII  
HAWAII RENTAL HOUSING SYSTEM REVENUE BONDS,  
2004 REFUNDING SERIES B,  
\$23,000,000

As bond counsel to the Corporation hereafter mentioned, we have examined into the validity of \$23,000,000 Hawaii Rental Housing System Revenue Bonds, 2004 Refunding Series B (the "Bonds"), of the Housing and Community Development Corporation of Hawaii (the "Corporation"). The Bonds are in fully registered form without coupons, are dated their date of delivery, are issuable in the denomination of \$25,000 or any integral multiple thereof during the Auction Rate Period (as defined in the First Supplemental Trust Indenture hereinafter mentioned) and in the denomination of \$5,000 or any integral multiple thereof during the Fixed Rate Period (as defined in the First Supplemental Trust Indenture), bear interest initially at an Auction Rate (as such term is defined in the First Supplemental Trust Indenture), are subject to change to Fixed Rate at the option of the Corporation, are payable as to interest on the dates established in accordance with the First Supplemental Trust Indenture and mature on July 1, 2033.

The Bonds are subject to redemption and mandatory tender prior to their stated maturity thereof upon the terms and conditions set forth therein. The Bonds are transferable and exchangeable upon the terms and conditions set forth therein.

The Bonds recite that they are issued under the authority of and in full compliance with the Constitution and statutes of the State of Hawaii, including particularly Part III of Chapter 39, and Chapter 201G, Hawaii Revised Statutes (collectively, the "Act"), under and pursuant to a resolution of the Board of Directors of the Corporation, duly adopted on September 16, 2004, and under and pursuant to a Trust Indenture by and between the Corporation and U.S. Bank National Association, as trustee thereunder, (the "Trustee"), dated as of October 1, 2004, as supplemented by the First Supplemental Trust Indenture, also dated as of October 1, 2004 (collectively, the "Indenture"), and that the Bonds are part of an issue of bonds issued, or to be issued, under the Indenture as supplemented from time to time, unlimited as to amount except as provided in the Indenture or as may be provided by law.

We have examined the Constitution and statutes of the State of Hawaii, a duplicate executed copy of the Indenture, certified copies of proceedings of the Corporation authorizing the issuance of the Bonds and the execution and delivery of the Indenture, such other records and documents as we have considered necessary or appropriate for the purposes of this opinion and a specimen Bond.

In our opinion:

1. The Bonds have been duly authorized and issued in accordance with the Constitution and statutes of the State of Hawaii and constitute valid general obligations of the Corporation, payable from and secured by a lien upon and pledge of the Net Revenues (as defined in the Indenture) and other funds and assets pledged under the Indenture and also payable out of any of the Corporation's legally available funds, revenues and assets, subject to the terms of the Indenture.

2. The Indenture has been duly authorized, executed and delivered by the Corporation and, assuming the due authorization, execution and delivery thereof by the Trustee, constitutes a valid instrument of the Corporation in accordance with the terms thereof, and the Bonds are entitled to the security and benefits of the Indenture for the payment thereof in accordance with the terms thereof, equally and ratably with any bonds heretofore or hereafter issued under the Indenture in accordance with the terms thereof, except as otherwise expressly provided in the Indenture.

3. Under existing statutes and court decisions and assuming continuing compliance with certain tax covenants (i) interest on the Bonds is excluded from gross income for Federal income tax purposes pursuant to Section 103 of the Internal Revenue Code of 1986, as amended (the "Code") and (ii) interest on the Bonds is not treated as a preference item in calculating the alternative minimum tax imposed on individuals and corporations under the Code; such interest, however, is included in the adjusted current earnings of certain corporations for purposes of calculating the alternative minimum tax imposed on such corporations. In rendering this opinion, we have relied on certain representations, certifications of fact, and statements of reasonable expectations made by the Corporation in connection with the Bonds, and assumed compliance by the Corporation with certain ongoing covenants to comply with applicable requirements of the Code to assure the exclusion of interest on the Bonds from gross income under Section 103 of the Code.

4. Under existing laws of the State of Hawaii, the Bonds and the income therefrom are exempt from taxation by the State or any county or other political subdivision thereof, except inheritance, transfer and estate taxes and except to the extent such income may be included in the measure of franchise taxes imposed on banks and other financial institutions pursuant to the laws of the State of Hawaii.

We express no opinion regarding any other Federal or state tax consequences with respect to the Bonds. We render our opinion under existing statutes and court decisions as of the issue date, and we assume no obligation to update our opinion after the issue date to reflect any future action, fact or circumstance, or change in law or interpretation, or otherwise. We express no opinion on the effect of any action hereafter taken or not taken in reliance upon an opinion of other counsel on the exclusion from gross income for Federal income tax purposes of interest on the Bonds, or under state and local tax law.

It is to be understood that the rights of the holders of the Bonds under the Bonds and under the Indenture and the enforceability thereof may be subject to the valid exercise of judicial discretion, the sovereign police powers of the State of Hawaii and the constitutional powers of the United States of America, and to valid bankruptcy, insolvency, reorganization, moratorium and other laws affecting creditors' rights.

Very truly yours,

**APPENDIX B**

**AUDITED FINANCIAL STATEMENTS OF THE (PRIOR) RENTAL HOUSING SYSTEM PROGRAM  
(RHSP)**

**(THIS PAGE INTENTIONALLY LEFT BLANK)**

**Grant Thornton** 

Financial statements and report of independent certified public accountants

**State of Hawaii, Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund**

June 30, 2003 and 2002

## CONTENTS

	Page
REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS	3
FINANCIAL STATEMENTS	
STATEMENTS OF NET ASSETS	4
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS	5
STATEMENTS OF CASH FLOWS	6
NOTES TO FINANCIAL STATEMENTS	8

**(THIS PAGE INTENTIONALLY LEFT BLANK)**

Report of Independent Certified Public Accountants

Board of Directors  
State of Hawaii  
Housing and Community Development Corporation of Hawaii

We have audited the accompanying statements of net assets of the State of Hawaii, Housing and Community Development Corporation of Hawaii Rental Housing System Revenue Bond Fund as of June 30, 2003 and 2002, and the related statements of revenues, expenses and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. 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 audits provide a reasonable basis for our opinion.

As described in note A2, the financial statements present only the Rental Housing System Revenue Bond Fund and do not purport to, and do not, present fairly the financial position of the State of Hawaii, Housing and Community Development Corporation of Hawaii as of June 30, 2003 and 2002, and the results of its operations and its cash flows for the years 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 financial position of the State of Hawaii, Housing and Community Development Corporation of Hawaii Rental Housing System Revenue Bond Fund as of June 30, 2003 and 2002, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The State of Hawaii, Housing and Community Development Corporation of Hawaii Rental Housing System Revenue Bond Fund has not presented Management's Discussion and Analysis that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be part of, the basic financial statements.

Honolulu, Hawaii  
November 3, 2003



State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

STATEMENTS OF NET ASSETS

June 30,

ASSETS	<u>2003</u>	<u>2002</u>
<b>CURRENT ASSETS</b>		
Cash in banks (notes A4 and B)	\$ 1,203,665	\$ 1,104,348
Accrued interest receivable	10,439	20,587
Tenant receivable, net of allowance of \$1,144,209 in 2003 and \$1,055,800 in 2002	727,509	595,361
Other receivable	473,260	458,450
Prepaid expenses and other assets	14,254	14,357
Deferred bond issuance costs (note A6)	<u>60,933</u>	<u>62,230</u>
Total current assets	2,490,060	2,255,333
<b>ASSETS HELD BY TRUSTEE UNDER REVENUE BOND PROGRAMS (notes A4, A5 and C)</b>		
Cash	11,310	72,913
Money market funds	19,237,221	18,025,113
U.S. government securities	<u>8,783,839</u>	<u>8,768,026</u>
	28,032,370	26,866,052
<b>DEFERRED BOND ISSUANCE COSTS, net of current portion (note A6)</b>	653,521	714,455
<b>PROPERTY AND EQUIPMENT, net (notes A8, D, E and F)</b>	<u>56,321,621</u>	<u>59,622,925</u>
<b>TOTAL ASSETS</b>	<u><u>\$87,497,572</u></u>	<u><u>\$89,458,765</u></u>
<b>LIABILITIES AND NET ASSETS</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 528,202	\$ 524,226
Accrued expenses		
Interest	499,200	503,397
Other	37,686	32,027
Due to other funds	45,932	43,553
Security deposits	603,929	582,075
Revenue bonds payable (note E)	<u>1,455,000</u>	<u>1,335,000</u>
Total current liabilities	3,169,949	3,020,278
ARBITRAGE REBATE PAYABLE (note E)	23,456	23,456
REVENUE BONDS PAYABLE, net of current portion (note E)	90,285,000	91,740,000
COMMITMENTS AND CONTINGENCIES (note G)	-	-
<b>NET ASSETS</b>		
Invested in capital assets, net of related debt	(34,703,925)	(32,675,390)
Unrestricted	<u>28,723,092</u>	<u>27,350,421</u>
	<u>(5,980,833)</u>	<u>(5,324,969)</u>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<u><u>\$87,497,572</u></u>	<u><u>\$89,458,765</u></u>

The accompanying notes are an integral part of these statements.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

Year ended June 30,

	<u>2003</u>	<u>2002</u>
Operating revenues		
Rental (notes E and F)	\$ 9,547,730	\$ 9,073,899
Other	427,848	396,185
	<hr/>	<hr/>
Total operating revenues	9,975,578	9,470,084
Operating expenses		
Depreciation	3,313,463	3,331,881
Project	3,533,485	3,407,766
Personal services	125,339	112,131
Provision (recovery) for losses	88,409	(70,337)
Administration	22,122	34,000
Professional services	22,626	14,710
Insurance	1,017	10,335
Repairs and maintenance	4,808	4,242
Utilities	938	1,771
Security	86	65
Capital expenditures	112,700	80,947
Other	7,500	8,774
	<hr/>	<hr/>
Total operating expenses	7,232,493	6,936,285
Operating income	2,743,085	2,533,799
Nonoperating revenues (expenses)		
Interest income	294,738	529,971
Other	41,120	61,563
Interest expense	(3,125,437)	(3,138,786)
Letter of credit fees	(371,171)	(375,007)
Trustee fees	(175,689)	(177,105)
Amortization of deferred bond issuance costs	(62,231)	(63,452)
Loss on disposal of property and equipment	(279)	(1,386)
	<hr/>	<hr/>
Total nonoperating expenses	(3,398,949)	(3,164,202)
CHANGE IN NET ASSETS	(655,864)	(630,403)
Total net assets at beginning of year	<u>(5,324,969)</u>	<u>(4,694,566)</u>
Total net assets at end of year	<u><u>\$ (5,980,833)</u></u>	<u><u>\$ (5,324,969)</u></u>

The accompanying notes are an integral part of these statements.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

STATEMENTS OF CASH FLOWS

Year ended June 30,

	2003	2002
Cash flows from operating activities:		
Cash received from renters	\$ 9,349,027	\$ 9,050,688
Cash payments to suppliers	(4,242,404)	(3,997,724)
Cash receipts from other funds	2,379	24,904
Other receipts	454,158	594,168
Cash payments to employees	(125,339)	(112,131)
	5,437,821	5,559,905
Net cash provided by operating activities		
Cash flows from capital and related financing activities:		
Principal paid on revenue bond maturities and redemptions	(1,335,000)	(1,215,000)
Interest paid on revenue bonds	(3,129,634)	(3,169,567)
Acquisition of property and equipment	(12,438)	-
	(4,477,072)	(4,384,567)
Net cash used in capital and related financing activities		
Cash flows from investing activities:		
Purchases of U.S. government securities	(35,323,650)	(35,406,097)
Proceeds from matured U.S. government securities	35,307,837	35,372,958
Interest received on investments	304,886	556,163
	289,073	523,024
Net cash provided by investing activities		
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,249,822	1,698,362
Cash and cash equivalents at beginning of year	19,202,374	17,504,012
Cash and cash equivalents at end of year	\$ 20,452,196	\$ 19,202,374
Reconciliation of cash to cash and cash equivalents		
Cash	\$ 1,214,975	\$ 1,177,261
Money market funds	19,237,221	18,025,113
Cash and cash equivalents at end of year	\$ 20,452,196	\$ 19,202,374

The accompanying notes are an integral part of these statements.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

STATEMENTS OF CASH FLOWS (continued)

Year ended June 30,

	2003	2002
Cash flows from operating activities:		
Operating income	\$ 2,743,085	\$ 2,533,799
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	3,313,463	3,331,881
Provision (recovery) for losses	88,409	(70,337)
Changes in:		
Tenant receivables	(220,557)	(50,538)
Other receivable	26,310	197,983
Prepaid expenses and other assets	103	133
Accounts payable	(542,884)	(444,516)
Accrued expenses - other	5,659	9,269
Due to other funds	2,379	24,904
Security deposits	21,854	27,327
	\$ 5,437,821	\$ 5,559,905

The accompanying notes are an integral part of these statements.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS

June 30, 2003 and 2002

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting policies consistently applied in the preparation of the accompanying financial statements follows.

1. Organization

Section 201E-57 of the Hawaii Revised Statutes, provided for the creation of special funds to account for housing projects or systems of housing projects financed from the proceeds of bonds secured under the same trust indenture. Accordingly, the Rental Housing System Revenue Bond Fund (Fund) was created on December 30, 1987, to account for various multifamily rental housing projects. For administrative purposes the Fund was placed within the Housing Finance and Development Corporation (HFDC). The Fund has completed four projects: La'ilani located in Kona, Hawaii, was completed during the year ended June 30, 1989; Honokowai located in Lahaina, Maui, was completed during the year ended June 30, 1991; Kamakee Vista, located in Honolulu, Oahu, was completed during the year ended June 30, 1992; and Pohulani, located in Honolulu, Oahu, was completed during the year ended June 30, 1993.

In accordance with Act 350, Session Laws of Hawaii 1997, effective July 1, 1998, the functions and employees of HFDC (as well as those of the Hawaii Housing Authority (Authority) and the Rental Housing Trust Fund) were transferred to the newly created Housing and Community Development Corporation of Hawaii (Corporation) and HFDC ceased to exist. The Corporation is a public body and a body corporate and politic and is, for administrative purposes only, considered to be a part of the State Department of Business, Economic Development and Tourism. In accordance with Act 92, Session Laws of Hawaii, 2003, effective July 1, 2003, administratively, the functions and employees of the Corporation were transferred to the State Department of Human Services.

2. Financial Statement Presentation

The Fund is a component of the Corporation. The Fund's financial statements are intended to present the financial position, results of operations and cash flows of only that portion of the funds of the Corporation that is attributable to the transactions of the Fund. They do not purport to, and do not, present fairly the financial position of the Corporation as of June 30, 2003 and 2002, and the changes in its financial position and cash flows, where applicable, for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements of the Fund have been prepared in conformity with accounting principles generally accepted in the United States of America prescribed by the

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2. Financial Statement Presentation (continued)

Governmental Accounting Standards Board (GASB). In June 1999, the GASB issued Statement 34, Basic Financial Statements – Management’s Discussion and Analysis – for State and Local Governments. This Statement establishes new financial reporting requirements for state and local governments in the United States of America. They require new information and restructure much of the information that governments have presented in the past. Comparability with reports issued in prior years is affected. The Corporation, and therefore the Fund, implemented these standards for the fiscal year ended June 30, 2002.

The adoption of GASB 34 did not have any significant effect to beginning net assets balance. Other GASB Statements are required to be implemented in conjunction with Statement 34. Therefore, the Fund implemented the following GASB Statements for the fiscal year June 30, 2002: Statement 36, Recipient Reporting for Certain Shared Nonexchange Revenues, Statement 37, Basic Financial Statements – Management’s Discussion and Analysis – for State and Local Governments: Omnibus and Statement 38, Certain Financial Statement Note Disclosures.

3. Measurement Focus and Basis of Accounting

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

Proprietary funds have the option under GASB 24, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting, to elect to apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless FASB conflicts with GASB. Management has elected to not apply FASB statements after the applicable date.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services or goods in connection with a proprietary fund’s principal ongoing operations. Revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses. The principal operating revenues of the Fund are rental revenues from the multifamily housing projects.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3. Measurement Focus and Basis of Accounting (continued)

Net assets are restricted when constraints placed on them are either externally imposed or imposed by constitutional provisions or enabling legislation, provided that the purpose is narrower than that of the Fund. Internally imposed designations of resources are not presented as restricted net assets. When both restricted and unrestricted resources are available for use, generally, it is management's policy to use restricted resources first, then unrestricted resources as they are needed.

4. Cash and Cash Equivalents

Cash and cash equivalents for the purpose of the statements of cash flows include all cash and investments with original purchased maturities of three months or less.

5. Investments

Investments in U.S. government securities and money market accounts that have a maturity at time of purchase of one year or less, are stated at cost. All other investments are carried at fair value.

6. Amortization

Issuance costs of revenue bonds are amortized ratably over the term of the bond principal outstanding.

7. Allocated Costs

The Corporation provides certain administrative services to the Fund. The cost of these services is allocated to the Fund based on estimates of the Corporation.

8. Property and Equipment

Property and equipment are recorded at cost. Depreciation is provided over the estimated useful lives of the assets using the straight-line method. The estimated useful lives are as follows:

Buildings	27 years
Equipment	3 – 10 years

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

9. Use of Estimates

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America (US GAAP), management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the 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.

NOTE B – CASH IN BANKS

Bank balances were \$1,214,823 and \$1,107,565 as of June 30, 2003 and 2002, which were entirely covered by collateral held by the pledging banks' agents in the Corporation's name.

NOTE C – ASSETS HELD BY TRUSTEE

Statutes authorize the Fund to invest in certificates of deposit, money market funds, U. S. government or agency obligations and repurchase agreements. These investments and any available cash are required under the trust indenture dated December 1, 1987 between the Corporation and U. S. Bank Trust, N. A., trustee for the bondholders, and under the eight supplemental trust indentures entered into subsequently (collectively referred to as the "Indenture") to be held by the trustee in various accounts and funds, including a security deposit account. The use of these assets is restricted by the terms of the above Indenture.

Cash, certificates of deposit and money market funds not covered by federal deposit insurance must be fully collateralized by government securities held in the name of the Fund by third-party custodians.

Investments can be categorized to give an indication of the level of risk assumed by the Fund. Category 1 includes investments that are insured or registered, or for which the securities are held by the Corporation or its agent in the Corporation's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the Corporation's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent, but not in the Corporation's name. All cash and investments are included in the Category 2 level of risk at June 30, 2003 and 2002.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE C – ASSETS HELD BY TRUSTEE (continued)

The Fund's investments as of June 30, 2003 and 2002 are shown below.

	2003		2002	
	Reported amount	Fair value	Reported amount	Fair value
Money market funds	\$19,237,221	\$19,237,221	\$18,025,113	\$18,025,113
U.S. government securities	8,783,839	8,784,143	8,768,026	8,767,600
Total investments	<u>\$28,021,060</u>	<u>\$28,021,364</u>	<u>\$26,793,139</u>	<u>\$26,792,713</u>

NOTE D – PROPERTY AND EQUIPMENT

Capital asset activity for the year ended June 30, 2003 was as follows:

	Beginning balance	Increases	Decreases	Ending balance
Capital assets, not being depreciated				
Land	\$ 5,163,516	\$ -	\$ -	\$ 5,163,516
Capital assets, being depreciated				
Buildings and improvements	88,608,504	-	-	88,608,504
Equipment	973,192	12,438	13,996	971,634
	<u>89,581,696</u>	<u>12,438</u>	<u>13,996</u>	<u>89,580,138</u>
Accumulated depreciation				
Buildings and improvements	34,225,256	3,281,796	-	37,507,052
Equipment	897,031	31,667	13,717	914,981
	<u>35,122,287</u>	<u>3,313,463</u>	<u>(13,717)</u>	<u>38,422,033</u>
Capital assets, net	<u>\$59,622,925</u>	<u>\$(3,301,025)</u>	<u>\$ (279)</u>	<u>\$56,321,621</u>

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE D – PROPERTY AND EQUIPMENT (continued)

Capital asset activity for the year ended June 30, 2002 was as follows:

	Beginning balance	Increases	Decreases	Ending balance
Capital assets, not being depreciated				
Land	\$ 5,163,516	\$ –	\$ –	\$ 5,163,516
Capital assets, being depreciated				
Buildings and improvements	88,608,504	–	–	88,608,504
Equipment	993,564	–	20,372	973,192
	<u>89,602,068</u>	<u>–</u>	<u>20,372</u>	<u>89,581,696</u>
Accumulated depreciation				
Buildings and improvements	30,943,460	3,281,796	–	34,225,256
Equipment	865,932	50,085	18,986	897,031
	<u>31,809,392</u>	<u>3,331,881</u>	<u>18,986</u>	<u>35,122,287</u>
Capital assets, net	<u>\$62,956,192</u>	<u>\$(3,331,881)</u>	<u>\$ 1,386</u>	<u>\$59,622,925</u>

The amount of land on the statements of net assets at June 30, 2003 and 2002 is comprised mainly of \$300,000 paid for the La'ilani project, and approximately \$4,800,000 for the Pohulani project. The 11.8 acres of land for the Honokowai project were purchased from the State Department of Land and Natural Resources for \$1. The land for the Kamakee Vista project is being leased from an outside party. The land for the Pohulani project was contributed by the State Hawaii Community Development Authority (HCDA) during the year ended June 30, 1993 (note F).

NOTE E – REVENUE BONDS PAYABLE

The provisions of Act 216, SLH 1987; Act 390, SLH 1988; Act 316, SLH 1989; Act 299, SLH 1990; and Act 172, SLH 1991, together, as amended, authorized the issuance of up to \$375,000,000 of revenue bonds. Through June 30, 2003, \$114,825,000 of revenue bonds have been issued under the Fund, \$17,680,000 under the University of Hawaii Faculty Housing Program Revenue Bond Fund, and \$37,720,000 under the State of Hawaii Affordable Rental Program. The Rental Housing System revenue bonds, issued to purchase various multifamily rental housing projects, are payable solely from and secured solely by the revenues, property and equipment of those four projects. They are also guaranteed by letters of credit drawn on The Industrial Bank of Japan, Ltd., BNP Paribas and available monies in the Corporation's Dwelling Unit Revolving Fund (DURF).

