HAWAIIAN HOLDINGS INC
Form 10-K
March 16, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-K

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

(Mark One)

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2006

or

o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from to .

Commission file number 1-31443

HAWAIIAN HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**71-0879698**
(State or other jurisdiction of incorporation or organization)	(I.R.S. employer identification no.)
3375 Koapaka Street, Suite G-350, Honolulu, Hawaii	**96819**
(Address of principal executive offices)	(Zip code)

Registrant s telephone number, including area code: (808) 835-3700

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	**Name of each exchange on which registered**
Common Stock ($.01 par value)	American Stock Exchange and NYSE Area

Securities registered pursuant to Section 12(g) of the Act: **None**

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes o No x

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No o

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant s knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer o Accelerated filer x Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Exchange Rule Act 12b-2). Yes o No x

The aggregate market value of the voting and non-voting common equity stock held by non-affiliates of the Registrant was approximately $158,283,308, computed by reference to the closing sale price of the Common Stock on the American Stock Exchange, on June 30, 2006, the last business day of the Registrant s most recently completed second fiscal quarter.

As of February 28, 2007, 46,583,914 shares of Common Stock of the Registrant were outstanding.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant s Proxy Statement for Annual Meeting of Stockholders to be held on May 30, 2007 will be incorporated by reference into Part III of this Form 10-K.

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This annual report on Form 10-K contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that reflect our current views with respect to certain current and future events and financial performance. These forward-looking statements are and will be, as the case may be, subject to many risks, uncertainties and factors relating to our operations and business environments which may cause our actual results to be materially different from any future results, expressed or implied, in these forward-looking statements.

Factors that could cause actual results to differ materially from these forward-looking statements include, but are not limited to, the following:

- aviation fuel costs;
- Hawaiian s dependence on tourist travel;
- competition in the interisland market;
- the effects of seasonality and cyclicality;
- the concentration of our business in Hawaii;
- the competitive advantages held by network carriers in the transpacific markets;
- the possibility of new entrants into the transpacific market;
- competitive pressures on pricing (particularly from lower-cost competitors);
- demand for transportation in the markets in which Hawaiian operates;
- the impact of our substantial financial and operating leverage;
- our ability to comply with financial covenants;
- the competitiveness of our labor costs;
- our relationship with our employees and possible work stoppages;
- our ability to attract, motivate and/or retain key executives and other employees;
- increasing dependence on technologies to operate Hawaiian s business;
- our reliance on other companies for facilities and services (including, without limitation, aircraft maintenance, code sharing, reservations, computer services, frequent flyer programs, passenger processing, ground facilities, baggage and cargo handling and personnel training);
- Hawaiian s fleet concentration in out-of-production Boeing 717-200 aircraft;
- the impact of indebtedness on our financial condition and results of operations;
- the effects of any hostilities or act of war (in the Middle East or elsewhere) or any terrorist attack;
- increases in aircraft maintenance costs due to the aging and increased utilization of our fleet, and the possible unavailability of aircraft;

- bankruptcies in the airline industry and the possible negative impact such bankruptcies might have on fares and excess capacity;

- government legislation and regulation, including the Aviation and Transportation Security Act (ATSA) and other such regulations stemming from the September 11, 2001 or future terrorist attacks;

- changes that may be required by the Federal Aviation Administration (FAA) or other regulators to Hawaiian s aircraft or operations;
- the impact of possible aircraft incidents;
- the impact of possible outbreaks of disease;
- economic conditions generally;
- changes in competition and capacity in all of the markets we serve;
- changes in the level of fares we can charge and remain competitive;
- the cost and availability of insurance, including aircraft insurance;
- security-related costs;
- consumer perceptions of the services of Hawaiian; and
- other risks and uncertainties set forth from time to time in our reports to the Securities and Exchange Commission, included under Risk Factors in this annual report.

We undertake no obligation to publicly update or revise any forward-looking statements to reflect events or circumstances that may arise after the date of this annual report.

PART I

ITEM 1. BUSINESS.

Overview

Hawaiian Holdings, Inc. (the Company, Holdings, we, us and our) is a holding company whose primary asset is the sole ownership of all issued and outstanding shares of common stock of Hawaiian Airlines, Inc. (Hawaiian). Based on the total number of miles flown by revenue passengers in 2006, Hawaiian was the largest airline headquartered in Hawaii and the seventeenth largest domestic airline in the United States. Hawaiian offers daily service on transpacific routes between Hawaii and Los Angeles, Sacramento, San Diego, San Francisco, San Jose, Las Vegas, Phoenix, Portland, and Seattle, as well as daily service among the Hawaiian Islands, and additional service to Australia, American Samoa and Tahiti. Charter service is also provided from Honolulu to Anchorage, Alaska. As of December 31, 2006, Hawaiian operated a fleet of 11 Boeing 717-200 aircraft for its interisland routes and 15 Boeing 767-300 aircraft for its transpacific, South Pacific and charter routes.