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE E – REVENUE BONDS PAYABLE (continued)

Revenue bonds payable consist of the following issues:

	June 30,	
	2003	2002
1989 Series A bonds (Honokowai Kauhale project) maturing annually through 2025 (variable rate in accordance with the terms of the Indenture, 1.03% at June 30, 2003)	\$14,600,000	\$14,900,000
1990 Series A bonds (Kamakee Vista project) maturing annually through 2026 (variable rate in accordance with the terms of the Indenture, 3.78% at June 30, 2003)	32,100,000	32,400,000
1990 Series B bonds (Pohulani project) maturing annually through 2026 (variable rate in accordance with the terms of the Indenture, 3.78% at June 30, 2003)	34,300,000	34,600,000
1993 Series A bonds (La'ilani project):		
Serial bonds maturing annually through 2006 (4.00% to 5.20%)	1,180,000	1,615,000
Term bonds maturing annually from 2006 through 2019 (5.60%)	9,560,000	9,560,000
	91,740,000	93,075,000
Less current maturities	1,455,000	1,335,000
	\$90,285,000	\$91,740,000

Revenue bonds activity during the year was as follows:

	2003	2002
Balance at beginning of year	\$93,075,000	\$94,290,000
Reductions	(1,335,000)	(1,215,000)
Balance at end of year	\$91,740,000	\$93,075,000

Under the trust indenture agreement between the Corporation and the trustee for the Rental Housing System revenue bonds, the Corporation is required to provide net revenues (as defined in the trust indenture agreement) together with lawfully available funds of at least 1.25 times the aggregate debt service (as defined in the trust indenture agreement) on outstanding bonds during

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE E – REVENUE BONDS PAYABLE (continued)

the bond year. Additionally, the Corporation is to provide net revenues (as defined in the trust indenture agreement) of at least 1.10 times the aggregate debt service on outstanding bonds during the bond year. At June 30, 2003 and 2002, the Fund provided net revenues (as defined in the trust indenture agreement) together with lawfully available funds of 6.72 and 6.65 times the aggregate debt service on outstanding bonds during the respective years, and net revenues (as defined in the trust indenture agreement) of 1.34 and 1.35 times the aggregate debt service on outstanding bonds during the respective years. As per the trust indenture agreement, the Fund may use unrestricted assets of the Corporation's other funds to calculate the ratio of net revenues and lawfully available funds to the aggregate debt service on outstanding bonds during the year.

Interest on the Fund's three series of bonds is currently payable monthly at variable rates that are determined weekly in accordance with the terms of the Indenture. Interest is convertible to a fixed rate payable semi-annually upon satisfying certain terms of the Indenture.

The bonds may be redeemed early, at face value, at the option of either the bondholders or the Corporation during the variable interest rate period. Subsequent to the variable interest rate period, the bonds may be redeemed early at the option of the Corporation, subject to a redemption premium that declines from 2% to zero. There were no early redemptions during the years ended June 30, 2003 and 2002.

The annual debt service requirements through 2008 and in five-year increments thereafter to maturity of revenue bonds are as follows:

	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Year ending June 30:			
2004	\$ 1,455,000	\$ 3,236,000	\$ 4,691,000
2005	1,675,000	3,179,000	4,854,000
2006	2,105,000	3,111,000	5,216,000
2007	2,430,000	3,028,000	5,458,000
2008	2,660,000	2,933,000	5,593,000
2009-2013	16,315,000	12,987,000	29,302,000
2014-2018	21,890,000	9,461,000	31,351,000
2019-2023	25,310,000	5,216,000	30,526,000
2024-2027	17,900,000	935,000	18,835,000
	<u>\$91,740,000</u>	<u>\$44,086,000</u>	<u>\$135,826,000</u>

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE E – REVENUE BONDS PAYABLE (continued)

In order to ensure the exclusion of interest on the Fund's revenue bonds from gross income for federal income tax purposes, the Fund calculates rebates due to the U.S. Treasury annually. The rebates are calculated by bond series based on the amount by which the cumulative amount of investment income exceeds the amount that would have been earned had funds been invested at the bond yield. The Corporation determined that there were \$23,456 of calculated rebates due to the U.S. Treasury at June 30, 2003 and 2002.

NOTE F – RELATED PARTY TRANSACTIONS

The Pohulani project (Project) is an elderly housing project developed by the Corporation and the Hawaii Community Development Authority (HCDA). The Project is located at Kakaako, Honolulu, Hawaii, and consists of two distinct phases; a 262-unit rental residential phase and a commercial phase. The commercial phase occupies approximately 41,000 square feet; 40,000 square feet of office space and a 1,000 square foot retail space. The office space is occupied by State agencies, including the State Department of Accounting and General Services (DAGS), who incurred approximately \$914,000 and \$881,000 in lease rent to the Fund for the years ended June 30, 2003 and 2002, respectively. The term of the lease is from September 1992 through August 2022. The minimum annual rent is determined by multiplying the previous year's minimum annual rent by one hundred three percent (103%). The minimum annual rent for the initial year was approximately \$493,000. The retail space is occupied by a sundries store. As of June 30, 2003, the HCDA has contributed approximately \$4,882,000 to the Fund for its portion of development costs associated with the Project.

The Corporation's Rental Assistance Fund provides rent subsidies to lessees of the Corporation's various projects. The Fund has reported those subsidies, which approximate \$955,000 and \$963,000 for the years ended June 30, 2003 and 2002, respectively, as rental income in the statements of revenues, expenses and changes in net assets. In addition, the Corporation's Section 8 Fund provides rental assistance payments to lessees of the Corporation's various projects. The Fund has reported subsidies from the Section 8 Programs, which totaled approximately \$219,400 and \$213,800 for the years ended June 30, 2003 and 2002, respectively, as rental income in the statements of revenues, expenses and changes in net assets.

The Corporation also relocated its offices to the Pohulani building in September 1992. During the years ended June 30, 2003 and 2002, the Fund charged the Corporation approximately \$855,000 and \$836,000, respectively, in lease rent.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
Rental Housing System Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE G – COMMITMENTS AND CONTINGENCIES

The Corporation leases the land for the Kamakee Vista project from HCDA under a cancelable lease (residential portion) and a noncancelable lease (commercial portion), both expiring December 31, 2056. Lease rent for the years ended June 30, 2003 and 2002 totaled approximately \$426,000 and \$415,000, respectively.

The net future minimum rent payments for this operating lease at June 30, 2003 are as follows:

	<u>Residential</u>	<u>Commercial</u>	<u>Total</u>
Year ending June 30,			
2004	\$ 1	\$ 362,000	\$ 362,001
2005	1	372,000	372,001
2006	1	384,000	384,001
2007	1	395,000	395,001
2008	1	407,000	407,001
2009 – 2013	5	2,225,000	2,225,005
2014 – 2018	5	2,580,000	2,580,005
2019 – 2023	5	2,954,000	2,954,005
2024 – 2028	5	3,214,000	3,214,005
2029 – 2033	5	3,639,000	3,639,005
2034 – 2038	5	3,857,000	3,857,005
2039 – 2043	5	4,367,000	4,367,005
2044 – 2048	5	4,629,000	4,629,005
2049 – 2053	5	5,240,000	5,240,005
2054 – 2056	3	3,668,000	3,668,003
	<u>\$53</u>	<u>\$ 38,293,000</u>	<u>\$38,293,053</u>

**(THIS PAGE INTENTIONALLY LEFT BLANK)**

**APPENDIX C**

**AUDITED FINANCIAL STATEMENTS OF THE STATE OF HAWAII  
AFFORDABLE RENTAL HOUSING PROGRAM  
(SHARP)**

**(THIS PAGE INTENTIONALLY LEFT BLANK)**

**Grant Thornton** 

Financial statements and report of independent certified public accountants

**State of Hawaii, Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revenue Bond Fund**

June 30, 2003 and 2002

## CONTENTS

	Page
REPORT OF INDEPENDENT CERTIFIED PUBLIC ACCOUNTANTS	3
FINANCIAL STATEMENTS	
STATEMENTS OF NET ASSETS	4
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS	5
STATEMENTS OF CASH FLOWS	6
NOTES TO FINANCIAL STATEMENTS	8

**(THIS PAGE INTENTIONALLY LEFT BLANK)**

Report of Independent Certified Public Accountants

Board of Directors  
State of Hawaii  
Housing and Community Development Corporation of Hawaii

We have audited the accompanying statements of net assets of the State of Hawaii, Housing and Community Development Corporation of Hawaii State of Hawaii Affordable Rental Program Revenue Bond Fund as of June 30, 2003 and 2002, and the related statements of revenues, expenses and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audits.

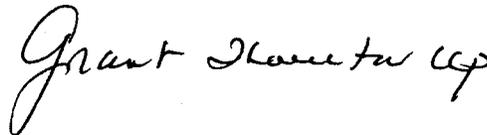
We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. 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 audits provide a reasonable basis for our opinion.

As discussed in note A2, the financial statements present only the State of Hawaii Affordable Rental Program Revenue Bond Fund and do not purport to, and do not, present fairly the financial position of the State of Hawaii, Housing and Community Development Corporation of Hawaii as of June 30, 2003 and 2002, and the results of its operations and its cash flows for the years 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 financial position of the State of Hawaii, Housing and Community Development Corporation of Hawaii State of Hawaii Affordable Rental Program Revenue Bond Fund as of June 30, 2003 and 2002, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The State of Hawaii, Housing and Community Development Corporation of Hawaii State of Hawaii Affordable Rental Program Revenue Bond Fund has not presented Management's Discussion and Analysis that the Governmental Accounting Standards Board has determined is necessary to supplement, although not required to be part of, the basic financial statements.

Honolulu, Hawaii  
November 3, 2003



State of Hawaii  
Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revenue Bond Fund

STATEMENTS OF NET ASSETS

June 30,

ASSETS	<u>2003</u>	<u>2002</u>
<b>CURRENT ASSETS</b>		
Cash in banks (notes A4 and B)	\$ 527,809	\$ 538,726
Accrued interest receivable	16,953	24,209
Tenant receivable, net of allowance of \$153,424 and \$113,422 in 2003 and 2002, respectively	14,907	53,698
Other receivable	148,795	155,261
Prepaid expenses and other assets	4,237	4,026
Deferred bond issuance costs (note A6)	<u>25,886</u>	<u>26,054</u>
Total current assets	738,587	801,974
<b>ASSETS HELD BY TRUSTEE UNDER REVENUE BOND PROGRAMS (notes A4, A5 and C)</b>		
Money market funds	16,494,610	15,316,976
Repurchase agreements	<u>3,018,000</u>	<u>3,018,000</u>
	19,512,610	18,334,976
DEFERRED BOND ISSUANCE COSTS, net of current portion (note A6)	408,069	433,956
PROPERTY AND EQUIPMENT, net (notes A7, D and F)	<u>38,900,014</u>	<u>40,463,537</u>
<b>TOTAL ASSETS</b>	<u><u>\$59,559,280</u></u>	<u><u>\$60,034,443</u></u>
<b>LIABILITIES AND NET ASSETS</b>		
<b>CURRENT LIABILITIES</b>		
Accounts payable	\$ 111,461	\$ 153,342
Accrued expenses		
Interest	236,133	242,947
Other	19,494	17,150
Due to other funds	21,494	1,684
Security deposits	260,784	259,119
Revenue bonds payable (note E)	<u>250,000</u>	<u>245,000</u>
Total current liabilities	899,366	919,242
ARBITRAGE REBATE PAYABLE (note E)	1,694	180,300
NOTE PAYABLE (note E)	3,500,000	3,500,000
REVENUE BONDS PAYABLE, net of current portion (note E)	36,840,000	37,090,000
<b>NET ASSETS</b>		
Invested in capital assets, net of related debt	(1,256,031)	88,547
Unrestricted	<u>19,574,251</u>	<u>18,256,354</u>
	18,318,220	18,344,901
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<u><u>\$59,559,280</u></u>	<u><u>\$60,034,443</u></u>

The accompanying notes are an integral part of these statements.

Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revenue Bond Fund

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

Year ended June 30,

	2003	2002
Operating revenues		
Rental (note F)	\$ 3,522,574	\$ 3,391,837
Other	164,682	180,196
	3,687,256	3,572,033
Operating expenses		
Project	1,048,530	1,017,251
Depreciation	1,563,387	1,563,594
Professional services	17,193	14,876
Personal services	53,001	66,186
Provision for losses	40,002	1,921
Administration	24,962	20,259
Security	31	45
Repairs and maintenance	3,382	2,615
Utilities	441	1,374
Insurance	497	5,851
Capital expenditures	15,568	30,892
Other	94,535	49,946
	2,861,529	2,774,810
Total operating expenses		
Operating income	825,727	797,223
Nonoperating revenues (expenses)		
Interest income	214,315	381,925
Other	17,227	18,848
Interest expense (note E)	(840,556)	(1,020,773)
Letter of credit fees	(154,843)	(155,759)
Trustee fees	(62,360)	(56,924)
Amortization of deferred bond issuance costs	(26,055)	(26,218)
Loss on disposal of property and equipment	(136)	(289)
	(852,408)	(859,190)
Total nonoperating expenses		
CHANGE IN NET ASSETS	(26,681)	(61,967)
Total net assets at beginning of year	18,344,901	18,406,868
Total net assets at end of year	\$ 18,318,220	\$ 18,344,901

The accompanying notes are an integral part of these statements.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revolving Bond Fund

STATEMENTS OF CASH FLOWS

Year ended June 30,

	2003	2002
Cash flows from operating activities:		
Cash received from renters	\$ 3,523,028	\$ 3,377,179
Cash payments to employees	(53,001)	(66,186)
Cash payments to suppliers	(1,462,090)	(1,308,793)
Cash receipts (payments) to other funds	19,810	(11,919)
Other receipts	188,375	214,240
	2,216,122	2,204,521
Cash flows from capital and related financing activities:		
Principal paid on revenue bond redemptions	(245,000)	(100,000)
Interest paid on revenue bonds	(847,370)	(1,060,461)
Arbitrage rebate liability paid	(178,606)	-
	(1,270,976)	(1,160,461)
Cash flows from investing activities:		
Proceeds from matured U.S. government securities	-	6,883
Interest received on investments	221,571	416,721
	221,571	423,604
NET INCREASE IN CASH AND CASH EQUIVALENTS	1,166,717	1,467,664
Cash and cash equivalents at beginning of year	15,855,702	14,388,038
Cash and cash equivalents at end of year	\$17,022,419	\$15,855,702
Reconciliation of cash to cash and cash equivalents		
Cash	\$ 527,809	\$ 538,726
Money market funds	16,494,610	15,316,976
Cash and cash equivalents at end of year	\$17,022,419	\$15,855,702

The accompanying notes are an integral part of these statements.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revenue Bond Fund

STATEMENTS OF CASH FLOWS (continued)

Year ended June 30,

	2003	2002
Cash flows from operating activities:		
Operating income	\$ 825,727	\$ 797,223
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation and amortization	1,563,387	1,563,594
Provision for losses	40,002	1,921
Changes in:		
Prepaid expenses and other assets	(211)	404
Other receivable	23,693	34,044
Tenant receivable	(1,211)	(36,468)
Accounts payable	(259,084)	(163,569)
Other accrued expenses	2,344	(2,519)
Due to other funds	19,810	(11,919)
Security deposits	1,665	21,810
	\$ 2,216,122	\$ 2,204,521

The accompanying notes are an integral part of these statements.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS

June 30, 2003 and 2002

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A summary of the significant accounting policies consistently applied in the preparation of the accompanying financial statements follows.

1. Organization

Section 201E-57 of the Hawaii Revised Statutes, provided for the creation of special funds to account for housing projects or systems of housing projects financed from the proceeds of bonds secured under the same trust indenture. Accordingly, the State of Hawaii Affordable Rental Housing Program Revenue Bond Fund (SHARP) was created on March 16, 1993, to account for various multifamily rental housing projects. For administration purposes SHARP was placed within the Housing Finance and Development Corporation (HFDC). SHARP has two projects. The Kauhale Kakaako project was developed by the Dwelling Unit Revolving Fund (DURF) and upon completion in December 1993 was transferred from DURF to SHARP. The Kekuilani Courts Rental Housing Project was purchased by SHARP in 1996.

In accordance with Act 350, Session Laws of Hawaii, 1997, effective July 1, 1998, the functions and employees of HFDC (as well as those of the Hawaii Housing Authority (Authority) and the Rental Housing Trust Fund) were transferred to the newly created Housing and Community Development Corporation of Hawaii (Corporation) and HFDC ceased to exist. The Corporation is a public body and a body corporate and politic and is, for administrative purposes only, considered to be a part of the State Department of Business, Economic Development and Tourism. In accordance with Act 92, Session Laws of Hawaii, 2003, effective July 1, 2003, administratively, the functions and employees of the Corporation were transferred to the State Department of Human Services.

2. Financial Statement Presentation

SHARP is a component of the Corporation. SHARP's financial statements are intended to present the financial position, results of operations and cash flows of only that portion of the funds of the Corporation that is attributable to the transactions of SHARP. They do not purport to, and do not, present fairly the financial position of the Corporation as of June 30, 2003 and 2002, and the changes in its financial position and cash flows, where applicable, for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements of SHARP have been prepared in conformity with accounting principles generally accepted in the United States of America prescribed by the Governmental Accounting Standards Board (GASB). In June 1999, the GASB issued Statement 34, Basic Financial Statements – Management's Discussion and Analysis – for State and Local

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

2. Financial Statement Presentation (continued)

Governments. This Statement establishes new financial reporting requirements for state and local governments in the United States of America. They require new information and restructure much of the information that governments have presented in the past. Comparability with reports issued in prior years is affected. The Corporation, and therefore SHARP, implemented these standards for the fiscal year ended June 30, 2002.

The adoption of GASB 34 did not have any significant effect to beginning net assets balance. Other GASB Statements were required to be implemented in conjunction with Statement 34. Therefore, the Fund implemented the following GASB Statements for the fiscal year ended June 30, 2002: Statement 36, Recipient Reporting for Certain Shared Nonexchange Revenues, Statement 37, Basic Financial Statements – Management’s Discussion and Analysis – for State and Local Governments: Omnibus and Statement 38, Certain Financial Statement Note Disclosures.

3. Measurement Focus and Basis of Accounting

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

Proprietary funds have the option under GASB 24, Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that Use Proprietary Fund Accounting, to elect to apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless FASB conflicts with GASB. Management has elected to not apply FASB statements after the applicable date.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services or goods in connection with a proprietary fund’s principal ongoing operations. Revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses. The principal operating revenues of SHARP are rental revenues from its multifamily housing projects.

Net assets are restricted when constraints placed on them are either externally imposed or imposed by constitutional provisions or enabling legislation, provided that the purpose is narrower than that

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

3. Measurement Focus and Basis of Accounting (continued)

of the Fund. Internally imposed designations of resources are not presented as restricted net assets. When both restricted and unrestricted resources are available for use, generally, it is management's policy to use restricted resources first, then unrestricted resources as they are needed.

4. Cash and Cash Equivalents

Cash and cash equivalents for the purpose of the statements of cash flows include all cash and investments with original purchased maturities of three months or less.

5. Investments

Investments in U.S. government securities are generally carried at fair value. Investments in U. S. government securities and money market investments that have a remaining maturity at time of purchase of one year or less are stated at amortized cost. Non-participating repurchase agreements are reported at cost.

6. Amortization

Issuance costs of revenue bonds are amortized ratably over the term of the bond principal outstanding.

7. Property and Equipment

Property and equipment are recorded at cost. Depreciation is provided over the estimated useful lives of the assets using the straight-line method. The estimated useful lives are as follows:

Buildings and improvements	27 years
Equipment	5 – 10 years

8. Allocated Costs

The Corporation provides certain administrative services to the SHARP. The cost of these services is allocated to the SHARP based on estimates of the Corporation.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

9. Use of Estimates

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America (US GAAP), management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the 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.

NOTE B – CASH IN BANKS

Bank balances were \$527,796 and \$538,713 as of June 30, 2003 and 2002, which were entirely covered by collateral held by the pledging banks' agents in the Corporation's name.

NOTE C – ASSETS HELD BY TRUSTEE

Statutes authorize the SHARP to invest in certificates of deposit, money market funds, U.S. Government or agency obligations and repurchase agreements. These investments and any available cash are required under the trust indenture dated February 1, 1993 between the Corporation and BNY Western Trust Company, trustee for the bondholders, and under the first supplemental trust indenture entered into subsequently (collectively referred to as the "Indenture") to be held by the trustee in various accounts and funds, including a security deposit account. The use of these assets is restricted by the terms of the above Indenture.

Cash, certificates of deposit and money market accounts not covered by federal deposit insurance must be fully collateralized by government securities held in the name of the SHARP by third-party custodians. Repurchase agreements are generally treated as collateralized lending. The underlying securities for repurchase agreements must be similarly held and are required to be U.S. Government or agency obligations with market values equal to or greater than the related agreements' carrying amounts. The SHARP monitors market values of these securities and obtains additional collateral when appropriate. The repurchase agreement matures on July 1, 2027. At June 30, 2003, the market values of the underlying securities approximated carrying amounts.

Investments can be categorized to give an indication of the level of risk assumed by the SHARP. Category 1 includes investments that are insured or registered, or for which the securities are held by the Corporation or its agent in the SHARP's name, or, for repurchase agreements, collateralized by underlying securities that are so held. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the Corporation's name.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE C – ASSETS HELD BY TRUSTEE (continued)

Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by the trust department or agent, but not in the Corporation's name. All cash and investments are included in the Category 2 level of risk at June 30, 2003 and 2002.

The fair value of investments at June 30, 2003 and 2002 approximated reported amounts.

NOTE D – PROPERTY AND EQUIPMENT

Capital asset activity for the year ended June 30, 2003 was as follows:

	Beginning balance	Increases	Decreases	Ending balance
Capital assets, not being depreciated				
Land	\$11,023,334	\$ -	\$ -	\$11,023,334
Capital assets, being depreciated				
Buildings and improvements	40,510,770	-	-	40,510,770
Equipment	640,558	-	1,088	639,470
	<u>41,151,328</u>	<u>-</u>	<u>1,088</u>	<u>41,150,240</u>
Accumulated depreciation				
Buildings and improvements	11,217,742	1,500,399	-	12,718,141
Equipment	493,383	62,988	952	555,419
	<u>11,711,125</u>	<u>1,563,387</u>	<u>952</u>	<u>13,273,560</u>
Capital assets, net	<u>\$40,463,537</u>	<u>\$(1,563,387)</u>	<u>\$(136)</u>	<u>\$38,900,014</u>

Capital asset activity for the year ended June 30, 2002 was as follows:

	Beginning balance	Increases	Decreases	Ending balance
Capital assets, not being depreciated				
Land	\$11,023,334	\$ -	\$ -	\$11,023,334
Capital assets, being depreciated				
Buildings and improvements	40,510,770	-	-	40,510,770
Equipment	641,548	-	990	640,558
	<u>41,152,318</u>	<u>-</u>	<u>990</u>	<u>41,151,328</u>
Accumulated depreciation				
Buildings and improvements	9,717,253	1,500,838	349	11,217,742
Equipment	430,979	62,756	352	493,383
	<u>10,148,232</u>	<u>1,563,594</u>	<u>701</u>	<u>11,711,125</u>
Capital assets, net	<u>\$42,027,420</u>	<u>\$(1,563,594)</u>	<u>\$289</u>	<u>\$40,463,537</u>

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE D – PROPERTY AND EQUIPMENT (continued)

Property and equipment consisted of the following at June 30:

	2003	2002
Buildings and improvements	\$ 40,510,770	\$ 40,510,770
Equipment	639,470	640,558
	41,150,240	41,151,328
Accumulated depreciation	(13,273,560)	(11,711,125)
	27,876,680	29,440,203
Land	11,023,334	11,023,334
	\$ 38,900,014	\$ 40,463,537

NOTE E – REVENUE BONDS AND NOTES PAYABLE

Revenue Bonds

The provisions of Act 216, SLH 1987; Act 390, SLH 1988; Act 316, SLH 1989; Act 299, SLH 1990; and Act 172, SLH 1991, together, as amended, authorized the issuance of up to \$375,000,000 of revenue bonds. Through June 30, 2003, \$114,825,000 of revenue bonds have been issued under the Rental Housing System Revenue Bond Fund, \$17,680,000 under the University of Hawaii Faculty Housing Program Revenue Bond Fund and \$37,720,000 under the SHARP. The State of Hawaii Affordable Rental Program revenue bonds are payable from and secured by the revenues, property and equipment of the two projects. The 1993 Series bonds are further secured by a Credit Facility with a bank.

Revenue bonds payable consist of the following issues:

	2003	2002
1993 Series A bonds (Kauhale Kakaako project) maturing annually through 2028 at variable rates in accordance with the terms of the Indenture (1.15% at June 30, 2003).	\$30,300,000	\$30,500,000
1995 Series A bonds (Kekuilani Courts Rental Housing project):		
Term bonds maturing annually from 2003 through 2031 (6.00%, 6.05% and 6.10%).	6,790,000	6,835,000
	37,090,000	37,335,000
Less current portion	250,000	245,000
	\$36,840,000	\$37,090,000

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE E – REVENUE BONDS AND NOTES PAYABLE (continued)

Revenue Bonds (continued)

Revenue bonds activity during the year was as follows:

	2003	2002
Balance at beginning of year	\$37,335,000	\$37,435,000
Reductions	(245,000)	(100,000)
Balance at end of year	\$37,090,000	\$37,335,000

Under the trust indenture agreement between the Corporation and the trustee for the SHARP revenue bonds, the Corporation is required to provide net revenues (as defined in the trust indenture agreement) together with lawfully available funds of at least 1.25 times the aggregate debt service on outstanding bonds during the year. Additionally, the Corporation is to provide net revenues (as defined in the trust indenture agreement) of at least 1.10 times the aggregate debt service on outstanding bonds during the year. At June 30, 2003 and 2002, the SHARP provided net revenues (as defined in the trust indenture agreement) together with lawfully available funds of 18.81 and 17.00 times the aggregate debt service on outstanding bonds during the respective years, and net revenues (as defined in the trust indenture agreement) of 2.20 times the aggregate debt service on outstanding bonds during 2003 and 2002.

Interest on the 1993 Series A bonds is currently payable monthly at variable rates that are determined weekly in accordance with the terms of the Indenture. Interest on the 1993 Series A bonds is convertible to a fixed rate payable semi-annually upon satisfying certain terms of the Indenture. Interest on the 1995 Series A bonds is payable semi-annually.

The 1993 Series A revenue bonds may be redeemed early, at face value, at the option of either the bondholders or the Corporation during the variable interest rate period. Subsequent to the variable interest rate period for the 1993 Series A revenue bonds and commencing in 2005 for the 1995 Series A revenue bonds, the bonds may be redeemed early at the option of the Corporation, subject to a redemption premium that declines from 2% to zero. There were no early redemptions during the years ended June 30, 2003 and 2002.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE E – REVENUE BONDS AND NOTES PAYABLE (continued)

Revenue Bonds (continued)

The annual debt service requirements through 2008 and in five-year increments thereafter to maturity are as follows:

Year ending June 30:	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2004	\$ 250,000	\$ 757,000	\$ 1,007,000
2005	355,000	751,000	1,106,000
2006	365,000	744,000	1,109,000
2007	470,000	736,000	1,206,000
2008	500,000	727,000	1,227,000
2009-2013	4,205,000	3,421,000	7,626,000
2014-2018	6,670,000	2,891,000	9,561,000
2019-2023	9,570,000	2,118,000	11,688,000
2024-2028	13,440,000	1,044,000	14,484,000
2029-2032	1,265,000	107,000	1,372,000
	<u>\$37,090,000</u>	<u>\$13,296,000</u>	<u>\$50,386,000</u>

In order to ensure the exclusion of interest on the SHARP's revenue bonds from gross income for federal income tax purposes, the SHARP calculates rebates due to the U.S. Treasury annually. The rebates are calculated by bond series based on the amount by which the cumulative amount of investment income exceeds the amount that would have been earned had funds been invested at the bond yield. Rebates to be paid in future years are subject to increase or decrease based on future events. The Corporation determined that there was approximately \$1,694 and \$180,300 of calculated rebates due to the U.S. Treasury at June 30, 2003 and 2002, respectively.

Note Payable

During 1996, the SHARP borrowed \$3.5 million from the State Department of Budget and Finance, Rental Housing Trust Fund (note A1) and issued approximately \$7 million of revenue bonds to purchase the Kekuilani Courts Rental Housing project from an unrelated party. The full amount of the non-interest bearing note shall become due and payable upon the earlier of June 30, 2027, or the redemption of all SHARP revenue bonds associated with the Kekuilani Courts Rental Housing project.

State of Hawaii  
Housing and Community Development Corporation of Hawaii  
State of Hawaii Affordable Rental Program Revenue Bond Fund

NOTES TO FINANCIAL STATEMENTS (continued)

June 30, 2003 and 2002

NOTE F – RELATED PARTY TRANSACTIONS

The Corporation participated in a joint development project with the State Hawaii Community Development Authority (HCDA) to develop Kauhale Kakaako, a 268-unit rental project located in Honolulu, Hawaii. The Corporation developed the project through its Dwelling Unit Revolving Fund (DURF) while the HCDA provided the site acquisition and equity financing for the project of \$19,423,000. The project was substantially completed in December 1993 at a cost of approximately \$42,800,000 and was transferred to SHARP at cost.

The Corporation's Rental Assistance Fund provides rent subsidies to lessees of the Corporation's various projects. Rent subsidies totaling approximately \$298,000 and \$302,000 were received for the years ended June 30, 2003 and 2002, respectively, and are reflected as rental income in the statements of revenues, expenses and changes in net assets. In addition, the Corporation's Section 8 Fund provides rental assistance payments to lessees of the Corporation's various projects. SHARP has reported subsidies from the Section 8 Programs, which totaled approximately \$224,000 and \$220,000 for the years ended June 30, 2003 and 2002, respectively, as rental income in the statements of revenues, expenses and changes in net assets.

## SUMMARY OF CERTAIN PROVISIONS OF THE TRUST INDENTURE

The following is a summary of certain provisions of the Trust Indenture. This summary does not purport to be comprehensive or definitive and is subject to all of the terms and provisions of the Trust Indenture, to which reference is hereby made, and, copies of which are available from the Corporation. Certain provisions of the Trust Indenture have been summarized in the sections of the Official Statement entitled "THE 2004B BONDS" and "SOURCES OF PAYMENT AND SECURITY FOR THE BONDS" and provisions related to the 2004B Bonds as Auction Rate Certificates are contained in "Appendix G – Provisions Related to 2004B Bonds (Auction Rate Certificates)."

### Certain Definitions

The following are definitions in summary form of certain terms contained in the Trust Indenture and the First Supplemental Trust Indenture and used in this Official Statement:

**Accrued Aggregate Debt Service** means, as of any date of calculation, the sum of the amounts of Debt Service that have accrued with respect to all Series of Bonds, calculating the Debt Service that has been accrued with respect to each Series of Bonds as an amount equal to the sum of (i) the interest on the Bonds of such Series that has accrued and is unpaid and that will have accrued or is estimated to accrue by the end of the then current calendar month, and (ii) that portion of the next due Principal Installment for the Bonds of such Series that would have accrued (if deemed to accrue in the manner set forth in the definition of "Debt Service" in this Summary) by the end of the then current calendar month.

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

**Authorized Officer** means the Executive Director, the Administrative Services Officer or the Finance Manager of the Corporation or any other officer or employee of the Corporation authorized by the by-laws or a resolution of the Board to perform the act or sign the document in question.

**Bondowner or Owner or Owner of Bonds**, or any similar term, means any person who shall be the registered owner of any Bond.

**Certified Interest Rate** means with respect to any Series of Variable Rate Bonds, the long-term rate of interest as certified by the Corporation at the time of issuance thereof; provided that in no event shall a Certified Interest Rate be less than 75% of the average weighted coupon rate of all Bonds (other than Variable Rate Bonds) Outstanding at the time of issuance of a Series of Variable Rate Bonds.

**Corporation** means the Housing and Community Development Corporation of Hawaii, a public body and a body corporate and politic, duly organized and existing under the laws of the State or any successor or successors thereto hereafter provided by law.

**Cost of Acquisition and Construction** means, with respect to any Program Development, the Corporation's cost properly attributable to the acquisition, construction, equipping, clearing, improving, rehabilitating, planning, development and financing thereof, and costs of preparing the same for use and occupancy, including but not limited to all costs of preparation and issuance of Bonds and related obligations; all properly chargeable initial costs of credit enhancement and liquidity facilities for Bonds; the cost of acquisition by or for the Corporation of real or personal property or any interest therein; costs of physical construction, purchasing and installing equipment, utilities, fixtures and apparatus necessary or convenient for the use and occupancy of any Program Development; costs of the Corporation incidental to such acquisition, construction, equipping, clearing, improving, rehabilitating, planning, development and financing; interest during acquisition or construction and for a period of time thereafter; the cost of any indemnity, performance, payment, maintenance and surety bonds and premiums on insurance during construction; engineering, architectural, supervisory, inspection, legal and clerical fees and expenses; costs of audits, fees and expenses of the Fiduciaries and costs of training, testing, financing,

administrative and general overhead and keeping accounts and making reports required by the Trust Indenture; amounts, if any, required by the Trust Indenture to be paid into the Acquisition and Construction Fund, to be remitted into the Acquisition and Construction Interest Account, the Debt Reserve Fund, the Renewal and Contingency Fund or any other reserve funds created under the Trust Indenture or a Supplemental Indenture upon the issuance of any Series of Bonds; payments when due (whether at the maturity of principal or the due date of interest or upon redemption) of any indebtedness of the Corporation (other than the Bonds) incurred for such Program Development, and costs required for the commencement of the use and occupancy of such Program Development; and shall include reimbursement to the Corporation for any such items of Cost of Acquisition and Construction theretofore paid by or on behalf of the Corporation, prior to the issuance of Bonds.

**Debt Reserve Requirement** means, as of the date of calculation, (i) with respect to any Series of Bonds, the amount required to be maintained in the Debt Reserve Fund with respect to such Series of Bonds in the Supplemental Indenture providing for the issuance of such Series of Bonds, and (ii) with respect to all Series of Bonds Outstanding, an amount equal to the aggregate of all Debt Reserve Requirements established in the Supplemental Indentures providing for the issuance of such Bonds.

**Debt Service** means, as of any date of calculation and with respect to any period for any Series, 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 (w) amounts on deposit in the Acquisition and Construction Interest Account in the Acquisition and Construction Fund, (x) amounts on deposit in the Debt Service Fund, (y) amounts on deposit in an Escrow Fund, or (z) any other provisions made for the payment of interest other than a Support Facility, and (ii) that portion of each Principal Installment for the Bonds of such Series that would have accrued during such period if each such Principal Installment were deemed to accrue daily 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, then from a date one year preceding the due date of such Principal Installment or from the date of issuance 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 interest rate on Variable Rate Bonds shall be determined as follows: (a) with respect to a Series of Variable Rate Bonds at the time of calculation then Outstanding, the interest rate shall be the higher of (1) the weighted average interest rate per annum borne by such issue of Variable Rate Bonds for the twelve month period then ended at the time of calculation or (2) the weighted average interest rate per annum on such issue of Variable Rate Bonds (computed on an actual day basis) for the three most recently completed calendar months and (b) with respect to Variable Rate Bonds then proposed to be issued, the interest rate shall be assumed to be the Certified Interest Rate. For all purposes of calculating the Debt Reserve Requirement under the Trust Indenture, Debt Service shall not include Debt Service on Bonds to the extent principal of and interest on such Bonds are secured by and payable from amounts on deposit in an Escrow Fund.

**Escrow Fund** means any escrow fund established pursuant to a Supplemental Indenture in connection with a Series of Bonds that serves as a repository for Proceeds of such Series of Bonds pending disbursement in accordance with the terms of such Supplemental Indenture.

**Estimated Net Revenues** means for any Fiscal Year, the Estimated Revenues for such Fiscal Year less the projected Operation and Maintenance Costs for such Fiscal Year.

**Estimated Revenues** means for any Fiscal Year, the projected Revenues for such Fiscal Year.

**Existing Program Developments** means the facilities that as of the date of the Trust Indenture are "Program Developments" for purposes of that certain Trust Indenture dated as of December 1, 1987 between the Housing Finance and Development Corporation (whose successor is the Corporation) and Peoples National Bank of Washington as trustee (whose successor as trustee is U.S. Bank National Association) and that certain Trust Indenture dated as of February 1, 1993 between the Housing Finance and Development Corporation and First Hawaiian Bank as trustee (whose successor trustee is BNY Western Trust Company), as each such Trust Indenture has been amended and supplemented.

**Fiscal Year** means a period beginning on July 1 in any year and ending on June 30 of the succeeding year or such other one year period as the Corporation shall determine and certify to the Trustee.

**Housing Consultant** means an independent consultant or firm of consultants not under the control of the Corporation recognized to be knowledgeable in housing matters relating to multi-family rental housing developments, such consultant or consultants to be selected by or on behalf of the Corporation.

**Investment Securities** means and includes any of the following securities, if and to the extent the same are at the time legal for investment of the Corporation's moneys and are not prohibited by a Rating Agency:

(i) direct obligations of or obligations guaranteed by the United States of America or obligations of any state of the United States of America or any political subdivision of such a state, assigned by a Rating Agency its highest rating and payment of which is secured by an irrevocable pledge of such obligations of the United States;

(ii) (A) bonds, debentures or other obligations issued by Student Loan Marketing Association, Federal Land Banks, Federal Intermediate Credit Banks, Banks for Cooperatives, Federal Home Loan Banks, Tennessee Valley Authority, the United States Postal Service, Federal Farm Credit System, Federal Home Loan Mortgage Corporation, Export Import Bank, World Bank, International Bank for Reconstruction and Development and Inter-American Development Bank; or (B) bonds, debentures or other obligations issued by Federal National Mortgage Association (excluding mortgage securities which are valued greater than par on the portion of unpaid principal or mortgage securities which represent payments of principal only or interest only with respect to the underlying mortgage loans);

(iii) any obligations of an agency controlled or supervised by or acting as an instrumentality of the United States Government pursuant to authority granted by the Congress of the United States;

(iv) obligations issued by public agencies or municipalities and fully secured as to the payment of both principal and interest by a pledge of annual contributions under an annual contributions contract or contracts with the United States of America, or temporary notes, preliminary loan notes or project notes issued by public agencies or municipalities and fully secured as to the payment of both principal and interest by a requisition or payment agreement with the United States of America;

(v) time deposits, certificates of deposit or any other deposit with a bank, trust company, national banking association, savings bank, federal mutual savings bank, savings and loan association, federal savings and loan association or any other institution chartered or licensed by any state or the U.S. Comptroller of the Currency to accept deposits in such state (as used herein, "deposits" shall mean obligations evidencing deposit liability which rank at least on a parity with the claims of general creditors in liquidation), which are (a) fully secured, to the extent not insured by the Federal Deposit Insurance Corporation, by any of the obligations described in (i) above having a market value (exclusive of accrued interest) not less than the uninsured amount of such deposit or (b) (1) unsecured or (2) secured to the extent, if any, required by the Corporation and made with an institution whose unsecured debt securities are rated at least the then existing ratings on the Bonds (or the highest ratings of short-term obligations if the investment is a short-term obligation) by a Rating Agency;

(vi) repurchase agreements backed by or related to obligations described in (i), (ii) or (iii) above (A) with any institution whose unsecured debt securities are rated at least the then existing ratings on the Bonds (or the highest rating of short-term obligations if the investment is a short-term obligation) by a Rating Agency or (B) with members of the Association of Primary Dealers which do not qualify under (A);

(vii) investment agreements, (A) secured or unsecured as required by the Corporation, with any institution whose debt securities are rated at least the then existing ratings on the Bonds (or the highest rating of short-term obligations if the investment is a short-term obligation) by a Rating Agency or (B) fully secured by obligations described in (i) with members of the Association of Primary Dealers who do not qualify under (A);

(viii) direct and general obligations of or obligations unconditionally guaranteed by the State, to the payment of the principal of and interest on which the full faith and credit of the State is pledged, and certificates of participation in obligations of the State including obligations the payment of which is subject to annual appropriations, if such obligations are rated at least the then existing ratings on the Bonds by a Rating Agency;

(ix) direct and general obligations of or obligations guaranteed by any state, municipality or political subdivision or agency thereof, which obligations are rated in the two highest rating categories of a Rating Agency;

(x) bonds, debentures, or other obligations issued by any bank, trust company, national banking association, insurance company, corporation, government or governmental entity (foreign or domestic), provided, that such bonds, debentures or other obligations are (a) payable in any coin or currency of the United States of America which at the time of payment will be legal tender for the payment of public and private debts, and (b) rated in the two highest rating categories of a Rating Agency;

(xi) commercial paper (having original maturities of not more than 270 days) rated in the highest category of a Rating Agency;

(xii) money market funds which invest in obligations described in clause (i) and which funds have been rated in the two highest rating categories by a Rating Agency; or

(xiii) any investments authorized in a Supplemental Indenture authorizing Bonds rated by a Rating Agency.

provided, that it is expressly understood that the definition of Investment Securities shall be, and be deemed to be, expanded, or new definitions and related provisions shall be added to the Trust Indenture by a Supplemental Indenture, thus permitting investments with different characteristics from those permitted which the Board deems from time to time to be in the interests of the Corporation to include as Investment Securities if at the time of inclusion such inclusion will not, in and of itself, impair, or cause the Bonds to fail to retain, the then existing ratings assigned to them by the Rating Agencies.

For purposes of this definition, "institution" means an individual, partnership, corporation, trust or unincorporated organization, or a government or agency, instrumentality, program, account, fund, political subdivision or corporation thereof.

**Operation and Maintenance Costs** means all actual operation and maintenance costs of the Program incurred by the Corporation in any particular Fiscal Year or period to which said term is applicable or charges made therefor during such Fiscal Year or period, including amounts reasonably required to be set aside as reserves for items of Operation and Maintenance Costs to the extent such amounts have not been previously spent for actual operation and maintenance costs of the Program.

Such Operation and Maintenance Costs include, but are not limited to, expenses for ordinary repairs, renewals and replacements of the Program, portions of salaries and wages, employees' health, hospitalization, pension and retirement expenses, fees for services, materials and supplies, rents, administrative and general expenses, insurance expenses, legal, architectural, engineering, accounting and financial advisory fees and expenses and costs of other consulting and technical services of the Corporation which are properly allocable and chargeable to the Program as provided in the annual budget of the Corporation and in accordance with generally accepted accounting principles and are not funded from proceeds of Bonds, taxes, payments in lieu of taxes and other governmental charges and any other current expenses or obligations required to be paid by the Corporation under the provisions of the Trust Indenture or by law, all to the extent properly allocable to the Program, and the fees and expenses of the Fiduciaries.

Such Operation and Maintenance Costs do not include depreciation or obsolescence charges or reserves therefor, amortization of intangibles or other bookkeeping entries of a similar nature, interest charges and

charges for the payment of principal, or amortization, of bonded or other indebtedness of the Corporation, costs, or charges made therefor, for capital additions, replacements, betterments, extensions or improvements to or retirements from the Program which under generally accepted accounting principles are properly chargeable to the capital account or the reserve for depreciation, and do not include losses from the sale, abandonment, reclassification, revaluation or other disposition of any properties of the Program nor such property items, including taxes, which are capitalized pursuant to the then existing accounting practice of the Corporation.

**Operation Date**, when used in reference to a Program Development or Program Developments being acquired, constructed, reconstructed, rehabilitated or improved by the Corporation means the date by which (i) certificates of occupancy have been issued by municipal or State officials having jurisdiction thereof and (ii) a Written Certificate of the Corporation is delivered to the Trustee certifying that such Program Development has received a certificate of occupancy from the proper governmental body and has been placed in substantial commercial operation in accordance with the prudent practice of the multi-family residential housing development industry.

**Outstanding** means, as of any date of calculation, all Bonds theretofore executed, issued and delivered by the Corporation and authenticated by the Trustee or the Authenticating Agent under the Trust Indenture except:

- (a) Bonds theretofore canceled by the Trustee or surrendered for cancellation;
- (b) Bonds in lieu of, or in exchange for which, other Bonds shall have been issued;
- (c) Bonds (or portions of Bonds) for the payment or redemption of which moneys, equal to the principal amount or Redemption Price thereof, as the case may be, with interest to the date of maturity or redemption date, shall be held in trust under the Trust Indenture and set aside for such payment or redemption (whether at or prior to the maturity or redemption date), provided that if such Bonds (or portions of Bonds) are to be redeemed, irrevocable notice of such redemption shall have been given as provided in Article IV or provision satisfactory to the Trustee shall have been made for the giving of such notice; and
- (d) Bonds deemed to have been paid or defeased as provided in the Trust Indenture.

For purposes of the Trust Indenture, in the event any Bonds 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, 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 taking of any other action that the Owners of the Bonds are entitled to take pursuant to the Trust Indenture or the determination of principal amounts payable to and the delivery of notices or requests by Bondowners upon an event of default under the Trust Indenture, shall be the accreted value thereof. The accreted value of any such Bond on any date shall be the present value thereof on the immediately preceding interest payment date (or if such date is an interest payment date, on such date) determined by computing the present worth of all payments of principal and interest remaining to be paid thereon using a discount factor equal to the yield at which such Bond was initially offered to the public. Prior to the issuance and delivery of any Bonds described in this paragraph, there shall be filed with the Trustee a certificate of the Corporation setting forth the accreted value thereof as of each interest payment date to the stated maturity date thereof, which certificate, if approved by the Trustee, shall be conclusive.