Hawaiian was originally incorporated in January 1929 under the laws of the Territory of Hawaii and became our indirect wholly-owned subsidiary pursuant to a corporate restructuring that was consummated in August 2002. Hawaiian became a Delaware corporation and our direct wholly-owned subsidiary in June 2005 pursuant to a short-form merger described in greater detail below under Consummation of Hawaiian s Joint Plan of Reorganization. We were incorporated in April 2002 under the laws of the State of Delaware.

General information about us, including our corporate governance guidelines and the charters for the committees of our Board of Directors, can be found at *http://www.hawaiianair.com/about/*. Our Board of Directors has adopted a code of ethics entitled Code of Business Ethics and Conduct that applies to all of our employees, officers and directors. Our code of ethics can be found at *http://www.hawaiianair.com/about/*. Our annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, as well as any amendments and exhibits to those reports, are available free of charge through our website as soon as reasonably practicable after we file them with, or furnish them to, the Securities and Exchange Commission (SEC). Information on our website is not incorporated into this Annual Report on Form 10-K or our other securities filings and is not a part of them.

Consummation of Hawaiian s Joint Plan of Reorganization

On March 21, 2003, Hawaiian filed a voluntary petition for reorganization under Chapter 11 of the U.S. Bankruptcy Code in the U.S. Bankruptcy Court for the District of Hawaii. We did not file for relief under Chapter 11 of the Bankruptcy Code. On May 30, 2003, a bankruptcy trustee was selected to serve in connection with the Chapter 11 filing and operate Hawaiian, which thereafter operated its business under the jurisdiction of the bankruptcy court and in accordance with the applicable provisions of the bankruptcy code and orders of the bankruptcy court until June 2, 2005, the effective date of Hawaiian s joint plan of reorganization as discussed further below. The appointment of the bankruptcy trustee effectively served to divest operational and financial control of Hawaiian from our officers and directors, and severed the availability of funds needed to support our efforts to meet our ongoing financial and other obligations, including our reporting requirements under the Securities Exchange Act of 1934, as amended.

On March 11, 2005, we, together with the bankruptcy trustee, the unsecured creditors of Hawaiian, our wholly-owned subsidiary formerly known as HHIC, Inc., a Delaware corporation (HHIC), and RC Aviation LLC (RC Aviation), a principal stockholder of the Company, sponsored the Third Amended Joint Plan of Reorganization (the Joint Plan) to provide for Hawaiian to emerge from bankruptcy. The Joint Plan provided for payment in full of all allowed claims, including unsecured claims. The Joint Plan also provided for the merger of Hawaiian Airlines, Inc., a Hawaii corporation, with and into HHIC, with HHIC as the surviving entity immediately changing its name to Hawaiian Airlines, Inc. As used in this

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report, the term Hawaiian refers to the predecessor company for all periods prior to the HHIC merger and the successor company for all periods subsequent to the merger. We retained our equity interest in Hawaiian; however, in connection with the Joint Plan, we issued shares of our common stock to creditors of Hawaiian to help fund the Joint Plan, resulting in a dilution of the ownership interest of our common stockholders.

The Joint Plan was consummated on June 2, 2005 (the Effective Date), at which point we regained control of Hawaiian. Except as otherwise provided in the Joint Plan, on such date, all property of the estate of Hawaiian as an entity in bankruptcy vested in Hawaiian. Hawaiian s emergence from bankruptcy was accounted for as a business combination, with the assets and liabilities of Hawaiian recorded in our consolidated financial statements at their fair values as of June 2, 2005 and the results of Hawaiian s operations included in our results of operations from that date.

The Joint Plan provided for the settlement of the allowed claims under Hawaiian s bankruptcy case by a combination of $126.4 million in cash payments and the issuance of approximately 14.1 million shares of our common stock. We also assumed long-term payment obligations of $32.9 million. We incurred substantial indebtedness to fund the Joint Plan including the issuance of $60.0 million of 5.0% unsecured subordinated convertible notes due June 1, 2010 (the Notes), a $50.0 million variable interest rate senior secured credit facility (of which $25.0 million was drawn in the form of a three-year term loan at June 2, 2005) and a $25.0 million 10.0% subordinated secured three-year term loan.