**Principal Installment** means, as of any date of calculation and with respect to any Series, 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 of any Sinking Fund Installment due on a certain future date for Bonds of such Series, plus the amount of the sinking fund redemption premiums, if any, 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 plus such applicable redemption premiums, if any, except to the extent any such Principal Installments are to be paid from amounts on deposit in an Escrow Fund.

**Program** means the system of multi-family rental housing developments owned and operated by or on behalf of the Corporation consisting of all Program Developments. "Program" shall not include any separate rental multi-family housing system established by the Corporation as permitted by the Trust Indenture or any separate multi-family rental housing development not designated as part of the Program.

**Program Development** means one or more of the facilities within the Existing Program Developments and/or any real and personal property, buildings and improvements, commercial space, lands for farming and gardening, and community facilities acquired or constructed or to be acquired or constructed, and all tangible or intangible assets held or used in connection therewith, or any one or more of the foregoing, or any combination thereof, if and to the extent that the same shall be designated by the Corporation as a Program Development to be included in the Program in a Supplemental Indenture authorizing the issuance of Bonds for such Program Development or in a certificate of the Corporation, in the case of a Program Development not financed with Bond proceeds.

**Rating Agency** means each of Fitch Ratings, Moody's Investors Service Inc. and Standard & Poor's Ratings Services, and their respective successors and assigns, in each case and at any time only if the same is maintaining a rating on the Bonds at the request of the Corporation.

**Redemption Price** means, with respect to any Bond, the principal amount thereof plus the applicable premium, if any, payable upon redemption thereof pursuant to the Trust Indenture or any Supplemental Indenture.

**Renewal and Contingency Fund Requirement** means (i) with respect to the Existing Program Developments, \$7,300,000, (ii) with respect to each additional Program Development, an amount equal to six percent (6%) of the construction cost or estimated construction cost of such Program Development as set forth in the certificate of the Corporation filed with the Trustee upon the Operation Date of such Program Development, and (iii) with respect to the Program, the aggregate of the amounts determined pursuant to clause (i) and clause (ii).

**Revenues** means (i) all revenues, income, rents, fees, charges and receipts derived by the Corporation from or attributable to the ownership and operation of the Program, including the applicable portion for any period of a federal, State or local rent subsidy payment; (ii) all interest, profits or other income derived from the investment of any moneys held pursuant to the Trust Indenture and required to be paid into the Revenue Fund; (iii) proceeds derived by the Corporation directly or indirectly from the sale, lease, or other disposition of property arising out of the Corporation's ownership of the Program which are deposited in the Revenue Fund in accordance with the provisions of the Trust Indenture; (iv) proceeds of insurance and condemnation awards arising out of the Corporation's ownership of the Program deposited in the Revenue Fund in accordance with the provisions of the Trust Indenture; and (v) any amounts specifically pledged or designated by the Corporation and deposited in the Revenue Fund as provided in a Supplemental Indenture. "Revenues" shall not include amounts on deposit in the Rebate Fund, investment earnings on any Escrow Fund except to the extent provided in a Supplemental Indenture or the proceeds of separate rental housing system obligations issued pursuant to the Trust Indenture or payments under a Support Facility except to the extent provided in a Supplemental Indenture.

**Series** means all of the Bonds designated as being of the same Series authenticated and delivered on original issuance in a simultaneous transaction, and any Bonds thereafter authenticated and delivered in lieu thereof or in substitution therefor pursuant to the Trust Indenture.

**Support Facility** means any instrument such as a letter of credit, a line of credit, insurance policy, surety bond, standby bond purchase agreement, any guaranty or similar instrument or any combination of the foregoing, and issued by a bank or banks, or other financial institution or institutions, or any combination of the foregoing, which Support Facility provides for the payment of (i) purchase price, including accrued interest, on Bonds delivered to a remarketing agent or any depository, tender agent or other party pursuant to a remarketing agreement or Supplemental Indenture and discount, if any, incurred in remarketing such Bonds, and/or (ii) principal of and interest on all Bonds becoming due and payable during the term thereof.

**Value of Investment Securities** and words of like import means the amortized value thereof, provided, however, that all United States of America, United States Treasury Obligations--State and Local

Government Series shall be valued at par and those obligations which are redeemable at the option of the holder shall be valued at the price at which such obligations are then redeemable. The computations 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 as 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.

**Pledge of the Trust Indenture; General Obligation of the Corporation (Trust Indenture, Section 5.01)**

The Bonds are obligations of the Corporation payable from and secured by the funds pledged therefor. There are pledged for the payment of the principal of, and Redemption Price and interest on, the Bonds in accordance with their terms and the provisions of the Trust Indenture, subject only to the provisions of the Trust Indenture permitting the application thereof for the purposes and on the terms and conditions set forth in the Trust Indenture: (i) the proceeds of sale of the Bonds, except proceeds of a Series on deposit in an Escrow Fund which shall be pledged as set forth in the Supplemental Indenture providing for the issuance thereof, (ii) the Net Revenues, and (iii) all funds and accounts other than the Escrow Funds or Rebate Funds established by the Trust Indenture, and the Bondowners shall have a lien on, and a security interest in, such proceeds and the Revenues and funds and accounts for such purpose and subject to such provisions of the Trust Indenture.

Subject to any agreements heretofore or hereafter made with the holders of any notes or bonds of the Corporation pledging any particular revenues or assets not pledged under the Trust Indenture or any other trust indenture, resolution or other proceedings, the Bonds shall be general obligations of the Corporation, payable from any of the legally available funds, revenues or assets of the Corporation not appropriated for or committed to any other purpose.

**Establishment and Flow of Funds (Trust Indenture, Section 5.02)**

The Trustee will hold the following Funds established pursuant to the Trust Indenture: the Acquisition and Construction Fund, Revenue Fund, Debt Service Fund, Debt Reserve Fund, Renewal and Contingency Fund, General Reserve Fund and Rebate Fund, The Trustee will also hold any Escrow Fund established pursuant to a Supplemental Indenture, as well as certain accounts within the funds mentioned in the preceding sentence.

**Acquisition and Construction Fund (Trust Indenture, Section 5.03)**

The Acquisition and Construction Fund will include a Program Development Account for each Program Development to be constructed or acquired and may include a corresponding Acquisition and Construction Interest Account. There shall be paid into the Acquisition and Construction Fund the proceeds of Bonds as required by the Trust Indenture or any Supplemental Indenture. In addition, the proceeds of insurance maintained pursuant to the Trust Indenture against physical loss or damage to the Program Development, or of contractors' performance bonds pertaining to the period of construction thereof shall be paid into the Program Development Account. The Corporation shall pay the Costs of Acquisition and Construction for the Program Development from the Program Development Account. Unless otherwise provided in the applicable Supplemental Indenture, investment earnings on the amounts deposited in the Program Development Account shall be retained in the Program Development Account and applied with other moneys on deposit in such Program Development Account to the purposes specified by the Trust Indenture.

A Supplemental Indenture may require the Corporation to deposit into an Acquisition and Construction Interest Account proceeds of the Bonds authorized thereby to pay interest on such Bonds. Investment earnings on amounts on deposit in an Acquisition and Construction Interest Account are to be retained therein until the amount deposited therein is sufficient to pay all of the interest on the applicable Series of Bonds through the estimated Operation Date of the applicable Program Development, and thereafter such investment earnings are to be

deposited in the corresponding Program Development Account. The Trustee shall transfer from each Acquisition and Construction Interest Account to the Debt Service Fund the portion of such interest payment payable from such Acquisition and Construction Interest Account. Upon receipt of the certificate of the Corporation referred to in the following paragraph, the balance, if any, in the Acquisition and Construction Interest Account is to be transferred to the corresponding Program Development Account.

The substantial completion of construction, reconstruction, rehabilitation or improvement of each Program Development or the acquisition of any Program Development financed with Bond proceeds will be evidenced by a certificate of the Corporation, filed with the Trustee, stating: (i) that the construction, reconstruction, rehabilitation or improvement of such Program Development has been completed substantially in accordance with the plans and specifications or that such Program Development has been acquired and is now owned by the Corporation; (ii) the date of such substantial completion or acquisition; (iii) the estimated Operation Date for such Program Development; (iv) an evaluation of the amount remaining in the Acquisition and Construction Interest Account available to pay the interest due on the Bonds; (v) the amounts, if any, required in the opinion of the Corporation for the payment of any remaining part of the Cost of Acquisition and Construction of such Program Development; and (vi) the construction cost or estimated construction cost of such Program Development. Amounts not required to be retained in the Acquisition and Construction Fund to pay remaining costs shall be transferred to the Debt Reserve Fund if necessary to cure any deficiency therein or the Debt Service Fund to redeem Bonds.

#### **Funds and Payments from Funds (Trust Indenture, Sections 5.04 through 5.10)**

All Revenues received by the Corporation or its agents are required to be deposited promptly by the Corporation in the Revenue Fund. All Revenues received by the Trustee shall be promptly deposited in the Revenue Fund. Amounts in the Revenue Fund are to be applied or paid to other funds established by the Trust Indenture in the following order of priority.

1. As promptly as practicable after the first day of each month, the Trustee shall apply the amount on deposit in the Revenue Fund to the payment of Operation and Maintenance Costs.

2. On each interest payment date for Bonds the Trustee shall make transfers from the Revenue Fund to the Debt Service Fund of the amount, if any, required to pay interest on and any Principal Installment of the Bonds due on such interest payment date, taking into account amounts to be transferred from any Acquisition and Construction Interest Account or Escrow Fund. The Trustee, unless otherwise provided in a Supplemental Indenture in respect of a Series of Bonds which are secured by a Support Facility, shall pay from the Debt Service Fund the Principal Installments and interest on the Bonds on the due dates therefor and the redemption price and interest on Bonds to be redeemed on the date fixed for the redemption.

Amounts accumulated in the Revenue Fund or Debt Service Fund with respect to any Sinking Fund Installment may, and, if so directed by the Corporation, shall, be applied to the purchase of Bonds to satisfy such Sinking Fund Installment, provided, however that no Bonds shall be so purchased during the interval between the date on which notice of redemption of such Bonds from Sinking Fund Installments is given and the date of redemption set forth in such notice, unless the Bonds so purchased are Bonds called for redemption in such notice,

Amounts held in the Debt Service Fund may be used to reimburse any institution providing a Support Facility for a draw on such Support Facility made to provide funds for the payment of principal and redemption price and interest on Bonds.

3. On or before each January 1 and July 1, the Trustee shall transfer to the Debt Reserve Fund the amount, if any, required so that the balance in the Debt Reserve Fund equals the Debt Reserve Requirement if amounts are not available for such purpose in the General Reserve Fund or Renewal and Contingency Fund. Any amounts required to eliminate a deficiency in the Debt Reserve Fund to the extent not remedied by transfers from the Renewal and Contingency Fund or the General Reserve Fund shall be accumulated from Revenues over a 36-month period. The failure of the Corporation to accumulate such moneys is not a default under the Trust Indenture if the Corporation presents to the Trustee and implements a plan to remedy such failure, or upon the failure of the Corporation to so act, either (i) the Housing Consultant provides such plan and the Corporation implements such plan or (ii) the Housing Consultant provides a certificate stating that the rates, rents, fees and charges necessary to

provide for such accumulation are impracticable and the Corporation establishes rates, rents, fees and charges as recommended by the Housing Consultant which will as nearly as practicable permit such accumulation. In the event no Housing Consultant is then currently serving the Corporation, the Trustee may retain a Housing Consultant at the expense of the Corporation for the sole purpose of assisting in the preparation of a plan for presentation to the Trustee.

If the moneys in the Debt Service Fund are insufficient, the Trustee shall transfer amounts from the General Reserve Fund and, to the extent amounts in the General Reserve Fund are insufficient, amounts in the Renewal and Contingency Fund. If moneys in the Debt Service Fund continue to be insufficient after such transfers, the Trustee shall transfer amounts, if any, in the Debt Reserve Fund and, if necessary, seek payment under any surety bond or insurance policy on deposit therein. Whenever the amount in the Debt Reserve Fund, together with the amount in the Debt Service Fund, is sufficient to pay in full all Outstanding Bonds in accordance with their terms, the funds on deposit in the Debt Reserve fund shall be transferred to the Debt Service Fund. Whenever moneys on deposit in the Debt Reserve Fund exceed the Debt Reserve Requirement, the excess may be transferred by the Trustee at the written direction of the Corporation to the Revenue Fund.

In the event of the issuance of a Series of Bonds, unless upon the delivery of such Bonds there shall then already be on deposit in the Debt Reserve Fund an amount equal to the total of the Debt Reserve Requirement for all Series of Bonds to be Outstanding upon the issuance of such Series, the amount of such requirement shall be deposited from Bond proceeds.

When Bonds are to be refunded in whole or in part or otherwise provided for so that such Bonds are no longer Outstanding, moneys may be withdrawn from the Debt Reserve Fund to provide for the payment of such Bonds, or may be transferred and applied to any reserve fund or account established for Bonds issued to refund such refunded Bonds; provided that immediately after such withdrawal or transfer there shall be on credit to the Debt Reserve Fund an amount equal to the Debt Reserve Requirement.

In lieu of the deposit of moneys into the Debt Reserve Fund, the Corporation may cause to be so credited a surety bond, insurance policy or letter of credit payable to the Trustee for the benefit of the Owners of Bonds or a letter of credit in an amount equal to the difference between the Debt Reserve Requirement and the amounts then on deposit in the Debt Reserve Fund and meeting other requirements set forth in the Trust Indenture.

4. On or before each January 1 and July 1, the Trustee shall transfer to the Renewal and Contingency Fund the amount necessary to be deposited therein to fund the Renewal and Contingency Fund Requirement and such additional amounts as may be budgeted by the Corporation. The amounts in the Renewal and Contingency Fund shall be used: (i) to reserve unexpended funds previously and currently budgeted for ordinary and anticipated renewals and replacements of the Program; (ii) to reserve unexpended funds previously budgeted for ordinary and anticipated Operation and Maintenance Costs; (iii) to pay the cost of extraordinary and unanticipated renewals and replacements (including those required to restore damage, loss or destruction of the Program, but only to the extent not covered by the proceeds of insurance or other moneys required to provide for the safe and efficient operation of the Program or to prevent loss of Revenues); and (iv) to the payment of extraordinary and unanticipated Operation and Maintenance Costs.

The Corporation shall calculate the Renewal and Contingency Fund Requirement for each Program Development: (i) upon the issuance of Bonds to finance such Program Development, and (ii) upon the Operation Date for such Program Development. The amount in the Renewal and Contingency Fund shall be at least equal to the Renewal and Contingency Fund Requirement for the Program; provided however, that to the extent the Renewal and Contingency Fund Requirement is being accrued from Net Revenues the amount in the Renewal and Contingency Fund must at least equal the amount required to be deposited as of such date.

Upon the issuance of a Series of Bonds the Corporation will pay into the Renewal and Contingency Fund the amount, if any, of the proceeds of the sale of such Series as specified in the Supplemental Indenture providing for the issuance of such Bonds. To the extent not theretofore funded with Bond proceeds or Revenues, the Reserve and Contingency Fund Requirement for any Program Development shall be funded from Revenues over a ten-year period after the Operation Date of the Program Development. Any deficiencies in the Renewal and Contingency Fund resulting from withdrawals therefrom to the extent not remedied from the General

Reserve Fund shall be accumulated from Net Revenues over a 36-month period. The failure of the Corporation to so accumulate such moneys is not a default under the Trust Indenture if the Corporation provides and implements a plan to remedy such failure or, upon the failure of the Corporation to so act, either (i) the Housing Consultant provides such plan and the Corporation implements such plan or (ii) the Housing Consultant provides a certificate stating that the rates, rents, fees and charges necessary to provide for such accumulation are impracticable, and the Corporation establishes rates, rents, fees and charges which will as nearly as practicable permit such accumulation.

If at any time the amount in the Debt Service Fund shall be less than the requirement of such fund or the amount in the Debt Reserve Fund shall be less than the amount required to be deposited therein and there shall not be on deposit in the General Reserve Fund sufficient moneys to cure such deficiency, then there shall be transferred from the Renewal and Contingency Fund to the Trustee for deposit in the appropriate fund the amount necessary (or all the moneys in said Renewal and Contingency Fund if less than the amount necessary) to remedy or lessen such deficiency.

Any balance of moneys and securities in the Renewal and Contingency Fund in excess of the minimum amount required or budgeted and reserved to be on deposit therein and not required to meet any such deficiencies in the Debt Service Fund or Debt Reserve Fund or needed for any of the purposes for which such funds were established, may be deposited in the General Reserve Fund or the Revenue Fund.

5. On or before each January 1 and July 1, the Trustee shall transfer to the General Reserve Fund, the balance, if any, in the Revenue Fund. The Trustee shall transfer, at any time, from the General Reserve Fund to the Debt Service Fund and the Debt Reserve Fund the amount necessary (or all the moneys in the General Reserve Fund if less than the amount necessary) to make up any deficiencies in payments to such Funds required by the Trust Indenture. Such transfer shall be made prior to the use of any moneys on deposit in the Renewal and Contingency Fund to cure such deficiencies. The General Reserve Fund is also required to be used to remedy deficiencies in the Renewal and Contingency Fund, Amounts in the General Reserve Fund not required to meet any of the foregoing deficiencies may be used for any one or more the following: (i) transfer to the Revenue Fund; (ii) transfer to the Debt Service Fund for the purchase or redemption of Bonds including any expenses in connection thereof; (iii) payments of principal or Redemption Price of or any interest on any subordinated indebtedness; (iv) payments into any Program Development Account or Accounts established in the Acquisition and Construction Fund; (v) improvements, extensions, betterments, renewals and replacements of any properties of the Program; (vi) any other purposes of the Corporation in connection with the Program, including, without limitation, payment of the costs of preliminary and development work including architectural, engineering, legal and financial studies in connection with the planning and development of Program Developments and the determination of the feasibility thereof; (vii) any purpose of a separate rental housing system or separate rental housing development of the Corporation; and (viii) any other public purpose of the Corporation, but only if the Corporation has determined pursuant to a resolution adopted by the Board of the Corporation to terminate the operation of the Program pursuant to the terms of the Trust Indenture.

#### **Rebate Fund (Trust Indenture, Section 5.11)**

If and to the extent necessary to comply with any covenant established in a Supplemental Indenture with respect to a Series of Bonds regarding maintaining the exclusion from gross income of interest on such Bonds for federal income tax purposes, the Corporation shall establish in the Supplemental Indenture with respect to a Series of Bonds an account in the Rebate Fund with respect to such Series of Bonds and shall establish terms, provisions and covenants regarding deposits or credits to and withdrawals from such account necessary in order to maintain the exclusion from gross income of interest on such Series of Bonds for federal income tax purposes.

#### **Investment of Certain Funds (Trust Indenture, Section 10.03)**

Moneys held in the Debt Service Fund and the Debt Reserve Fund shall be invested and reinvested by the Trustee, to the fullest extent practicable only in those investments defined in clauses (i), (ii) and (iii) of the definition of Investment Securities which mature not later than such times as shall be necessary to provide moneys when needed for payments to be made from the Debt Service Fund or the Debt Reserve Fund. Moneys held by the Trustee in the Revenue Fund shall be deposited with any qualified depository and invested and reinvested by the

Trustee at the direction of the Corporation in any Investment Securities which mature not later than such times as shall be necessary to provide moneys when needed for payments to be made from such fund. Moneys held by the Trustee in the Renewal and Contingency Fund shall be deposited with any qualified depository and invested and reinvested by the Trustee at the direction of the Corporation in any Investment Securities, provided moneys shall be available for the purposes specified for such Fund. Moneys held by the Trustee in the General Reserve Fund may be invested at the direction and in the sole discretion of the Corporation in Investment Securities, provided that the Corporation shall make sufficient moneys available for the purposes specified for such Fund. Net interest earned on any moneys or investments in the Revenue Fund, the Debt Service Fund, the Debt Reserve Fund, the Renewal and Contingency Fund and the General Reserve Fund, if in excess of the requirements for such Funds shall be paid into the Revenue Fund.

Amounts in the Acquisition and Construction Fund shall be invested and reinvested at the direction of the Trustee at the direction of the Corporation in Investment Securities so as to provide funds to make all required payments from such Fund. Net interest earned on any moneys or investments in the Acquisition and Construction Fund, if in excess of the requirements of such Fund may, at the option of the Corporation, be retained in such Fund or paid into the Revenue Fund.

### **Additional Bonds and Refunding Bonds (Trust Indenture, Section 2.03)**

After issuance of the 2004 Bonds, the Corporation may issue one or more Series of Additional Bonds from time to time in such principal amount as the Corporation may determine for the purpose of paying all or a portion of the Cost of Acquisition and Construction of a Program Development or repayment of moneys borrowed by the Corporation through the issuance of subordinated indebtedness for the purpose of paying all or a portion of the Cost of Acquisition and Construction of a Program Development.

Each Series of Additional Bonds shall be authenticated and delivered by or upon the direction of the Trustee only upon receipt by the Trustee of the following documents in addition to any other requirements of the Trust Indenture:

(i) An opinion of counsel to the effect that the Corporation is authorized to undertake the Program Development financed by the Additional Bonds;

(ii) If a Program Development is to be constructed, reconstructed, rehabilitated or improved by the Corporation, an Engineer's Certificate setting forth the estimated Cost of Acquisition and Construction of the Program Development, or if a Program Development is to be acquired by the Corporation, a certificate of the Corporation setting forth the estimated Cost of Acquisition and Construction of the Program Development and, in either case, a certificate of the Corporation setting forth the estimated Operation Date of such Program Development; and

(iii) A certificate of the Corporation setting forth: (a) the Debt Service for each Fiscal Year of the Bonds of such Series; or (b) the Aggregate Debt Service for all Outstanding Bonds including the Series of Bonds being issued, for each Fiscal Year, and any other statements necessary to show compliance with the, provisions of the Trust Indenture.

The Trustee must also receive the following in the case of Additional Bonds issued and delivered to pay the Cost of Acquisition and Construction of any Program Development for which Bonds have not previously been issued:

(1) An Accountant's Certificate setting forth the following: Net Revenues produced in each of the three Fiscal Years preceding the issuance of such Additional Bonds (or, if less than three Fiscal Years have elapsed from the date of the Trust Indenture until the issuance of such Additional Bonds, then for each Fiscal Year which has elapsed from the date of the Trust Indenture until the issuance of such Additional Bonds) were at least equal to 1.10 times the Aggregate Debt Service on Outstanding Bonds for each such Fiscal Year;

(2) A certificate of the Corporation setting forth the following: (i) estimated Net Revenues produced in each of the five Fiscal Years following the Operation Date of the Program Development to be financed with such Additional Bonds will be at least equal to 1.10 times the Aggregate Debt Service on Outstanding Bonds, including such Additional Bonds, for each such Fiscal Year; and (ii) a confirming certificate of the Housing Consultant as to the reasonableness of the Corporation estimates and the underlying assumptions for such estimates. For purposes of estimating Net Revenues, the Corporation may rely on projected rent increases deemed feasible by the Corporation as approved by the Housing Consultant; and

(3) A feasibility study prepared by a Housing Consultant concerning the Program Development to be financed with such Additional Bonds including an analysis of the rental market demand for such Program Development and the Revenues expected to be produced by such Program Development; provided however, that a feasibility study need not be prepared if: (i) a certificate of the Corporation approved by the Housing Consultant is delivered to the Trustee setting forth the following: Net Revenues produced in each of the five Fiscal Years following the issuance of such Additional Bonds will be at least equal to 1.10 times the Aggregate Debt Service on Outstanding Bonds, including such Additional Bonds, for each such Fiscal Year without taking into account Revenues to be produced during any such Fiscal Year by the Program Development to be financed by the issuance of such Additional Bonds, or (ii) the Program Development is to be leased to or operated by a department, agency or instrumentality of the State under a lease or operating agreement that obligates the lessee or operator to pay the Operation and Maintenance Costs of the Program Development and an amount equal to 1.10 times the Aggregate Debt Service on the Bonds to be issued to finance such Program Development.

The Trustee must also receive each of the foregoing items in the case of Additional Bonds issued and delivered to pay the Cost of Acquisition and Construction of any Program Development for which Bonds have previously been issued, provided however, that:

(1) The certificate for the Corporation setting forth the estimated Net Revenues and the confirming certificate of the Housing Consultant as to the reasonableness of the Corporation estimates and the underlying assumptions for such estimates shall show that Net Revenues in at least the fourth and fifth Fiscal Years following the Operation Date of the Program Development to be financed with such Additional Bonds will be at least equal to 1.10 times the Aggregate Debt Service on Outstanding Bonds, including such Additional Bonds, for each Fiscal Year; and

(2) The feasibility study prepared by the Housing Consultant concerning the Program Development to be financed with such Additional Bonds must be prepared and delivered regardless of any estimates of Net Revenues.

The provisions for the issuance of Additional Bonds contained in the preceding two paragraphs will not apply to any Series of Bonds necessary to be issued to provide funds for additions, extraordinary repairs, renewals, replacements, expansions, betterments, modifications, capital additions and improvements for any Program Development: (a) which are required by any governmental agency or authority; or (b) which in the opinion of the Corporation are necessary or desirable to improve the efficient use and occupancy the Program, to prevent a loss of Revenues or for safety, public health or environmental purposes.

One or more Series of Refunding Bonds may be issued in such principal amount which, when taken together with funds otherwise provided by the Corporation will provide the Corporation with funds sufficient for the purpose of refunding all or a portion of Outstanding Bonds of one or more Series, or of one or more maturities within a Series without meeting any additional bonds tests described above with respect to Additional Bonds, but upon the satisfaction of certain other conditions set forth in the Trust Indenture. These requirements include that if the Debt Service on the Series of Refunding Bonds proposed to be issued will be greater than the Debt Service on the Bonds to be refunded, the Trustee must receive a certificate of the Corporation demonstrating that estimated Net Revenues produced in each of the five Fiscal Years following the issuance of the proposed Refunding Bonds will be at least equal to 1.10 times the Aggregate Debt Service on Outstanding Bonds, including such Refunding Bonds for each such Fiscal Year and a confirming certificate of the Housing Consultant as to the reasonableness of the Corporation's estimates and, the underlying assumption for such estimates. The Corporation may simultaneously issue Additional Bonds to finance the Cost of Acquisition and Construction of a Program Development and Refunding Bonds pursuant to a Supplemental Indenture.

### **Subordinated Indebtedness (Trust Indenture, Section 2.05)**

The Corporation may at any time issue indebtedness payable out of and secured by a pledge of amounts in the General Reserve Fund as may from time to time be available for the purpose of paying such indebtedness provided however that: (i) such indebtedness may be incurred only to pay the Cost of Acquisition and Construction of a Program Development and the proceeds of such indebtedness shall be applied only for such purpose; (ii) such pledge shall be expressly subordinate in all respects to the pledge of the Net Revenues, moneys, securities and funds created by the Trust Indenture; (iii) the instrument pursuant to which such subordinated indebtedness is issued shall contain a provision to the effect that the trustee for, and the holders of, such subordinated indebtedness will have no right to cause the acceleration of the payment of the principal of or interest on such subordinated indebtedness unless and until the payment of the principal of and interest on the Outstanding Bonds has been accelerated under the Trust Indenture; and (iv) no payment out of the General Reserve Fund shall be made for such indebtedness if there shall occur an Event of Default under the Trust Indenture. Nothing in the Trust Indenture prevents the Corporation, for purposes of hedging, from entering into interest rate swaps, exchange or similar agreements which are payable from Net Revenues, on a basis subordinate, junior and inferior to all Bonds.

### **Separate Program Developments and Separate Programs (Trust Indenture, Section 2.06)**

The Corporation may issue indebtedness to acquire or construct separate rental housing developments not included within the, Program, which separate rental housing developments may be included in a separate rental housing system and which indebtedness shall be payable solely from the revenues or other income derived from the ownership or operation of such separate system; provided, however, that the Corporation will not issue indebtedness for the purpose of acquiring or constructing a separate rental housing development whether or not included in a separate rental housing system unless the Corporation shall deliver a certificate to the Trustee to the effect that the acquisition, construction or operation of such rental housing development will not result in a reduction of the Net Revenues for each of the next succeeding five Fiscal Years below the amount required to be maintained by the Trust Indenture.

### **Variable Rate Bonds (Trust Indenture, Section 2.07)**

The Corporation is authorized by the Trust Indenture to issue Variable Rate Bonds. The Supplemental Indenture providing for the issuance of such Variable Rate Bonds may provide for the Corporation to obtain a Support Facility or Facilities or alternate Support Facilities and enter into Support Agreements in connection therewith, enter into Remarketing Agreements and appoint Remarketing Agents, appoint tender agents to accept mandatory or optional tenders of Variable Rate Bonds, provide for interest to be payable and the interest rate redetermined on such dates and interest to accrue over such periods as set forth in such Supplemental Indenture, provide for the establishment, use, composition, adjustment and change of interest indices or modes or the establishment and use of alternate interest indices or the establishment of a fixed interest rate or rates, provide for the establishment and investment of special funds and accounts in connection with the issuance of such Variable Rate Bonds, including Escrow Funds, provide for special redemption or purchase provisions for such Variable Rate Bonds and establish notice provisions in connection with the purchase, redemption, delivery or tender of such Variable Rate Bonds. Any Supplemental Indenture providing for the issuance of Variable Rate Bonds may provide for the Corporation to issue to the provider or providers of a Support Facility or Facilities a Bond or Bonds to evidence the Corporation's obligations to such provider or providers.

### **Covenants of the Corporation (Trust Indenture, Article VI)**

**Encumbrances.** The Corporation covenants in the Trust Indenture that the Corporation will not create a mortgage upon the Program or any facilities of the Program while any Bonds are Outstanding. The Corporation will use its best efforts to prevent the creation of any lien upon the Program or any property essential to the proper operation of the Program or to the maintenance of the Revenues other than as permitted by the Trust Indenture. The Corporation will not create, or permit the creation of, any pledge, lien, charge or encumbrance upon the Revenues except as permitted the Trust Indenture.

**Disposition of Property.** The Corporation may not sell, lease, exchange, remove or otherwise dispose of the Program or any property of the Program except in accordance with law and as follows:

(a) Prior to the Operation Date of any Program Development, any payments to the Corporation under or in connection with any lease, contract, license, easement or right in respect of any Program Development or any part thereof, and any proceeds of sale, exchange, lease, removal or disposition thereof not used to replace property so sold, leased, exchanged, removed or disposed of, shall be deposited into any Program Development Account in the Acquisition and Construction Fund selected by the Corporation.

(b) The Corporation may sell, lease, exchange, remove or otherwise dispose of at any time and from time to time any property or facilities constituting a part of the Program only if the Corporation shall file with the Trustee a certificate stating that the sale, lease, exchange, removal or disposal of such property from the Program will not impair the ability of the Corporation to comply with its rate covenant under the Trust Indenture during the current Fiscal Year and during each Fiscal Year through and including the fifth Fiscal Year after such sale, exchange or removal and will not impair the ability of the Corporation to meet its obligations under the Trust Indenture. The proceeds, if any, of any such sale, lease exchange, removal or disposal not used to acquire other property necessary or desirable for the safe or efficient operation of the Program shall be deposited in the Revenue Fund or in the Debt Service Fund to be applied to the purchase or redemption of Bonds. Property and facilities removed by the Corporation from the Program and not sold, leased, exchanged or otherwise disposed of may be used by the Corporation for any public purpose of the Corporation, the revenues from which shall be free and clear from the pledge, lien and security interest created by the Trust Indenture.

(c) Except as otherwise provided in (b) above, any payments received by the Corporation pursuant to (a) above from the sale, lease, exchange, removal or disposition of property from the Program under or in connection with any lease, contract, license, arrangement, easement or right in respect of the Program or any part thereof shall constitute Revenues.

**Operation and Maintenance of the Program.** The Corporation will operate the Program continuously in an efficient and economical manner, and will maintain, preserve and keep the Program, including all parts thereof, in good repair, working order and condition. The Corporation will from time to time make all necessary and proper repairs and replacements so that the business carried on in connection with the Program by the Corporation at all times may be properly conducted in a manner consistent with prudent management.

**Insurance.** The Corporation is required to carry, or cause to be carried, insurance with generally recognized responsible insurers with policies payable to the Corporation, including the State, against risks, accidents or casualties at least to the extent that similar insurance is usually carried by multi-family rental housing programs operating properties similar to the Program. Any insurance carried by the Corporation pursuant to the Trust Indenture may be procured and maintained as part of or in conjunction with any other policy or policies carried by the Board, the Corporation or the State. The Board may create and establish special funds for self-insurance.

**Accounts, Reports and Annual Budget.** The Corporation will keep books of record and accounts in accordance with generally accepted accounting principles in which complete and accurate entries shall be made of all transactions relating to the Program and the Revenues. The books of record and accounts are subject to the inspection of the Trustee, or the Owners of not less than 10% of the Bonds then Outstanding, or their representatives authorized in writing.

The Corporation will file with the Trustee annually within 270 days after the close of each Fiscal Year, while any Bonds are Outstanding, a financial statement in reasonable detail for the preceding Fiscal Year showing the Revenues and all expenses together with a balance sheet in reasonable detail reflecting the balance of all funds relating to the Program as of the end of each Fiscal Year, which financial statement and balance sheet are to be accompanied by a certificate of a certified public accountant regarding compliance with generally accepted accounting principles.

The Corporation will adopt and file with the Trustee an annual budget prior to the beginning of each Fiscal Year setting forth for the coming Fiscal Year: (i) the estimated Revenues; (ii) the Aggregate Debt Service Requirement; (iii) the estimated Operation and Maintenance Costs; (iv) the estimated requirements for the Debt Reserve Fund and the Renewal and Contingency Fund, if any; (v) the outstanding subordinated debt service requirements if any; and (vi) any other requirements of the Program and the Trust Indenture,

**Rates, Rents, Fees and Charges.** If then permitted by law, the Corporation will, while any Bonds are Outstanding, establish, fix, prescribe, maintain and collect rates, rents, fees and charges for the use and occupancy of Program Developments so as to provide: (a) Net Revenues, which together with other lawfully available funds, shall be sufficient in each Fiscal Year, to provide an amount equal to 1.25 times the Aggregate Debt Service on Outstanding Bonds for such Fiscal Year; and (b) Net Revenues which shall be sufficient in each Fiscal Year, to provide an amount equal to 1.10 times the Aggregate Debt Service on Outstanding Bonds for such Fiscal Year.

The Corporation shall establish, adopt and review not less than annually rates, rents, fees and charges.

The failure by the Corporation to comply with the foregoing rate covenant shall not be deemed a default in the observance of a covenant under the Trust Indenture if (A) the Corporation presents a plan to the Trustee to remedy such failure within ninety (90) days from the date of notification of such failure by the Trustee and the Corporation implements such plan and pursues the same diligently until the failure is corrected or (B) upon the failure of the Corporation to present such plan within such ninety (90) day period, either (i) the Housing Consultant, upon request by the Trustee, presents such plan within sixty (60) days thereafter and the Corporation implements such plan provided by the Housing Consultant and pursues the same diligently until the failure is corrected or (ii) a Housing Consultant's Certificate is delivered to the Trustee stating that the schedule of rates, rents, fees and charges which will comply with such covenant are impracticable at such time and the Corporation establishes a schedule of rates, rents, fees and charges, as recommended by the Housing Consultant, which permits the Corporation to comply as nearly as practicable with such covenant. In the event no Housing Consultant is then currently serving the Corporation, the Trustee may retain a Housing Consultant at the expense of the Corporation for the sole purpose of assisting in the preparation of a plan for presentation to the Trustee.

**Additions to the Program.** The Corporation will not include a multi-family rental housing development in the Program unless the Corporation files with the Trustee a certificate and a concurring certificate of the Housing Consultant stating that the addition of such multi-family rental housing development to the Program will not impair the ability of the Corporation to comply, during the current Fiscal Year or any Fiscal Year through and including the fifth Fiscal Year after such addition, with its rate covenant, and will not impair the ability of the Corporation to meet its obligations under the Trust Indenture,

#### **Amending and Supplementing the Trust Indenture (Trust Indenture, Section Article VIII)**

Any provision of the Trust Indenture may be amended by the Corporation by a Supplemental Indenture upon the consent: (i) of the Owners of at least 51% in principal amount of all Bonds then Outstanding; and (ii) if less than all Series of Outstanding Bonds are affected, of the Owners of at least 51% in principal amount of the Bonds of each affected Series; and (iii) if the amendment changes the terms of any Sinking Fund Installment, of the Owners of at least 51% in principal amount of the Bonds of the Series and maturity for which such Sinking Fund Installment was established; excluding, in each case, from such consent, and from the Outstanding Bonds, the Bonds of any Series and maturity if such amendment by its terms will not take effect while any of such Bonds are Outstanding. No such amendment may permit a change in the terms of redemption or maturity of the principal of any Outstanding Bond or any installment of interest or a reduction in principal or Redemption Price or interest without the consent of the Owner, or reduce the percentages or otherwise affect the classes of Bonds the consent of the Owner of which is required for any such amendment.

The Corporation may adopt (without the consent of any Owners of the Bonds) Supplemental Indentures for any of the following purposes among others: (i) to cure or clarify any ambiguity, supply any omission or correct any defect or inconsistent provision in the Trust Indenture; (ii) to clarify matters or questions arising under the Trust Indenture and not contrary to or inconsistent with the Trust Indenture; (iii) to further restrict or impose limitations upon the issuance of Bonds or other evidences of indebtedness; (iv) to add to the covenants and agreements of the Corporation contained in the Trust Indenture; (v) to add to the restrictions contained in the Trust Indenture; (vi) to authorize Bonds of a Series; (vii) to confirm any pledge under the Trust Indenture of Net Revenues or other moneys, securities or funds; (viii) to obtain or maintain ratings; (ix) to add or modify any provision of the Trust Indenture as the result of enactment of any state or federal law which changes the treatment of the Bonds or interest thereon for tax purposes, and (x) to provide that the Corporation may hold the Revenue Fund, Renewal and

Contingency Fund or General Reserve Fund, if the Corporation determines such holding will provide for more efficient operation of the Program.

### **Events of Default and Remedies of Owners of the Bonds (Trust Indenture, Article IX)**

**Events of Default.** Events of default (each an "Event of Default") under the Trust Indenture include:

(i) failure to pay principal or Redemption Price or purchase price of any Bond upon tender for purchase when due and payable, whether at maturity, by proceedings for redemption, by declaration, by tender or otherwise;

(ii) failure to pay any installment of interest on any Bond or any Sinking Fund Installment when due and payable;

(iii) failure to observe any covenant, agreement or condition and continuation of such failure for 90 days after written notice thereof is delivered to the Corporation by the Trustee or the Owners of not less than 25 % in aggregate principal amount of the Bonds, unless such failure cannot be corrected within such 90 day period and corrective action is instituted and diligently pursued;

(iv) certain events of bankruptcy or insolvency;

(v) the entry of an order or decree with the consent of the Corporation appointing a receiver of the Program or any substantial part thereof so as to adversely affect Revenues or the entry of such an order without the consent of the Corporation, if such order shall not be vacated or stayed within 90 days of the date of entry thereof; and

(vi) an event provided in a Supplemental Indenture to constitute an Event of Default.

**Remedies.** If any Event of Default has occurred and has not been remedied, the Trustee or the Owners of not less than 25% in principal amount of the Bonds Outstanding (100% in the case of an Event of Default described in (iii) or (vi) above) shall be entitled, upon notice in writing to the Corporation (in the case of action by the Owners notice shall be delivered to both the Corporation and the Trustee) to declare the principal of and accrued interest on all of the Bonds then Outstanding to be due and payable immediately (subject to a rescission of such declaration upon the curing of such default).

If an Event of Default has occurred and has not been remedied, the Corporation will, upon demand of the Trustee, pay over to the Trustee forthwith all Revenues and all moneys, securities and funds then held by the Corporation in any fund or account under the Trust Indenture. The Trustee will apply such Revenues and such moneys, securities and funds and the income therefrom in the following order: (i) to payment of the reasonable and proper charges, expenses and liabilities of the Trustee, including the cost of securing the services of any Housing Consultant (or other consultant) retained to render advice to the Trustee; (ii) to the payment of the reasonable and proper charges and expenses of the Program including repairs and, replacement of facilities of the Program, necessary in the discretion of the Trustee to prevent loss of Revenues; and (iii) to the payment of interest and principal or the Redemption Price of Bonds. In addition, the Trustee will have the right to apply in an appropriate proceeding for appointment of a receiver of the Program. The Trustee shall not apply the proceeds of any draw on a Support Facility for purposes of items (i) and (ii) above.

If an Event of Default has occurred and has not been remedied, the Trustee may, or on request of the Owners of not less than 25% in principal amount of Bonds Outstanding must, proceed to protect and enforce its rights and the rights of the Owners under the Trust Indenture forthwith by a suit or suits in equity or at law, whether for the specific performance of any covenant in the Trust Indenture or of any power granted in the Trust Indenture or any remedy granted under the Act, or in the enforcement of any other legal or equitable right as the Trustee deems most effectual to enforce any of its rights or to perform any of its duties under the Trust Indenture. The Trustee may and upon the request of the Owners of a majority in principal amount of the Bonds Outstanding and upon being

furnished with reasonable security and indemnity must, institute and maintain proper actions to prevent any impairment of the security under the Trust Indenture or to preserve or protect the interest of the Trustee and of the Owners. All rights of action under the Trust Indenture may be enforced by the Trustee.

No Owner of a Bond shall have any right to institute any suit, action or proceeding for the enforcement of any provision of the Trust Indenture or the execution of any trust under the Trust Indenture or for any remedy under the Trust Indenture, unless: (i) such Owner previously has given the Trustee written notice of an Event of Default; (ii) the Owners of at least 25% in principal amount of Bonds Outstanding have filed a written request with the Trustee and have afforded the Trustee a reasonable opportunity either to exercise its powers or to institute such action, suit or proceeding; (iii) there have been offered to the Trustee adequate security and indemnity against its costs, expenses and liabilities to be incurred; and (iv) the Trustee has refused to comply with such request within 60 days.

The Owners of not less than a majority in principal amount of Bonds Outstanding may direct the time, method and place of conducting any proceeding for any remedy available to the Trustee or of exercising any trust or power conferred upon the Trustee, subject to the Trustee's right to decline to follow such direction upon advice of counsel that an action may not be taken or upon the Trustee's good faith determination that such action would involve the Trustee in personal liability or would be unjustly prejudicial to Owners not parties to such direction.

Nothing in the Trust Indenture or in the Bonds shall affect or impair the obligation of the Corporation to pay Bonds or interest thereon when due or any Owner to enforce such payment.

**Notice of Default.** The Trustee shall promptly mail notice of the occurrence of any Event of Default to each Owner of Bonds Outstanding.

#### **Defeasance (Trust Indenture, Article XI)**

If the Corporation shall pay or cause to be paid the principal or Redemption Price, if applicable, and interest due or to become due on all Bonds Outstanding, then the pledge of any Net Revenues, and other moneys, securities and funds pledged under the Trust Indenture and all covenants, agreements and other obligations of the Corporation to the Owners shall at the option of the Corporation expressed in writing thereupon cease, terminate and become void and be discharged and satisfied. If the Corporation shall pay or caused to be paid the principal or Redemption Price, if applicable, and interest due or to become due on any Bonds Outstanding, such Bonds shall cease to be entitled to any lien, benefit or security under the Trust Indenture, and all covenants, agreements and obligations of the Corporation to the Owners of such Bonds shall thereupon cease, terminate and become void and be discharged and satisfied.

Bonds will be deemed to have been paid within the meaning of the preceding paragraph when the following conditions are met: (i) in case of Bonds to be redeemed prior to maturity, the Corporation has given to the Trustee irrevocable instructions to mail notice of redemption therefor; (ii) there have been deposited with the Trustee either moneys in an amount which shall be sufficient, or certain specified Investment Securities the principal of and the interest on which when due will provide moneys which, together with other moneys deposited with the Trustee, will be sufficient to pay when due the principal or Redemption Price, if applicable, and interest due and to become due on such Bonds on and prior to the Redemption Date or at maturity, plus all fees and expenses, including reasonable attorneys' fees relating to such Bonds which are or will be due on such date or dates, as the case maybe; and (iii) in the event such Bonds are not subject to redemption within the next succeeding 60 days, the Corporation has given the Trustee irrevocable instructions to mail, as soon as practicable, a notice to the Owners of such Bonds that such deposit has been made with the Trustee and that such Bonds are deemed to be paid and stating the maturity or Redemption Date upon which moneys are to be available to pay the principal or Redemption Price, if applicable, on such Bonds. If a Support Facility has been established to pay such Bonds then: (i) the deposit required by clause (ii) above must be made from moneys drawn or paid under such Support Facility; or (ii) the Trustee must receive an opinion of counsel, nationally recognized in matters relating to bankruptcy law and acceptable to each Rating Agency, that the deposit required by clause (ii) above to be made from moneys other than those drawn or paid under such Support Facility is not subject to a preference under U.S. bankruptcy law.