Flight Operations

Our flight operations are based in Honolulu, Hawaii. In January 2007, we operated approximately 152 scheduled and charter flights per day with:

- Daily service on our transpacific routes between Hawaii and Los Angeles, Sacramento, San Diego, San Jose, and San Francisco, California; Las Vegas, Nevada; Phoenix, Arizona; Portland, Oregon and Seattle, Washington;
- Daily service on our interisland routes among the four major islands of the State of Hawaii;
- Scheduled service on our South Pacific routes between Hawaii and Pago Pago, American Samoa, and Papeete, Tahiti and Sydney, Australia;
- Public charter service between Honolulu and Anchorage, Alaska; and
- Other ad hoc charters.

Fuel

Our operations and financial results are significantly affected by the availability and price of jet fuel. The following table sets forth statistics about Hawaiian s aircraft fuel consumption and cost, including the impact of Hawaiian s fuel hedging program, for the years 2006 through 2004.

Year	**Gallons consumed (in thousands)**	**Total cost, including taxes**	**Average cost per gallon**	**Percent of operating expenses**
2006	114,236	$ 241,611	$ 2.12	27.3
2005	111,220	$ 201,157	$ 1.81	24.6
2004	104,911	$ 135,866	$ 1.30	19.3

As illustrated by the table above, fuel costs constitute a significant portion of Hawaiian s operating expense. Approximately 55% of Hawaiian s fuel is based on Singapore jet fuel prices; the remaining 45% is

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based on U.S. West Coast jet fuel prices. Fuel prices are volatile; based on gallons expected to be consumed in 2007, for every one cent change in the cost per gallon of jet fuel, Hawaiian s annual fuel expense increases or decreases by approximately $1.3 million. Jet fuel costs represented 27.3% of Hawaiian s operating expenses in 2006. The cost of jet fuel is influenced by international political and economic circumstances, such as unrest in Iraq and other conflicts in the Middle East, OPEC production curtailments, disruption of oil imports, increased demand by China, India and other developing countries, environmental concerns, weather and other unpredictable events. Further increases in jet fuel prices or disruptions in fuel supplies, whether as a result of natural disasters or otherwise, could have a material adverse effect on our results of operations, financial position or liquidity.

Hawaiian purchases aircraft fuel at prevailing market prices, but seeks to manage market risk through execution of a hedging strategy. From time to time, Hawaiian has entered into various derivative instruments to hedge a portion of our anticipated jet fuel requirements. In September 2004, Hawaiian resumed a jet fuel hedging program which utilized forward heating oil contracts in order to moderate market risks and mitigate its financial exposure to fluctuations in its cost of jet fuel. In May 2005, Hawaiian terminated its heating oil contracts and entered into jet fuel forward contracts with a single counterparty to hedge a portion of its fuel consumption requirements. Jet fuel forward contracts are not traded on commodities exchanges due to the limited market for such contracts. However, they tend to have a higher level of effectiveness than do heating oil forward contracts. As of December 31, 2006, our fuel hedges outstanding were in a loss position. The fair value of our obligation related to these contracts was $1.1 million. As of February 2007, Hawaiian had hedged approximately 44%, 23%, 4% and 1% of its anticipated aircraft fuel consumption for the first, second, third and fourth quarters of 2007, respectively.

Aircraft Maintenance

Our aircraft maintenance programs consist of a series of phased or continuous checks for each aircraft type. These checks are performed at specified intervals measured by calendar months, time flown or by the number of takeoffs and landings, or cycles, operated. In addition, we perform inspections, repairs and modifications of our aircraft in response to Federal Aviation Administration (FAA) directives. Checks range from walk around inspections before each flight departure to major overhauls of the airframes which can take several weeks to complete. Aircraft engines are subject to phased maintenance programs designed to detect and remedy potential problems before they occur. The service lives of certain airframe and engine parts and components are time or cycle controlled, and such parts and components are replaced or refurbished prior to the expiration of their time or cycle limits.