**Appointment and Removal of Trustee (Trust Indenture, Sections 7.07 and 7.12)**

The Trust Indenture contains provisions regarding the appointment, resignation and removal of the Trustee. The Corporation may at any time remove the Trustee; provided that such removal is subject to revocation by the Owners of 10% of the Bonds Outstanding. The Corporation shall review the desirability of removing the Trustee every three Fiscal Years beginning after Fiscal Year 2008. No removal may be effected if an Event of Default has occurred and is continuing, or there is any deficiency in any fund or account, or if such removal would result in a reduction or withdrawal of the ratings of the Bonds by any Rating Agency.

## FORM OF CONTINUING DISCLOSURE CERTIFICATE

This Continuing Disclosure Undertaking (the "Undertaking") is dated and made as of October 1, 2004 by the Housing and Community Development Corporation of Hawaii (the "Corporation") in connection with the issuance of the Corporation's Hawaii Rental Housing System Revenue Bonds, 2004 Refunding Series A and 2004 Refunding Series B (the "Bonds"). As authorized by Section 8 of Resolution No. 092, adopted by the Board of Directors of the Corporation on September 16, 2004, the Corporation agrees as follows:

### ARTICLE I

#### The Undertaking

Section 1.1. Purpose. This Undertaking is being executed, delivered and made solely to assist the underwriter of the Bonds in complying with subsection (b)(5) of the Rule.

Section 1.2. Annual Financial Information. (a) The Corporation shall provide Annual Financial Information with respect to each fiscal year of the Corporation, commencing with the fiscal year ending June 30, 2004, by no later than nine months after the end of the respective fiscal year, to each NRMSIR and the SID.

(b) The Corporation shall provide, in a timely manner, notice of any failure of the Corporation to provide the Annual Financial Information by the date specified in subsection (a) above to (i) either the MSRB or each NRMSIR, and (ii) the SID.

Section 1.3. Audited Financial Statements. If not provided as part of Annual Financial Information by the date required by Section 1.2(a) hereof, the Corporation shall provide Audited Financial Statements, when and if available, to each NRMSIR and the SID.

Section 1.4 Material Event Notices. (a) If a Material Event occurs, the Corporation shall provide, in a timely manner, notice of such Material Event to (i) either the MSRB or each NRMSIR, (ii) the SID, and (iii) the Trustee.

(b) Any such notice of a defeasance of Bonds shall state whether the Bonds have been escrowed to maturity or to an earlier redemption date and the timing of such maturity or redemption.

Section 1.5. Additional Disclosure Obligations. The Corporation acknowledges and understands that other state and federal laws, including but not limited to the Securities Act of 1933 and Rule 10b-5 promulgated under the Securities Exchange Act of 1934, may apply to the Corporation and that, under some circumstances, additional disclosures or other action in addition to those required by this Undertaking may be required to enable the Corporation to fully discharge all of its duties and obligations under such laws.

Section 1.6. Additional Information. Nothing in this Undertaking shall be deemed to prevent the Corporation from disseminating any other information, using the means of dissemination set forth in this Undertaking or any other means of communication, or including any other information in any Annual Financial Information or notice of Material Event hereunder, in addition to that which is required by this Undertaking. If the Corporation chooses to do so, the Corporation shall have no obligation under this Undertaking to update such additional information or include it in any future Annual Financial Information or notice of a Material Event hereunder.

Section 1.7. No Previous Non-Compliance. The Corporation represents that, except as disclosed in the Official Statement with respect to the Bonds, since July 3, 1995, it has not failed to comply in any material respect with any previous undertaking in a written contract or agreement specified in paragraph (b)(5)(i) of the Rule.

### ARTICLE II

#### Operating Rules

Section 2.1. Reference to Other Documents. It shall be sufficient for purposes of Section 1.2 hereof if the Corporation provides Annual Financial Information by specific reference to documents (i) either (1) provided to each NRMSIR existing at the time of such reference and the SID or (2) filed with the SEC, or (ii) if such document is an Official Statement, available from the MSRB.

Section 2.2. Submission of Information. Annual Financial Information may be provided in one document or multiple documents, and at one time or in part from time to time.

Section 2.3. Material Event Notices. Each notice of a Material Event hereunder shall be captioned "Notice of Material Event" and shall prominently state the title, date and CUSIP numbers of the Bonds.

Section 2.4. Filing with Certain Dissemination Agents. The Corporation may satisfy its obligations hereunder to file any notice, document or information with a NRMSIR or SID by filing the same with any dissemination agent or conduit, including any "central post office" or similar entity, assuming or charged with responsibility for accepting notices, documents or information for transmission to such NRMSIR or SID, to the extent permitted by the SEC or SEC staff or required by the SEC. For this purpose, permission shall be deemed to have been granted by the SEC staff if and to the extent the agent or conduit has received an interpretive letter, which has not been revoked, from the SEC staff to the effect that using the agent to transmit information to the NRMSIRs and the SID will be treated for purposes of the Rule as if such information were transmitted directly to the NRMSIRs and the SID.

Section 2.5. Transmission of Information and Notices. Unless otherwise required by law and, in the Corporation's sole determination, subject to technical and economic feasibility, the Corporation shall employ such methods of information and notice transmission as shall be requested or recommended by the herein-designated recipients of the Corporation's information and notices.

Section 2.6. Fiscal Year. (a) The Corporation's current fiscal year is the twelve-month period ending on June 30. The Corporation shall promptly notify (i) each NRMSIR, (ii) the SID and (iii) the Trustee of each change in its fiscal year.

(b) Annual Financial Information shall be provided at least annually notwithstanding any fiscal year longer than 12 calendar months.

### ARTICLE III

#### Effective Date, Termination, Amendment and Enforcement

Section 3.1. Effective Date; Termination. (a) This Undertaking shall be effective upon the issuance of the Bonds.

(b) The Corporation's obligations under this Undertaking shall terminate upon a legal defeasance, prior redemption or payment in full of all of the Bonds.

(c) This Undertaking, or any provision hereof, shall be null and void in the event that the Corporation (1) receives an opinion of Counsel to the effect that those portions of the Rule which require this Undertaking, or such provision, as the case may be, do not or no longer apply to such Bonds, whether because such portions of the Rule are invalid, have been repealed, or otherwise, as shall be specified in such opinion, and (2) delivers copies of such opinion to each NRMSIR and the SID.

Section 3.2. Amendment. (a) This Undertaking may be amended, by written agreement of the parties, without the consent of the holders of the Bonds (except to the extent required under clause (4)(ii) below), if all of the following conditions are satisfied: (1) such amendment is made in connection with a change in circumstances that arises from a change in legal (including regulatory) requirements, a change in law (including rules or regulations) or in interpretations thereof, or a change in the identity, nature or status of the Corporation or the type of business conducted thereby, (2) this Undertaking as so amended would have complied with the requirements of the Rule as of the date of this Undertaking, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances, (3) the Corporation shall have received an opinion of Counsel to the effect as set forth in clause (2) above, (4) either (i) the Corporation shall have received either an opinion of Counsel or a determination by a person, in each case unaffiliated with the Corporation, to the effect that the amendment does not materially impair the interests of the holders of the Bonds or (ii) the holders of the Bonds consent to the amendment to this Undertaking pursuant to the same procedures as are required for amendments to the Indenture with consent of holders of Bonds pursuant to the Indenture as in effect on the date of this Undertaking, and (5) the Corporation shall have delivered copies of such opinion(s) and amendment to each NRMSIR and the SID.

(b) This Undertaking may be amended without the consent of the holders of the Bonds, if all of the following conditions are satisfied: (1) an amendment to the Rule is adopted, or a new or modified official

interpretation of the Rule is issued, after the effective date of this Undertaking which is applicable to this Undertaking, (2) the Corporation shall have received an opinion of Counsel, to the effect that performance by the Corporation under this Undertaking as so amended will not result in a violation of the Rule and (3) the Corporation shall have delivered copies of such opinion and amendment to each NRMSIR and the SID.

(c) To the extent any amendment to this Undertaking results in a change in the type of financial information or operating data provided pursuant to this Undertaking, the first Annual Financial Information provided thereafter shall include a narrative explanation of the reasons for the amendment and the impact of the change in the type of operating data or financial information being provided.

(d) If an amendment is made to the accounting principles to be followed by the Corporation in preparing its financial statements, the Annual Financial Information for the fiscal year in which the change is made shall present a comparison between the financial statements or information prepared on the basis of the new accounting principles and those prepared on the basis of the former accounting principles. Such comparison shall include a qualitative and, to the extent reasonably feasible, quantitative discussion of the differences in the accounting principles and the impact of the change in the accounting principles on the presentation of the financial information.

Section 3.3. Benefit; Third-Party Beneficiaries; Enforcement. (a) The provisions of this Undertaking shall constitute a contract with, and inure solely to the benefit of, the holders from time to time of the Bonds, except that beneficial owners of Bonds shall be third-party beneficiaries of this Undertaking and shall be deemed to be holders of Bonds for purposes of Section 3.3(b) hereof. The provisions of this Undertaking shall create no rights in any person or entity except as provided in this subsection (a) and Section 3.3(b).

(b) The obligations of the Corporation to comply with the provisions of this Undertaking shall be enforceable (i) in the case of enforcement of obligations to provide financial statements, financial information, operating data and notices, by any holder of Outstanding Bonds, or (ii), in the case of challenges to the adequacy of the financial statements, financial information and operating data so provided, by the holders of not less than a majority in aggregate principal amount of the Bonds at the time Outstanding. The holders' rights to enforce the provisions of this Undertaking shall be limited solely to a right, by action in mandamus or for specific performance, to compel performance of the Corporation's obligations under this Undertaking.

(c) Any failure by the Corporation to perform in accordance with this Undertaking shall not constitute a default or an Event of Default under the Indenture, and the rights and remedies provided by the Indenture upon the occurrence of a default or an Event of Default shall not apply to any such failure.

(d) This Undertaking shall be construed and interpreted in accordance with the laws of the State, and any suits and actions arising out of this Undertaking shall be instituted in a court of competent jurisdiction in the State; provided, however, that to the extent this Undertaking addresses matters of federal securities laws, including the Rule, this Undertaking shall be construed in accordance with such federal securities laws and official interpretations thereof.

## ARTICLE IV

### Definitions

Section 4.1. Definitions. The following terms used in this Undertaking shall have the following respective meanings:

(1) "Annual Financial Information" means, collectively, (i) the financial information and operating data with respect to the Program, for each fiscal year of the Corporation, of the types included in the Official Statement under the caption "The Program" including information of the type shown in Table 1 for the five most recent fiscal years, and (ii) the information regarding amendments to this Undertaking required pursuant to Sections 3.2(c) and (d) of this Undertaking. Annual Financial Information shall include Audited Financial Statements, if available, or Unaudited Financial Statements.

The descriptions contained in clause (i) of the preceding paragraph of financial information and operating data constituting Annual Financial Information are of general categories of financial information and operating data. When such descriptions include information that no longer can be generated because the operations to which it related have been materially changed or discontinued, a statement to that effect shall be provided in lieu of such information.

(2) "Audited Financial Statements" means the annual financial statements, if any, with respect to the Program, audited by such auditor as shall then be required or permitted by State law or the Indenture. Audited Financial Statements shall be prepared in accordance with GAAP.

(3) "Counsel" means Hawkins Delafield & Wood LLP or other nationally recognized bond counsel or counsel expert in federal securities laws.

(4) "GAAP" means generally accepted accounting principles as prescribed from time to time for governmental units by the Governmental Accounting Standards Board, the Financial Accounting Standards Board, or any successor to the duties and responsibilities of either of them.

(5) "Indenture" means the Trust Indenture between the Corporation and U.S. Bank National Association, as Trustee, dated as of October 1, 2004, as supplemented by the First Supplemental Trust Indenture also dated as of October 1, 2004, between the Corporation and the Trustee, providing for the issuance of the Bonds.

(6) "Material Event" means any of the following events with respect to the Bonds, whether relating to the Corporation or otherwise, if material:

- (i) principal and interest payment delinquencies;
- (ii) non-payment related defaults;
- (iii) unscheduled draws on debt service reserves reflecting financial difficulties;
- (iv) unscheduled draws on credit enhancements reflecting financial difficulties;
- (v) substitution of credit or liquidity providers, or their failure to perform;
- (vi) adverse tax opinions or events affecting the tax-exempt status of the security;
- (vii) modifications to rights of security holders;
- (viii) bond calls
- (ix) defeasances;
- (x) release, substitution, or sale of property securing repayment of the securities; and
- (xi) rating changes.

(7) "MSRB" means the Municipal Securities Rulemaking Board established pursuant to Section 15B(b)(1) of the Securities Exchange Act of 1934.

(8) "NRMSIR" means, at any time, a then-existing nationally recognized municipal securities information repository, as recognized from time to time by the SEC for the purposes referred to in the Rule. NRMSIRs currently are identified on the SEC website at [www.sec.gov/consumer/nrmsir.htm](http://www.sec.gov/consumer/nrmsir.htm).

(9) "Official Statement" means each of the Official Statements dated October 5 and 7, 2004 related to the Bonds.

(10) "Rule" means Rule 15c2-12 promulgated by the SEC under the Securities Exchange Act of 1934 (17 CFR Part 240, §240.15c2-12), as in effect on the date of this Undertaking, including any official interpretations thereof issued either before or after the effective date of this Undertaking which are applicable to this Undertaking.

(11) "SEC" means the United States Securities and Exchange Commission.

(12) "SID" means, at any time, a then-existing state information depository, if any, as operated or designated as such by or on behalf of the State for the purposes referred to in the Rule. As of the date of this Undertaking, there is no SID.

(13) "Unaudited Financial Statements" means the same as Audited Financial Statements, except that they shall not have been audited.

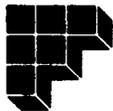
HOUSING AND COMMUNITY  
DEVELOPMENT CORPORATION OF HAWAII

By: \_\_\_\_\_

Executive Director

**FORM OF BOND INSURANCE POLICY**

**(THIS PAGE INTENTIONALLY LEFT BLANK)**



**FINANCIAL  
SECURITY  
ASSURANCE®**

## **MUNICIPAL BOND INSURANCE POLICY**

ISSUER:

BONDS:

Policy No.: -N

Effective Date:

Premium:

FINANCIAL SECURITY ASSURANCE INC. ("Financial Security"), for consideration received, hereby UNCONDITIONALLY AND IRREVOCABLY agrees to pay to the trustee (the "Trustee") or paying agent (the "Paying Agent") (as set forth in the documentation providing for the issuance of and securing the Bonds) for the Bonds, for the benefit of the Owners or, at the election of Financial Security, directly to each Owner, subject only to the terms of this Policy (which includes each endorsement hereto), that portion of the principal of and interest on the Bonds that shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer.

On the later of the day on which such principal and interest becomes Due for Payment or the Business Day next following the Business Day on which Financial Security shall have received Notice of Nonpayment, Financial Security will disburse to or for the benefit of each Owner of a Bond the face amount of principal of and interest on the Bond that is then Due for Payment but is then unpaid by reason of Nonpayment by the Issuer, but only upon receipt by Financial Security, in a form reasonably satisfactory to it, of (a) evidence of the Owner's right to receive payment of the principal or interest then Due for Payment and (b) evidence, including any appropriate instruments of assignment, that all of the Owner's rights with respect to payment of such principal or interest that is Due for Payment shall thereupon vest in Financial Security. A Notice of Nonpayment will be deemed received on a given Business Day if it is received prior to 1:00 pm (New York time) on such Business Day; otherwise, it will be deemed received on the next Business Day. If any Notice of Nonpayment received by Financial Security is incomplete, it shall be deemed not to have been received by Financial Security for purposes of the preceding sentence and Financial Security shall promptly so advise the Trustee, Paying Agent or Owner, as appropriate, who may submit an amended Notice of Nonpayment. Upon disbursement in respect of a Bond, Financial Security shall become the owner of the Bond, any appurtenant coupon to the Bond or right to receipt of payment of principal of or interest on the Bond and shall be fully subrogated to the rights of the Owner, including the Owner's right to receive payments under the Bond, to the extent of any payment by Financial Security hereunder. Payment by Financial Security to the Trustee or Paying Agent for the benefit of the Owners shall, to the extent thereof, discharge the obligation of Financial Security under this Policy.

Except to the extent expressly modified by an endorsement hereto, the following terms shall have the meanings specified for all purposes of this Policy. "Business Day" means any day other than (a) a Saturday or Sunday or (b) a day on which banking institutions in the State of New York or the Insurer's Fiscal Agent are authorized or required by law or executive order to remain closed. "Due for Payment" means (a) when referring to the principal of a Bond, payable on the stated maturity date thereof or the date on which the same shall have been duly called for mandatory sinking fund redemption and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by mandatory sinking fund redemption), acceleration or other advancement of maturity unless Financial Security shall elect, in its sole discretion, to pay such principal due upon such acceleration together with any accrued interest to the date of acceleration and (b) when referring to interest on a Bond, payable on the stated date for payment of interest. "Nonpayment" means, in respect of a Bond, the failure of the Issuer to have provided sufficient funds to the Trustee or, if there is no Trustee, to the Paying Agent for payment in full of all principal and interest that is Due for Payment on such Bond. "Nonpayment" shall also include, in respect of a Bond, any payment of principal or interest that is Due for Payment made to an Owner by or on behalf of the Issuer 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. "Notice" means telephonic or telecopied notice, subsequently confirmed in a signed writing, or written notice by registered or certified mail, from an Owner, the Trustee or the Paying Agent to Financial Security which notice shall specify (a) the person or entity making the claim, (b) the Policy Number, (c) the claimed amount and (d) the date such claimed amount became Due for Payment. "Owner" means, in respect of a Bond, the person or entity who, at the time of Nonpayment, is entitled under the terms of such Bond to payment thereof, except that "Owner" shall not include the Issuer or any person or entity whose direct or indirect obligation constitutes the underlying security for the Bonds.

Financial Security may appoint a fiscal agent (the "Insurer's Fiscal Agent") for purposes of this Policy by giving written notice to the Trustee and the Paying Agent specifying the name and notice address of the Insurer's Fiscal Agent. From and after the date of receipt of such notice by the Trustee and the Paying Agent, (a) copies of all notices required to be delivered to Financial Security pursuant to this Policy shall be simultaneously delivered to the Insurer's Fiscal Agent and to Financial Security, and shall not be deemed received until received by both and (b) all payments required to be made by Financial Security under this Policy may be made directly by Financial Security or by the Insurer's Fiscal Agent on behalf of Financial Security. The Insurer's Fiscal Agent is the agent of Financial Security only and the Insurer's Fiscal Agent shall in no event be liable to any Owner for any act of the Insurer's Fiscal Agent or any failure of Financial Security to deposit or cause to be deposited sufficient funds to make payments due under this Policy.

To the fullest extent permitted by applicable law, Financial Security agrees not to assert, and hereby waives, only for the benefit of each Owner, all rights (whether by counterclaim, setoff or otherwise) and defenses (including, without limitation, the defense of fraud, whether acquired by subrogation, assignment or otherwise, to the extent that such rights and defenses may be available to Financial Security) to avoid payment of its obligations under this Policy in accordance with the express provisions of this Policy.

This Policy sets forth in full the undertaking of Financial Security, and shall not be modified, altered or affected by any other agreement or instrument, including any modification or amendment thereto. Except to the extent expressly modified by an endorsement hereto, (a) any premium paid in respect of this Policy is nonrefundable for any reason whatsoever, including payment, or provision being made for payment, of the Bonds prior to maturity and (b) this Policy may not be canceled or revoked. THIS POLICY IS NOT COVERED BY THE PROPERTY CASUALTY INSURANCE SECURITY FUND SPECIFIED IN ARTICLE 76 OF THE NEW YORK INSURANCE LAW.

In witness whereof, FINANCIAL SECURITY ASSURANCE INC. has caused this Policy to be executed on its behalf by its Authorized Officer.

[Counter signature]

FINANCIAL SECURITY ASSURANCE INC.

By \_\_\_\_\_

By \_\_\_\_\_  
Authorized Officer

A subsidiary of Financial Security Assurance Holdings Ltd.  
350 Park Avenue, New York, N.Y. 10022-6022

(212) 826-0100

Form 500NY (5/90)

**PROVISIONS RELATING TO 2004B BONDS (AUCTION RATE CERTIFICATES)**

Section 100. Certain Definitions. In addition to the terms defined elsewhere in the First Supplemental Indenture, the following terms shall have the following meanings with respect to the 2004B Bonds, unless the context otherwise requires:

**AA Financial Rate** means, on any date of determination, for any Auction Period, the interest equivalent of commercial paper having a maturity of 30 days as such rate is published on the Business Day prior to such date by the Board of Governors of the Federal Reserve System on its World Wide Web site <http://www.federalreserve.gov/releases/cp/histrates.txt>, or any successor publication (“H.15(519)”) under the caption “AA Financial.” In the event that such publication has not been published in a timely manner, the AA Financial Rate shall be calculated by the Market Agent, and shall be the bond equivalent yield of the arithmetic mean of the offered rates as of 11:00 A.M., New York City time, on the determination date of three leading dealers of U.S. dollar commercial paper in the City of New York (which may include the Market Agent) selected by the Market Agent, for U.S. dollar commercial paper having a maturity of 30, 60 or 90 days, as applicable, placed for financial issuers whose bond rating is “AA” or the equivalent, from a nationally recognized securities rating agency; provided, however, that if the dealers selected as aforesaid by the Market Agent are not quoting as mentioned in this sentence (and if the Market Agent, in its discretion, determines that such quotations can not be obtained from any three leading dealers of U.S. dollar commercial paper in the City of New York) such rate shall be the same rate as in effect for the immediately preceding Auction Period. For purposes of this definition, the “interest equivalent” of a rate stated on a discount basis (a “discount rate”) for commercial paper of a given day’s maturity shall be equal to the product of (A) 100 times (B) the discount rate times (C) the quotient (rounded upwards to the next higher one-thousandth (.001) of 1%) of (x) the applicable number of days in a year (365 or 366) divided by (y) the difference between (1) 360 and (2) the product of the discount rate (expressed in decimals) times the applicable number of days in which such commercial paper matures.

**After-Tax Equivalent Rate** means, on any date of determination, the interest rate per annum equal to the product of:

- (i) the “AA” Financial Rate on such date; and
- (ii) 1.00 minus the Statutory Corporate Tax Rate on such date.