Code Sharing and Other Alliances

We have marketing alliances with other airlines that provide reciprocal frequent flyer mileage accrual and redemption privileges and code sharing on certain flights (one carrier placing its name and flight numbers, or code, on flights operated by the other carrier). We have code sharing agreements with American Airlines, American Eagle, Continental Airlines, Harmony Airways, Island Air, Korean Air, Northwest Airlines and US Airways. We also participate in the frequent flyer programs of American Airlines, American Eagle, Continental Airlines, Island Air, Northwest Airlines, US Airways, Virgin Atlantic Airways and Virgin Blue. We also have a code share and reciprocal frequent flyer agreement with Alaska Airlines that expires on April 30, 2007. These programs enhance our revenue opportunities by:

- providing our customers more value by offering easier access to more travel destinations and better mileage accrual/redemption opportunities;
- gaining access to more connecting traffic from other airlines; and
- providing members of our alliance partners frequent flyer programs an opportunity to travel on our system while earning mileage credit in the alliance partners programs.

Although these programs and services increase our ability to be more competitive, they also increase our reliance on third parties.

Marketing

In an effort to reduce our reliance on travel agencies and lower our distribution costs, we continue to pursue e-commerce initiatives. We currently utilize web-fare discounts to improve service to our customers and to reduce our distribution costs. In addition, we provide internet check-in and self-service kiosks to improve the customer check-in process. Our website, www.HawaiianAirlines.com, offers our customers information on our flight schedules, our *HawaiianMiles* frequent flyer program, the ability to book reservations on our flights or connecting flights with any of our code share partners, the status of our flights as well as the ability to purchase tickets or travel packages. We also publish fares with web-based travel services such as Orbitz, Travelocity, Expedia, Hotwire and Priceline. These comprehensive travel planning websites provide customers with convenient online access to airline, hotel, car rental and other travel services.

On October 19, 2006, our website began to allow the general public to purchase gift certificates via Hawaiian Gifts, LLC (Hawaiian Gifts), a newly created subsidiary of the Company. In addition, Hawaiian Gifts also sells gift cards which are available at supermarkets in Hawaii and West Coast regions that we serve. These gift certificates and gift cards are to be redeemed for air transportation on Hawaiian.

Frequent Flyer Program

The *HawaiianMiles* frequent flyer program was initiated in 1983 to encourage and develop customer loyalty. *HawaiianMiles* allows passengers to earn mileage credits by flying with us and our partner carriers. In addition, members earn mileage credits for patronage with our other program partners, including hotels, car rental firms, credit card issuers and long distance telephone companies, pursuant to our exchange partnership agreements. We also sell mileage credits to other companies participating in the program.

HawaiianMiles members have a choice of various awards based on accumulated mileage credits, with most of the awards being for free air travel on Hawaiian. Travel awards range from a 5,000 mile award, which is redeemable for a SuperSaver one-way interisland flight, to a 105,500 mile award, which is redeemable for an Anytime one-way first class travel between the mainland U.S. and Sydney, Australia. In January 2006, we amended the HawaiianMiles program to allow members increased flexibility in redeeming their mileage credits for travel on Hawaiian.

Competition

Transpacific

We face multiple competitors on our transpacific routes including major network carriers such as American Airlines, Continental Airlines, Northwest Airlines, Delta Air Lines, United Airlines (United) and US Airways. ATA Airlines (ATA), a low-cost carrier, offers scheduled service to Hawaii with Southwest Airlines as a code share partner on its routes. Aloha Airlines provides scheduled service to multiple mainland cities from Hawaii, and various charter companies also provide unscheduled service to Hawaii mostly under public charter arrangements. We believe that transpacific competition is primarily based on fare levels, flight frequency, on-time performance and reliability, name recognition, schedule, affiliations, frequent flyer programs, customer service, aircraft type and in-flight service.

South Pacific

Currently, we are the only provider of nonstop service between Honolulu and each of Pago Pago, American Samoa, and Papeete, Tahiti. We also operate roundtrip flights between Honolulu and Sydney, Australia, competing directly against Qantas Airways, its low-cost affiliate Jetstar and Air Canada on this route.

Interisland

Interisland routes are served by several carriers including Aloha Airlines, Island Air, Pacific Wings and a number of air taxi companies. Also, Mesa Airlines, through its *go!* operating division, began interisland service in June 2006. In January 2007, we operated approximately 120 daily interisland flights, which represented approximately 36% of the total daily interisland flights operated by all carriers in that month. We believe that interisland competition is primarily based on fare levels, flight frequency, on-time performance and reliability, name recognition, affiliations, frequent flyer programs, customer service and aircraft type.