**All-Hold Rate** means, on any date of determination, the interest rate per annum equal to 90% (as such percentage may be adjusted pursuant to Section 110 of this Exhibit A) of the lesser on such date of:

- (a) the After-Tax Equivalent Rate on such date; or
- (b) the Kenny Index on such date;

rounded to the nearest one thousandth (.001) of 1%; provided that in no event shall the All-Hold Rate be more than the Maximum Rate or less than zero.

**Applicable ARCs Rate** has the meaning assigned to such term in Section 102(b) of this Exhibit A.

**Applicable Number of Business Days** means the greater of two Business Days or one Business Day plus the number of Business Days by which the Auction Date precedes the first day of the next succeeding Auction Period.

**Applicable Percentage** means, on any date of determination, the percentage determined (as such percentage may be adjusted pursuant to Section 110 of this Exhibit A) based on the lower of the prevailing credit ratings on the ARCs in effect at the close of business on the Business Day immediately preceding such date, as set forth below:

<u>Moody's</u>	<u>S &amp; P</u>	<u>Fitch</u>	<u>Applicable Percentage</u>
"Aaa"	"AAA"	"AAA"	175%
"Aa3" to "Aa1"	"AA-" to "AA+"	"AA-" to "AA+"	175%
"A3" to "A1"	"A-" to "A+"	"A-" to "A+"	175%
"Baa3" to "Baa1"	"BBB-" to "BBB+"	"BBB-" and "BBB+"	200%
Below "Baa3"	Below "BBB-"	Below "BBB-"	265%

provided, that, in the event that the ARCs are not rated by any nationally recognized securities rating agency and if a Payment Default shall have occurred and be continuing, the Applicable Percentage shall be 265%. For purposes of this definition, Moody's rating categories of "Aaa," "Aa," "A" and "Baa," and S&P and Fitch's rating categories of "AAA," "AA," "A," and "BBB" refer to and include the respective rating categories correlative thereto if one or more of such rating agencies have changed or modified their generic rating categories or if Moody's, S&P or Fitch no longer rates the ARCs and have been replaced.

*ARCs* means the Auction Rate Certificates Outstanding. All ARCs shall bear the same Auction Rate.

*Auction* means each periodic implementation of the Auction Procedures.

*Auction Agreement* means the Auction Agreement, dated as of October 1, 2004, relating to the ARCs among the Corporation, the Trustee and the Auction Agent, and any similar agreement with a successor Auction Agent, in each case as from time to time amended or supplemented.

*Auction Agent* means any person appointed as such pursuant to Section 112 of this Exhibit A.

*Auction Date* means October 19, 2004 and thereafter, the Business Day immediately preceding the first day of each Auction Period, other than:

- (a) each Auction Period commencing after the ownership of the ARCs is no longer maintained in book entry form by DTC;
- (b) each Auction Period commencing after the occurrence and during the continuance of a Payment Default;
- (c) any Auction Period commencing less than the Applicable Number of Business Days after the cure or waiver of a Payment Default;
- (d) the Initial Auction Period; or
- (e) with respect to certain ARCs, each Auction Period during which such ARCs are subject to redemption or maturity.

Notwithstanding the foregoing, the Auction Date for one or more Auction Periods may be changed pursuant to Section 114 of this Exhibit A.

*Auction Period* means with respect to the ARCs (a) the Initial Auction Period, (b) each successive 7-day period after the Initial Auction Period, commencing on a Wednesday (or the Business Day following the last day of the prior Auction Period, if the prior Auction Period does not end on a Tuesday) and ending on (and including) (i) a Tuesday (unless such Tuesday is not followed by a Business Day, in which case such Auction Period will end on the next succeeding day that is followed by a Business Day) or (ii) a day when ARCs, or portion thereof, are subject to redemption or at maturity and (c) each Special Auction Period.

*Auction Procedures* means the procedures set forth in Section 104 of this Exhibit A.

*Auction Rate* means, with respect to ARCs, the rate of interest per annum on any Auction Date that results from the implementation of the Auction Procedures, and determined as described in Section 104 of this Exhibit A.

*Available ARCs* has the meaning assigned to such term in Section 104(c)(i)(A) of this Exhibit A.

**Bid** has the meaning assigned to such term in Section 104(a)(i) of this Exhibit A.

**Bidder** has the meaning assigned to such term in Section 104(a)(i) of this Exhibit A.

**Broker-Dealer** means UBS Financial Services Inc. (sole Broker-Dealer for the ARCs), or any other broker or dealer (each as defined in the Securities Exchange Act), commercial bank or other entity permitted by law to perform the functions required of a Broker-Dealer set forth in the Auction Procedures that (i) is a Participant (or an affiliate of a Participant), (ii) has been approved by the Corporation and (iii) has entered into a Broker-Dealer Agreement that remains effective.

**Broker-Dealer Agreement** means (a) the Broker-Dealer Agreement, dated as of October 1, 2004, between the Auction Agent and UBS Financial Services Inc. in relation to the ARCs, and (b) each other agreement between the Auction Agent and a Broker-Dealer pursuant to which the Broker-Dealer agrees to participate in Auctions as set forth in the Auction Procedures, in each case as from time to time amended or supplemented.

**Broker-Dealer Fee** means the fee to be paid to the Broker-Dealer for the services rendered by them under the Broker-Dealer Agreement.

**Business Day** means any day other than (i) April 14, April 15, December 30, December 31, (ii) any day on which banks in the City of New York, New York, the New York Stock Exchange, the Trustee or the Auction Agent are authorized or permitted by law or executive order to close, or (iii) such other days as may be agreed to in writing by the Trustee, the Market Agent, the Auction Agent, the Broker-Dealer, and the Corporation.

**Change of Preference Law** means, with respect to any Owner of ARCs, any amendment to the Code or other statute enacted by the Congress of the United States or any temporary, proposed or final regulation promulgated by the United States Treasury, after the Date of Delivery which (i) changes or would change any deduction, credit or other allowance allowable in computing liability for any federal tax with respect to, or (ii) imposes or would impose or reduces or would reduce or increases or would increase any federal tax (including, but not limited to, preference or excise taxes) upon, any interest earned by any holder of bonds the interest on which is excluded from federal gross income under Section 103 of the Code.

**Commission** means the Securities and Exchange Commission.

**Date of Delivery** means the date of issuance and delivery of the ARCs.

**Default Rate** on any date of determination means the interest rate per annum equal to the lesser of (i) the Applicable Percentage of the Kenny Index or (ii) the Maximum Interest Rate.

**Existing Owner** means (a) with respect to and for the purpose of dealing with the Auction Agent in connection with an Auction, a Broker-Dealer listed in the Existing Owner Registry at the close of business on the Business Day immediately preceding the Auction Date for such Auction and (b) with respect to and for the purpose of dealing with the Broker-Dealer in connection with an Auction, a Person who is a beneficial owner of ARCs listed in the Existing Owner Registry.

**Existing Owner Registry** means the register maintained by the Auction Agent pursuant to Section 2.2(a)(i) of the Auction Agreement.

**Hold Order** has the meaning set forth in Section 104(a)(i) of this Exhibit A.

**Initial Auction Period** means the period from and including the Date of Delivery to (but not including) the Initial Interest Payment Date.

**Initial Interest Payment Date** means October 20, 2004.

**Interest Amount** means the amount of interest distributable in respect of each \$1,000 in principal amount (taken, without rounding, to .0001 of one cent) of ARCs for any Auction Period or part thereof, as calculated in accordance with Section 108 of this Exhibit A.

**Interest Payment Date** means, with respect to the ARCs, the day following the end of each Auction Period and shall also mean the date of redemption and the stated maturity date for such ARCs. Except for an Interest Payment Date occurring on a redemption date or at the stated maturity of ARCs, if any such date is not a Business Day, the Interest Payment Date shall be the next succeeding Business Day.

**Kenny Index** means the applicable index most recently made available by Kenny S&P Evaluation Services (“Kenny”) or any successor thereto (the “Indexing Agent”) based upon 30-day yield evaluations at par of securities, the interest on which is excluded from gross income for federal income tax purposes under the Code, of not less than five “Intermediate Grade” component issuers selected by the Indexing Agent which shall include, without limitation, issuers of general obligation bonds. The specific issuers included among the component issuers may be changed from time to time by the Indexing Agent in its discretion. The securities on which the Kenny Index is based shall not include any securities the interest on which is subject to a “minimum tax” or similar tax under the Code, unless all such securities are subject to such tax. In the event that Kenny no longer publishes an index satisfying the above definition of the Kenny Index or the Market Agent reasonably concludes that the Kenny Index will not be announced in a timely manner, then the Market Agent shall announce a rate based upon the same criteria used by Kenny to determine the Kenny Index and the rate announced by the Market Agent for each Auction Date thereafter shall be used in lieu of the Kenny Index for each Auction Date.

**Market Agent** means initially UBS Financial Services Inc., or any successor appointed as such pursuant to Section 111 of this Exhibit A, and its or their successors or assigns.

**Market Agent Agreement** means the Market Agent Agreement, dated as of October 1, 2004, relating to the ARCs between the Trustee and UBS Financial Services Inc., as Market Agent, and any similar agreement with a successor Market Agent, in each case as from time to time amended or supplemented.

**Maximum Interest Rate** means the lesser of (a) 12% per annum or (b) the maximum rate of interest permitted by State law.

**Maximum Rate** means on any date of determination, the interest rate per annum equal to the lesser of:

- (a) the Applicable Percentage of the higher of (i) the After-Tax Equivalent Rate on such date or (ii) the Kenny Index on such date; or
- (b) the Maximum Interest Rate;

rounded to the nearest one thousandth (.001) of 1%.

**Order** has the meaning assigned to such term in Section 104(a) of this Exhibit A.

**Payment Default** means the failure by the Corporation and Insurer to make payment of interest on, premium, if any, and principal of the ARCs to Owners when due.

**Potential Owner** means, any Person (including an Existing Owner that is (a) a Broker-Dealer when dealing with the Auction Agent and (b) a potential beneficial owner when dealing with a Broker-Dealer) who may be interested in acquiring ARCs (or, in the case of an Existing Owner thereof, an additional principal amount of ARCs).

**Record Date** with respect to the ARCs means the Applicable Number of Business Days immediately preceding each Interest Payment Date.

**Redemption Date** (whether in upper or lower case) means the date fixed for redemption.

**Securities Exchange Act** means the Securities Exchange Act of 1934, as amended.

**Sell Order** has the meaning assigned to such term in Section 104(a) of this Exhibit A.

**Special Auction Period** means any period, other than the Auction Period, which begins on an Interest Payment Date and ends on a Tuesday unless such Tuesday is not followed by a Business Day, in which case on the next succeeding day which is followed by a Business Day.

**State** means the State of Hawaii.

**Statutory Corporate Tax Rate** means, as of any date of determination, the highest tax rate bracket (expressed in decimals) now or hereafter applicable in each taxable year on the taxable income of every corporation as set forth in Section 11 of the Code or any successor section, without regard to any minimum additional tax provision or provisions regarding changes in rates during a taxable year.

**Submission Deadline** means 1:00 P.M., New York City time, on any Auction Date or any other time on any Auction Date by which Broker-Dealers are required to submit Orders to the Auction Agent as specified by the Auction Agent from time to time.

**Submitted Bid** has the meaning assigned to such term in Section 104(c)(i) of this Exhibit A.

**Submitted Hold Order** has the meaning assigned to such term in Section 104(c)(i) of this Exhibit A.

**Submitted Order** has the meaning assigned to such term in Section 104(c)(i) of this Exhibit A.

**Submitted Sell Order** has the meaning assigned to such term in Section 104(c)(i) of this Exhibit A.

**Sufficient Clearing Bids** has the meaning assigned to such term in Section 104(c)(i)(B) of this Exhibit A.

**Winning Bid Rate** has the meaning assigned to such term in Section 104(c)(i)(C) of this Exhibit A.

Section 101. Book-Entry ARCs. So long as ARCs are held by DTC, an Existing Owner may sell, transfer or otherwise dispose of its beneficial interest in ARCs only pursuant to a Bid or Sell Order placed in any Auction or to or through a Broker-Dealer, provided that in the case of all transfers other than pursuant to Auctions such Existing Owner, its Broker-Dealer or its Participant shall advise the Auction Agent of such transfer.

Section 102. Interest on ARCs. (a) Interest on the ARCs shall accrue during respective Auction Periods and shall be payable in arrears, commencing on the Initial Interest Payment Date and on each Interest Payment Date thereafter.

(b) The rate of interest on the ARCs shall be \_\_\_% per annum for the Initial Auction Period. The rate of interest on the ARCs for each subsequent Auction Period shall be the Auction Rate unless the Auction Rate exceeds the Maximum Rate, in which case the rate of interest on the respective ARCs for such Auction Period shall be the Maximum Rate, or unless the Maximum Rate shall actually be lower than the All-Hold Rate, in which case the rate of interest on the respective ARCs for such Auction Period also shall be the Maximum Rate; provided that if, on any Auction Date, an Auction is not held for any reason, then the rate of interest for ARCs for the next succeeding Auction Period shall equal the Maximum Rate on such Auction Date. Notwithstanding the foregoing, if:

(i) the ARCs are no longer held by DTC, the rate of interest on the ARCs for any Auction Period commencing after the delivery of certificates representing ARCs pursuant to the First Supplemental Indenture shall equal the Maximum Rate as of the Business Day immediately preceding the first day of such Auction Period; or

(ii) if a Payment Default occurs, Auctions will be suspended and the Applicable ARCs Rate for the Auction Period commencing on or after such Payment Default and for each Auction Period

thereafter to and including the Auction Period, if any, during which, or commencing less than the Applicable Number of Business Days after, such Payment Default is cured will equal the Default Rate.

The rate per annum at which interest is payable on the ARCs for any Auction Period is herein referred to as the "Applicable ARCs Rate." Notwithstanding anything herein to the contrary, the Applicable ARCs Rate cannot exceed the Maximum Rate.

(c) Notwithstanding anything herein to the contrary, if any ARC or portion thereof has been selected for redemption during the succeeding Auction Period, said ARC or portion thereof will not be included in the Auction immediately preceding such redemption date, and said ARC or portion thereof will continue to bear interest until the redemption date at the rate established for the Auction Period prior to said Auction.

Section 103. Payments. So long as the ARCs are held by DTC, or the nominee thereof, payment (other than at maturity) of interest and premium, if any, on, and of principal at redemption of, the ARCs shall be made to DTC by wire transfer provided proper wire instructions are received. Each Owner of ARCs, by such Owner's purchase of ARCs, appoints the Paying Agent as its agent in connection with the payment by such Owner of its share, if any, of the amounts payable to the Auction Agent and the Broker-Dealers pursuant to Section 106 of this Exhibit A.

Section 104. Auction Procedures. Auctions for ARCs shall be conducted on each respective Auction Date (other than the Auction Date immediately preceding (i) each Auction Period commencing after the ownership of the ARCs is no longer maintained in book-entry form by DTC; (ii) each Auction Period commencing after the occurrence and during the continuance of a Payment Default; or (iii) any Auction Period commencing less than the Applicable Number of Business Days after the cure of a Payment Default). If there is an Auction Agent on such Auction Date, Auctions shall be conducted in the following manner:

(a) **Orders by Existing Owners and Potential Owners.** (i) Prior to the Submission Deadline on each Auction Date:

(A) each Existing Owner of ARCs may submit to the appropriate Broker-Dealer information as to:

(I) the principal amount of Outstanding ARCs, if any, held by such Existing Owner which such Existing Owner desires to continue to hold without regard to the Auction Rate for the next succeeding Auction Period;

(II) the principal amount of Outstanding ARCs, if any, which such Existing Owner offers to sell if the Auction Rate for the next succeeding Auction Period shall be less than the rate per annum specified by such Existing Owner; and/or

(III) the principal amount of Outstanding ARCs, if any, held by such Existing Owner which such Existing Owner offers to sell without regard to the Auction Rate for the next succeeding Auction Period; and

(B) each Broker-Dealer may contact Potential Owners to determine the principal amount of ARCs which each such Potential Owner offers to purchase if the Auction Rate for the next succeeding Auction Period shall not be less than the rate per annum specified by such Potential Owner.

The communication to a Broker-Dealer of information referred to in clause (A)(I), (A)(II), (A)(III) or (B) of this paragraph (i) is hereinafter referred to as an "Order" and collectively as "Orders" and each Existing Owner and each Potential Owner placing an Order is hereinafter referred to as a "Bidder" and collectively as "Bidders"; an Order containing the information referred to in (x) clause (A) (I) of this paragraph (i) is hereinafter referred to as a "Hold Order" and collectively as "Hold Orders," (y) clause (A)(II) or (B) of this paragraph (i) is hereinafter referred to as a "Bid" and collectively as "Bids" and (z) clause (A)(III) of this paragraph (i) is hereinafter referred to as a "Sell Order" and collectively as "Sell Orders."

(ii) (A) Subject to the provisions of subsection (b) of this Section 104, a Bid by an Existing Owner shall constitute an irrevocable offer to sell:

(I) the principal amount of Outstanding ARCs held by such Owner specified in such Bid if the Auction Rate determined as provided in this Section 104 shall be less than the rate specified in such Bid; or

(II) such principal amount or a lesser principal amount of Outstanding ARCs held by such Owner to be determined as set forth in clause (D) of paragraph (i) of subsection (d) of this Section 104, if the Auction Rate determined as provided in this Section 104 shall be equal to the rate specified in such Bid; or

(III) such principal amount or a lesser principal amount of Outstanding ARCs held by such Owner to be determined as set forth in clause (C) of paragraph (ii) of subsection (d) of this Section 104 if the rate specified in such Bid shall be higher than the Maximum Interest Rate and Sufficient Clearing Bids have not been made.

(B) Subject to the provisions of subsection (b) of this Section 104, a Sell Order by an Existing Owner shall constitute an irrevocable offer to sell:

(I) the principal amount of Outstanding ARCs specified in such Sell Order; or

(II) such principal amount or a lesser principal amount of Outstanding ARCs as set forth in clause (C) of paragraph (ii) of subsection (d) of this Section 104 if Sufficient Clearing Bids have not been made.

(C) Subject to the provisions of subsection (b) of this Section 104, a Bid by a Potential Owner shall constitute an irrevocable offer to purchase:

(I) the principal amount of Outstanding ARCs specified in such Bid if the Auction Rate determined as provided in this Section 104 shall be higher than the rate specified in such Bid; or

(II) such principal amount or a lesser principal amount of Outstanding ARCs as set forth in clause (E) of paragraph (i) of subsection (d) of this Section 104 if the Auction Rate determined as provided in this Section 104 shall be equal to the rate specified in such Bid.

(b) **Submissions by Broker-Dealer to the Auction Agent.** (i) Each Broker-Dealer shall submit in writing to the Auction Agent prior to the Submission Deadline on each Auction Date all Orders obtained by such Broker-Dealer and shall specify with respect to each such Order:

(A) the name of the Bidder placing such Order;

(B) the aggregate principal amount of ARCs that are the subject of such Order;

(C) to the extent that such Bidder is an Existing Owner:

(I) the principal amount of ARCs, if any, subject to any Hold Order placed by such Existing Owner;

(II) the principal amount of ARCs, if any, subject to any Bid placed by such Existing Owner and the rate specified in such Bid; and

(III) the principal amount of ARCs, if any, subject to any Sell Order placed by such Existing Owner.

(D) to the extent such Bidder is a Potential Owner, the rate and amount specified in such Potential Owner's Bid.

(ii) If any rate specified in any Bid contains more than three figures to the right of the decimal point, the Auction Agent shall round such rate up to the next highest one thousandth (.001) of 1%.

(iii) If an Order or Orders covering all Outstanding ARCs held by any Existing Owner is not submitted to the Auction Agent prior to the Submission Deadline, the Auction Agent shall deem a Hold Order to have been submitted on behalf of such Existing Owner covering the principal amount of Outstanding ARCs held by such Existing Owner and not subject to an Order submitted to the Auction Agent.

(iv) Neither the Corporation, the Trustee nor the Auction Agent shall be responsible for any failure of a Broker-Dealer to submit an Order to the Auction Agent on behalf of any Existing Owner or Potential Owner.

(v) If any Existing Owner submits through a Broker-Dealer to the Auction Agent one or more Orders covering in the aggregate more than the principal amount of Outstanding ARCs held by such Existing Owner, such Orders shall be considered valid as follows and in the following order of priority:

(A) all Hold Orders shall be considered valid, but only up to and including in the aggregate the principal amount of ARCs held by such Existing Owner, and if the aggregate principal amount of ARCs subject to such Hold Orders exceeds the aggregate principal amount of ARCs held by such Existing Owner, the aggregate principal amount of ARCs subject to each such Hold Order shall be reduced pro rata to cover the aggregate principal amount of Outstanding ARCs held by such Existing Owner;

(B) (I) any Bid shall be considered valid up to and including the excess of the principal amount of Outstanding ARCs held by such Existing Owner over the aggregate principal amount of ARCs subject to any Hold Orders referred to in clause (A) of this paragraph (v);

(II) subject to subclause (I) of this clause (B), if more than one Bid with the same rate is submitted on behalf of such Existing Owner and the aggregate principal amount of Outstanding ARCs subject to such Bids is greater than such excess, such Bids shall be considered valid up to and including the amount of such excess and the stated amount of ARCs subject to each Bid with the same rate shall be reduced pro rata to cover the stated amount of ARCs equal to such excess;

(III) subject to subclause (I) and (II) of this clause (B), if more than one Bid with different rates is submitted on behalf of such Existing Owner, such Bids shall be considered valid first in the ascending order of their respective rates until the highest rate is reached at which such excess exists and then at such rate up to and including the amount of such excess; and

(IV) in any such event, the aggregate principal amount of Outstanding ARCs, if any, subject to Bids not valid under this clause (B) shall be treated as the subject of a Bid by a Potential Owner at the rate therein specified; and

(C) all Sell Orders shall be considered valid up to and including the excess of the principal amount of Outstanding ARCs held by such Existing Owner over the aggregate principal amount of ARCs subject to valid Hold Orders referred to in clause (A) of this paragraph (v) and valid Bids referred to in clause (B) of this paragraph (v).

(vi) If more than one Bid for ARCs is submitted on behalf of any Potential Owner, each Bid submitted shall be a separate Bid with the rate and principal amount therein specified.

(vii) Any Bid or Sell Order submitted by an Existing Owner covering an aggregate principal amount of ARCs not equal to an Authorized Denomination therefor shall be rejected and shall be deemed a Hold Order. Any Bid submitted by a Potential Owner covering an aggregate principal amount of ARCs not equal to an Authorized Denomination therefor shall be rejected.