Employees

As of December 31, 2006, Hawaiian had 3,454 active employees, consisting of 1,153 flight deck and cabin crew members, 933 customer service representatives, 573 ground support personnel, 246 maintenance and engineering personnel and 549 general management, administrative and clerical personnel. Approximately 84% of our employees are covered by labor agreements with the following organized labor groups:

Represented by	Employee Group	Agreement amendable on(*)
Air Line Pilots Association (ALPA)	Flight deck crew members	June 30, 2007
Association of Flight Attendants (AFA)	Cabin crew members	November 1, 2007
International Association of Machinists and Aerospace Workers (IAM)	Maintenance and engineering personnel	March 31, 2008
IAM	Customer service representatives	March 31, 2008
Network Engineering Group (NEG)	Communications personnel	March 31, 2008
Transport Workers Union (TWU)	Flight dispatch personnel	November 30, 2007

(*) Our relations with our labor organizations are governed by the Title II of the Railway Labor Act of 1926, pursuant to which act the collective bargaining agreements between us and these organizations do not expire but instead become amendable as of a certain date if either party wishes to modify the terms of the agreement.

Seasonality

Our operations and financial results are subject to substantial seasonal and cyclical volatility, primarily due to leisure and holiday travel patterns. Hawaii is a popular vacation destination for travelers. Demand levels are typically weaker in the first quarter of the year with stronger demand periods occurring during June, July, August and December. During weaker demand periods, we may adjust our flight availability to obtain a profitable passenger load factor, or utilize discounted fare pricing strategies to increase our traffic volume, which may involve higher ticket discounts during these periods.

Customers

Our business is not dependent upon a single customer, or a few customers, the loss of any one or more of which would have a material adverse effect on our business.

Regulation

Our business is subject to extensive and evolving federal, state, local and transportation laws and regulations in the U.S. Many of these agencies regularly examine our operations to monitor compliance with applicable laws and regulations. Governmental authorities can enforce compliance with applicable laws and regulations and obtain injunctions or impose civil or criminal penalties in case of violations.

We cannot guarantee that we will be able to obtain or maintain necessary governmental approvals. Once obtained, operating permits are subject to modification and revocation by the issuing agencies. Compliance with these and any future regulatory requirements could require us to make significant capital and operating expenditures. However, most of these expenditures are made in the normal course of business and do not place us at any competitive disadvantage. The primary U.S. federal statutes affecting our business are summarized below:

Industry Regulations

As a certificated air carrier, we and all other U.S. domestic airlines are subject to the regulatory jurisdiction of the U.S. Department of Transportation (DOT) and the FAA. The DOT has jurisdiction over certain aviation matters such as a carrier s certificate of public convenience and necessity, international routes and fares, consumer protection policies including baggage liability and denied-boarding compensation, and unfair competitive practices as set forth in the Airline Deregulation Act of 1978. We operate under a Certificate of Public Convenience and Necessity issued by the DOT (authorizing us to provide commercial aircraft service) as well as a Part 121 Scheduled Carrier Operating Certificate issued by the FAA. These certificates may be altered, amended, modified or suspended by the DOT if public convenience and necessity so require, or may be revoked for intentional failure by the holder of the certificate to comply with the terms and conditions of a certificate. The FAA has regulatory jurisdiction over flight operations generally, including equipment, ground facilities, security systems, maintenance and other safety matters. Pursuant to these regulations, we have established, and the FAA has approved, a maintenance program for each type of aircraft we operate that provides for the ongoing maintenance of our aircraft, ranging from frequent routine inspections to major overhauls. To assure compliance with its operational standards, the FAA requires air carriers to obtain operating, airworthiness and other certificates, which may be suspended or revoked for cause. The FAA also conducts safety audits and has the power to impose fines and other sanctions for violations of aviation safety and security regulations. Like other carriers, we are subject to inspections by the FAA in the normal course of business and on a routine basis.

Maintenance Directives

The FAA approves all airline maintenance programs, including modifications to the programs. In addition, the FAA licenses the mechanics who perform the inspection, repairs and overhauls, as well as the inspectors who monitor the work.

The FAA frequently issues airworthiness directives, often in response to specific incidents or reports by operators or manufacturers, requiring operators of specified equipment types to perform prescribed inspections, repairs or modifications within stated time periods or numbers of cycles. In the last several years, the FAA has issued a number of maintenance directives and other regulations relating to, among other things, cargo compartment fire detection/suppression systems, collision avoidance systems, airborne windshear avoidance systems, noise abatement and increased inspection requirements. We cannot predict what new airworthiness directives will be issued and what new regulations will be adopted, or how our businesses will be affected by any such directives or regulations. We expect that we may incur expenses to comply with new airworthiness directives and regulations.