(viii) Any Bid submitted by an Existing Owner or a Potential Owner specifying a rate lower than the All-Hold Rate shall be treated as a Bid specifying the All-Hold Rate and any such Bid shall be considered as valid and shall be selected in the ascending order of the respective rates in the Submitted Bids.

(ix) An Existing Owner that offers to purchase additional ARCs is, for purposes of such offer, treated as a Potential Owner.

(x) Any Bid specifying a rate higher than the Maximum Interest Rate will (a) be treated as a Sell Order if submitted by an Existing Owner and (b) not be accepted if submitted by a Potential Owner.

(c) Determination of Sufficient Clearing Bids, Auction Rate and Winning Bid Rate.

(i) Not earlier than the Submission Deadline on each Auction Date, the Auction Agent shall assemble all valid Orders submitted or deemed submitted to it by the Broker-Dealers (each such Order as submitted or deemed submitted by a Broker-Dealer being hereinafter referred to individually as a "Submitted Hold Order," a "Submitted Bid" or a "Submitted Sell Order," as the case may be, or as a "Submitted Order" and collectively as "Submitted Hold Orders," "Submitted Bids" or "Submitted Sell Orders," as the case may be, or as "Submitted Orders") and shall determine:

(A) the excess of the total principal amount of Outstanding ARCs over the sum of the aggregate principal amount of Outstanding ARCs subject to Submitted Hold Orders (such excess being hereinafter referred to as the "Available ARCs"); and

(B) from such Submitted Orders whether:

(I) the aggregate principal amount of Outstanding ARCs subject to Submitted Bids by Potential Owners specifying one or more rates equal to or lower than the Maximum Rate;

exceeds or is equal to the sum of:

(II) the aggregate principal amount of Outstanding ARCs subject to Submitted Bids by Existing Owners specifying one or more rates higher than the Maximum Interest Rate; and

(III) the aggregate principal amount of Outstanding ARCs subject to Submitted Sell Orders

(in the event such excess or such equality exists, other than because the sum of the principal amounts of ARCs in subclauses (II) and (III) above is zero because all of the Outstanding ARCs are subject to Submitted Hold Orders, such Submitted Bids in subclause (I) above being hereinafter referred to collectively as "Sufficient Clearing Bids"); and

(C) if Sufficient Clearing Bids have been made, the lowest rate specified in such Submitted Bids (which shall be the "Winning Bid Rate") such that if:

(I) (aa) each such Submitted Bid from Existing Owners specifying such lowest rate and (bb) all other Submitted Bids from Existing Owners specifying lower rates were rejected, thus entitling such Existing Owners to continue to hold the principal amount of ARCs subject to such Submitted Bids; and

(II) (aa) each such Submitted Bid from Potential Owners specifying such lowest rate and (bb) all other Submitted Bids from Potential Owners specifying lower rates were accepted,

the result would be that such Existing Owners described in subclause (I) above would continue to hold an aggregate principal amount of Outstanding ARCs which, when added to the aggregate principal amount of Outstanding ARCs to be purchased by such Potential Owners described in subclause (II) above, would equal not less than the Available ARCs.

(ii) Promptly after the Auction Agent has made the determinations pursuant to paragraph (i) of this subsection (c), the Auction Agent shall advise the Paying Agent of the Maximum Rate and the All-Hold Rate and the components thereof on the Auction Date and, based on such determinations, the Auction Rate for the next succeeding Auction Period (the "Auction Rate") as follows:

(A) if Sufficient Clearing Bids have been made, that the Auction Rate for the next succeeding Auction Period shall be equal to the Winning Bid Rate so determined;

(B) if Sufficient Clearing Bids have not been made (other than because all of the Outstanding ARCs are subject to Submitted Hold Orders), that the Auction Rate for the next succeeding Auction Period shall be equal to the Maximum Rate; or

(C) if all Outstanding ARCs are subject to Submitted Hold Orders, that the Auction Rate for the next succeeding Auction Period shall be equal to the All-Hold Rate.

(d) Acceptance and Rejection of Submitted Bids and Submitted Sell Orders and Allocation of ARCs.

Existing Owners shall continue to hold the principal amount of ARCs that are subject to Submitted Hold Orders, and, based on the determinations made pursuant to paragraph (i) of subsection (d) of this Section 104, Submitted Bids and Submitted Sell Orders shall be accepted or rejected and the Auction Agent shall take such other action as set forth below:

(i) If Sufficient Clearing Bids have been made, all Submitted Sell Orders shall be accepted and, subject to the provisions of paragraph (iv) of this subsection (d), Submitted Bids shall be accepted or rejected as follows in the following order of priority and all other Submitted Bids shall be rejected:

(A) Existing Owners' Submitted Bids specifying any rate that is higher than the Winning Bid Rate shall be accepted, thus requiring each such Existing Owner to sell the aggregate principal amount of ARCs subject to such Submitted Bids;

(B) Existing Owners' Submitted Bids specifying any rate that is lower than the Winning Bid Rate shall be rejected, thus entitling each such Existing Owner to continue to hold the aggregate principal amount of ARCs subject to such Submitted Bids;

(C) Potential Owners' Submitted Bids specifying any rate that is lower than the Winning Bid Rate shall be accepted, thus requiring such Potential Owner to purchase the aggregate principal amount of ARCs subject to such Submitted Bids;

(D) Each Existing Owner's Submitted Bid specifying a rate that is equal to the Winning Bid Rate shall be rejected, thus entitling such Existing Owner to continue to hold the aggregate principal amount of ARCs subject to such Submitted Bid, unless the aggregate principal amount of Outstanding ARCs subject to all such Submitted Bids shall be greater than the principal amount of ARCs (the "remaining principal amount") equal to the excess of the Available ARCs over the aggregate principal amount of ARCs subject to Submitted Bids described in clauses (B) and (C) of this paragraph (i), in which event such Submitted Bid of such Existing Owner shall be rejected in part, and such Existing Owner shall be entitled to continue to hold the principal amount of ARCs subject to such Submitted Bid, but only in an

amount equal to the aggregate principal amount of ARCs obtained by multiplying the remaining principal amount by a fraction the numerator of which shall be the principal amount of Outstanding ARCs held by such Existing Owner subject to such Submitted Bid and the denominator of which shall be the sum of the principal amount of Outstanding ARCs subject to such Submitted Bids made by all such Existing Owners that specified a rate equal to the Winning Bid Rate; and

(E) Each Potential Owner's Submitted Bid specifying a rate that is equal to the Winning Bid Rate shall be accepted but only in an amount equal to the principal amount of ARCs obtained by multiplying the excess of the aggregate principal amount of Available ARCs over the aggregate principal amount of ARCs subject to Submitted Bids described in clauses (B), (C) and (D) of this paragraph (i) by a fraction the numerator of which shall be the aggregate principal amount of Outstanding ARCs subject to such Submitted Bid and the denominator of which shall be the sum of the principal amounts of Outstanding ARCs subject to Submitted Bids made by all such Potential Owners that specified a rate equal to the Winning Bid Rate.

(ii) If Sufficient Clearing Bids have not been made (other than because all of the Outstanding ARCs are subject to Submitted Hold Orders), subject to the provisions of paragraph (iv) of this subsection (d), Submitted Orders shall be accepted or rejected as follows in the following order of priority and all other Submitted Bids shall be rejected:

(A) Existing Owners' Submitted Bids specifying any rate that is equal to or lower than the Maximum Rate shall be rejected, thus entitling such Existing Owners to continue to hold the aggregate principal amount of ARCs subject to such Submitted Bids;

(B) Potential Owners' Submitted Bids specifying any rate that is equal to or lower than the Maximum Rate shall be accepted, thus requiring each Potential Owner to purchase the aggregate principal amount of ARCs subject to such Submitted Bids; and

(C) Each Existing Owner's Submitted Bid specifying any rate that is higher than the Maximum Rate and the Submitted Sell Order of each Existing Owner shall be accepted, thus entitling each Existing Owner that submitted any such Submitted Bid or Submitted Sell Order to sell the ARCs subject to such Submitted Bid or Submitted Sell Order, but in both cases only in an amount equal to the aggregate principal amount of ARCs obtained by multiplying the aggregate principal amount of ARCs subject to Submitted Bids described in clause (B) of this paragraph (ii) by a fraction the numerator of which shall be the aggregate principal amount of Outstanding ARCs held by such Existing Owner subject to such Submitted Bid or Submitted Sell Order and the denominator of which shall be the aggregate principal amount of Outstanding ARCs subject to all such Submitted Bids and Submitted Sell Orders.

(iii) If all Outstanding ARCs are subject to Submitted Hold Orders, all Submitted Bids shall be rejected.

(iv) If, as a result of the procedures described in paragraph (i) or (ii) of this subsection (d), any Existing Owner would be entitled or required to sell, or any Potential Owner would be entitled or required to purchase, a principal amount of ARCs that is not equal to an Authorized Denomination therefor the Auction Agent shall, in such manner as it shall, in its sole discretion, determine, round up or down the principal amount of ARCs to be purchased or sold by any Existing Owner or Potential Owner so that the principal amount of ARCs purchased or sold by each Existing Owner or Potential Owner shall be equal to an Authorized Denomination therefor, even if such allocation results in one or more of such Potential Owners not purchasing any ARCs.

(e) Based on the results of each Auction, the Auction Agent shall determine the aggregate principal amount of ARCs to be purchased and the aggregate principal amount of ARCs to be sold by Potential Owners and Existing Owners on whose behalf each Broker-Dealer submitted Bids or Sell Orders and, with respect to each Broker-Dealer, to the extent that such aggregate principal amount of ARCs to be sold differs from such aggregate principal amount of ARCs to be purchased, determine to which other Broker-Dealer or Broker-Dealers acting for one or more purchasers such Broker-Dealer shall deliver, or from which other Broker-Dealer or Broker-Dealers acting for one or more sellers such Broker-Dealer shall receive, as the case may be, ARCs.

Section 105. Certain Orders Not Permitted. The Corporation may not submit an Order in any Auction. The Corporation shall not purchase or otherwise acquire ARCs unless the Corporation redeems or otherwise cancels such ARCs on the day of any purchase. The Auction Agent shall have no duty or liability in monitoring or enforcing compliance with this Section 105.

Section 106. Payment of Service Charges; Notice of Payment Defaults and Cures. (a) The Corporation shall pay to the Auction Agent on behalf of the Owners of the ARCs (i) when due, an amount equal to the Auction Agent Fee as calculated in the Auction Agreement and (ii) when due, an amount equal to the Broker-Dealer Fee as calculated in the Broker-Dealer Agreement.

(b) By 12:30 P.M. New York City time on the Business Day immediately succeeding each Interest Payment Date, the Trustee will determine if a Payment Default has occurred. If a Payment Default has occurred, the Trustee shall notify the Auction Agent and Broker-Dealer by 1:00 P.M. New York City time on said date. If a Payment Default has been cured, the Trustee shall so notify the Auction Agent and the Broker-Dealer by 5:00 P.M. New York City time on the day such Payment Default is cured.

Section 107. Calculation of the Rates. The Auction Agent shall calculate the Maximum Interest Rate, the Maximum Rate, the All-Hold Rate, and the 'AA' Financial Rate on each Auction Date. The determination by the Auction Agent of each of such rates will (in the absence of manifest error) be final and binding upon all Owners of ARCs and upon all other parties. If the ownership of the ARCs is no longer maintained in book-entry form by DTC, the Paying Agent shall calculate the Maximum Rate on the Business Day immediately preceding the first day of each Auction Period commencing after the delivery of certificates representing the ARCs pursuant to Subsection 101(c) of this Exhibit A. If a Payment Default shall have occurred, the Paying Agent shall calculate the Default Rate on the first day of (i) each Auction Period commencing after the occurrence and during the continuance of such Payment Default and (ii) any Auction Period commencing less than the Applicable Number of Business Days after the cure of any Payment Default.

Section 108. Computation of Interest. The amount of interest distributable to Owners of ARCs in respect of each \$25,000 in principal amount thereof for any Auction Period or part thereof shall be calculated by applying the Applicable ARCs Rate for such Auction Period or part thereof to the principal amount of \$25,000, multiplying such product by the actual number of days in the Auction Period or part thereof concerned divided by 365 or 366, as applicable, and truncating the resultant figure to the nearest one cent. Interest on the ARCs shall be computed by the Trustee on the basis of a 365-day year for the number of days actually elapsed; except that for any such calculation with respect to an Interest Payment Date occurring after January 1 of a leap year through December 31 of such leap year, such interest (for any day occurring during such period) shall be computed on the basis of a 366-day year period. In the event an Interest Payment Date occurs in any Auction Period on a date other than the first day of such Auction Period, the Trustee, after confirming the calculation required above, shall calculate the portion of the Interest Amount payable on such Interest Payment Date and the portion payable on the next succeeding Interest Payment Date. The Trustee shall make the calculation required in this Section 108 not later than the close of business on each Auction Date.

Section 109. Notification of Rates, Amounts, and Payment Dates. (a) The Trustee shall determine the aggregate amount of interest distributable on the next succeeding Interest Payment Date to the Owners of the ARCs. So long as the ARCs are held by DTC, the Trustee shall advise DTC of each Record Date for the ARCs at least two Business Days prior thereto.

(b) Promptly after the Date of Delivery and in any event at least 10 days prior to each Interest Payment Date thereafter, the Trustee shall:

(i) so long as no Payment Default has occurred and is continuing and the ownership of the ARCs is held by DTC, confirm the Auction Agent's determination of (A) the date of such next Interest Payment Date and (B) the amount payable to the Auction Agent on each Interest Payment Date pursuant to Section 106 of this Exhibit A and notify the Auction Agent of any discrepancy therein; and

(ii) advise DTC, so long as the ownership of the ARCs is held by DTC, of the Applicable ARCs Rate and the interest amount calculated in accordance with Section 108 above in respect of the next succeeding Interest Payment Date.

In the event that any day that is scheduled to be an Interest Payment Date shall be changed after the Paying Agent shall have given the notice referred to in clause (i) of the preceding sentence, not later than 9:15 A.M., New York City time, on the Business Day next preceding the earlier of the new Interest Payment Date or the old Interest Payment Date, the Trustee shall, by such means as the Trustee deems practicable, give notice of such change to the Auction Agent, so long as no Payment Default has occurred and is continuing and the ownership of the ARCs is held by DTC.

Section 110. Adjustment in Percentages. (a) The Market Agent shall adjust the percentage used in determining the All-Hold Rate, the Applicable Percentage used in determining the Maximum Rate and the Applicable Percentage of the Kenny Index used in determining the Default Rate, if any such adjustment is necessary, in the judgment of the Market Agent, to reflect any Change of Preference Law such that ARCs paying the Maximum Rate, ARCs paying the All-Hold Rate and ARCs paying the Default Rate shall have substantially equal market values before and after such Change of Preference Law. Prior to any such adjustment, the Corporation shall give notice thereof to each rating agency then rating the ARCs, *provided, however*, no such adjustment shall be made unless such adjustment will not adversely affect any rating on the ARCs. In making any such adjustment, the Market Agent shall take the following factors, as in existence both before and after such Change of Preference Law, into account:

- (i) short-term taxable and tax-exempt market rates and indices of such short-term rates;
- (ii) the market supply and demand for short-term tax-exempt securities;
- (iii) yield curves for short-term and long-term tax-exempt securities or obligations having a credit rating that is comparable to the ARCs;
- (iv) general economic conditions; and
- (v) economic and financial factors present in the securities industry that may affect or that may be relevant to the ARCs.

(b) The Market Agent shall effectuate an adjustment in the percentage used in determining the All-Hold Rate, the Applicable Percentage used in determining the Maximum Rate and the Applicable Percentage of the Kenny Index used to determine the Default Rate pursuant to subsection (a) of this Section 110 by delivering to the Corporation, the ARCs and the Auction Agent at least 10 days prior to the Auction Date on which the Market Agent desires to effect such change (i) a favorable opinion of nationally recognized bond counsel to the effect that such adjustment is authorized by the First Supplemental Indenture, is permitted under State law and will not have an adverse effect on the exclusion of interest on the ARCs from gross income for federal income tax purposes, and (ii) a certificate authorizing the adjustment of the percentage used in determining the All-Hold Rate, the Applicable Percentage used in determining the Maximum Rate and the Applicable Percentage of the Kenny Index used to determine the Default Rate, which shall be specified in such certificate.

Section 111. Market Agent. The Trustee shall enter into a Market Agent Agreement with UBS Financial Services Inc., as the initial Market Agent. The Market Agent shall serve as such under the terms and provisions hereof and of the Market Agent Agreement. The Market Agent, including any successor appointed pursuant hereto, shall be a member of the National Association of Securities Dealers, Inc. having capitalization of at least \$25,000,000, and be authorized by law to perform all the duties imposed upon it by the First Supplemental Indenture, and the Market Agent Agreement. The Market Agent may be removed at any time by the Paying Agent, acting at the direction of the Corporation, provided that such removal shall not take effect until the appointment of a successor Market Agent. The Market Agent may resign upon 30 days' written notice delivered to the Corporation and the Trustee. The Corporation shall use its best efforts to appoint a successor Market Agent that is a qualified institution, effective as of the effectiveness of any such resignation or removal. Notwithstanding that the Market

Agent is the agent of the Trustee under the Market Agent Agreement, the Trustee shall not be liable in any way for any action taken, suffered, or omitted, or for any error of judgment made by the Market Agent, whether in the performance of its duties under the Market Agent Agreement or otherwise.

Section 112. Auction Agent. (a) Wilmington Trust Company shall serve as the initial Auction Agent for the ARCs. The Trustee is hereby directed to enter into an agreement with the Auction Agent which shall provide as follows: The Auction Agent shall be (i) a bank or trust company duly organized under the laws of the United States of America or any state or territory thereof having its principal place of business in the Borough of Manhattan, The City of New York, and having a combined capital stock, surplus and undivided profits of at least \$15,000,000 or (ii) a member of the National Association of Securities Dealers, Inc., having a capitalization of at least \$15,000,000 and, in either case, authorized by law to perform all the duties imposed upon it hereunder and under the Auction Agreement. The Auction Agent may resign and be discharged of the duties and obligations created by the First Supplemental Indenture by giving at least 90 days' written notice to the Corporation, the Trustee and the Market Agent (30 days' written notice if the Auction Agent has not been paid its fee for more than 30 days after such fee is due). The Auction Agent may be removed at any time by the Trustee if the Auction Agent is an entity other than the Trustee, acting at the direction of the Corporation or the Insurer, by an instrument signed by the Trustee and filed with the Auction Agent, the Corporation, the Insurer and the Market Agent upon at least 90 days' notice; provided that, if required by the Market Agent, an agreement in substantially the form of the Auction Agreement shall be entered into with a successor Auction Agent. If the Auction Agent and the Trustee are the same entity, the Auction Agent may be removed as described above, with the Corporation acting in lieu of the Trustee.

(b) In the event that the Auction Agent shall resign or be removed or dissolved, or if the property or affairs of the Auction Agent shall be taken under the control of any state or federal court or administrative body because of bankruptcy or insolvency, or for any other reason, the Corporation shall use its best efforts to appoint a successor as Auction Agent acceptable to the Insurer, and the Trustee shall thereupon enter into an Auction Agreement with such successor.

(c) The Auction Agent shall be acting as agent for the Trustee and the Corporation in connection with Auctions. In the absence of bad faith or negligence on its part, the Auction Agent shall not be liable for any action taken, suffered or omitted or for any error of judgment made by it in the performance of its duties under the Auction Agreement and shall not be liable for any error of judgment made in good faith unless the Auction Agent shall have been negligent in ascertaining (or failing to ascertain) the pertinent facts necessary to make such judgment.

(d) Notwithstanding that the Auction Agent is the agent of the Paying Agent hereunder and under the Auction Agreement, the Trustee shall not be liable in any way for any action taken, suffered or omitted, or for any error of judgment made by the Auction Agent, whether in the performance of its duties under the Auction Agreement or otherwise, subject to the Auction Agreement.

Section 113. Broker-Dealers. (a) The Auction Agent shall enter into a Broker-Dealer Agreement with UBS Financial Services Inc., as the initial Broker-Dealer. The Market Agent may from time to time propose to the Corporation one or more additional persons to serve as Broker-Dealers under Broker-Dealer Agreement.

(b) Any Broker-Dealer may be removed at any time by the Corporation, but there shall, at all times, be at least one Broker-Dealer appointed and acting as such for ARCs.

Section 114. Changes in Auction Date. (a) The Market Agent:

(i) in order to conform with then current market practice with respect to similar securities, shall; or

(ii) in order to accommodate economic and financial factors that may affect or be relevant to the day of the week constituting an Auction Date and the interest rate borne on the ARCs and with the written consent of the Corporation, may specify an earlier Auction Date (but in no event more than five Business Days earlier) than the Auction Date that would otherwise be determined in accordance with the definition of "Auction Date" in Section 100 of this Exhibit A with respect to one or more specified Auction Periods. The Corporation shall

not consent to such change in the Auction Date unless the Corporation shall have received from the Market Agent not less than three days nor more than 20 days prior to the effective date of such change a written request for consent together within a certificate demonstrating the need for change in reliance on such factors. When the Corporation consents, the Market Agent shall provide notice of any determination to specify an earlier Auction Date for one or more Auction Periods by means of a written notice delivered at least 10 days prior to the proposed changed Auction Date to the Trustee, the Auction Agent, the Corporation, and DTC.

(c) In connection with any change described in this Section 114, the Auction Agent shall provide such further notice to such parties as is specified in the Auction Agreement.

(d) No change shall be made to the Auction Period or Auction Date unless the Corporation shall give notice thereof to each rating agency then rating the ARCs and the Insurer, and no change shall be made unless such change will not adversely affect any rating on the ARCs.

Section 115. Credit Ratings. The Corporation shall take all reasonable action necessary to enable at least one nationally recognized statistical rating organization (as that term is used in the rules and regulations of the Commission under the Securities Exchange Act) to provide credit ratings for the ARCs.

Section 116. Notices. The Market Agent shall provide the Paying Agent and, so long as no default under the Resolution has occurred and is continuing and the ownership of the ARCs is held by DTC, the Auction Agent with notice of any change in the Maximum Interest Rate calculation.

Section 117. Notice of Payment Default. (a) So long as the ownership of the ARCs is held by DTC, upon the occurrence of a Payment Default the Trustee shall immediately send a notice thereof to the Auction Agent and Market Agent by telecopy or similar means.

(b) So long as the ownership of the ARCs is held by DTC, the Trustee shall immediately send notice to the Auction Agent by telecopy or similar means if a Payment Default is cured.

Section 118. Redemption Dates and Prices. The outstanding ARCs are subject to optional and mandatory redemption in accordance with the First Supplemental Indenture.

**(THIS PAGE INTENTIONALLY LEFT BLANK)**