We believe we are in compliance with all requirements necessary to be in good standing with our air carrier operating certificate issued by the FAA. A modification, suspension or revocation of any of our FAA authorizations or certificates would have a material adverse effect on our operations.

Airport Security

The Aviation and Transportation Security Act (ATSA), enacted in November 2001, created the Transportation Security Administration (TSA), which is part of the Department of Homeland Security (DHS) and is responsible for aviation security. The ATSA mandates that the TSA provide for the screening of all passengers and property, including mail, cargo, carry-on and checked baggage, and other articles that will be carried aboard a passenger aircraft. Under the ATSA, substantially all security screeners at airports are now federal employees, and significant other elements of airline and airport security are now overseen and performed by federal employees, including security managers, law enforcement officers and federal air marshals. The ATSA also provides for increased security on flight decks of aircraft and requires federal air marshals to be present on certain flights, improved airport perimeter access security, airline crew security training, enhanced security screening of passengers, baggage, cargo, mail, employees and vendors, enhanced training and qualifications of security screening personnel, additional provision of passenger data to U.S. Customs and Border Protection and enhanced background checks. Funding for airline and airport security under the law is primarily provided by a $2.50 per enplanement security service fee ($5.00 one-way maximum fee for multiple segments) which is being collected from passengers by the air carriers and submitted to the government. The TSA also has the authority to impose additional fees on the air carriers if necessary to cover additional federal aviation security costs. Since 2002, the TSA has imposed an Aviation Security Infrastructure Fee on all airlines to assist in the cost of providing aviation security. The fees assessed are based on airlines actual security costs for the year ended December 31, 2000. The TSA has announced that this fee structure will remain in place until further notice. Furthermore, because of significantly higher security and other costs incurred by airports since September 11, 2001, many airports have significantly increased their rates and charges to airlines, including us, and may do so again in the future. Most airports where we operate impose passenger facility charges of up to $4.50 per segment, subject to an $18 per roundtrip cap.

Noise Abatement

The DOT allows local airport authorities to implement procedures designed to abate special noise problems, provided such procedures do not unreasonably interfere with interstate and foreign commerce, or the national transportation system. Certain airports, including the major airports at Los Angeles, San Diego, San Francisco, San Jose and Sydney, Australia, have established airport restrictions to limit noise, including restrictions on aircraft types to be used and limits on the number of hourly or daily operations or the time of such operations. Local authorities at other airports could consider adopting similar noise regulations. In some instances, these restrictions have caused curtailments in services or increases in operating costs, and such restrictions could limit our ability to expand our operations.

Environmental and Employee Safety and Health

We are subject to various laws and government regulations concerning environmental matters and employee safety and health in the U.S. and other countries which we do business. Many aspects of airlines operations are subject to increasingly stringent federal, state and local laws protecting the environment. U.S. federal laws that have a particular impact on us include the Airport Noise and Capacity Act of 1990, the Clean Air Act, the Resource Conservation and Recovery Act, the Clean Water Act, the Safe Drinking Water Act, and the Comprehensive Environmental Response, Compensation and Liability Act. Certain of our operations are also subject to the oversight of the Occupational Safety and Health Administration (OSHA) concerning employee safety and health matters. The U.S. Environmental Protection Agency (EPA), OSHA, and other federal agencies have been authorized to promulgate regulations that impact our operations. In addition to these federal activities, various states have been delegated certain authorities under the aforementioned federal statutes. Many state and local governments have adopted environmental and employee safety and health laws and regulations, some of which are similar to or stricter than federal requirements, such as California.

Taxes

The airline industry is subject to various passenger, cargo and fuel taxes, which change from time to time. Certain of these taxes are assessed directly to the air carrier (e.g., excise taxes on fuel); while certain other of these taxes are pass though taxes (e.g., excise taxes on air transportation of passengers and cargo). The Bush Administration has proposed changing the current funding mechanism for the FAA air traffic control system and the airport improvement program, which involves the imposition of certain taxes and fees, by introducing a cost-based user fee to be collected from all users of the system, including additional fees charged to users of highly congested airports. The Administration also proposed that Congress authorize the FAA to borrow $5 billion to fund capital improvements necessary to upgrade the air traffic control system and reduce costly delays, which would require additional user fees between 2013 and 2017, and allow airports to increase their passenger facility charges from $4.50 to $6 per segment. We cannot predict what future actions Congress may take in response to the proposal or whether any such actions will have a material effect on our costs or revenue.

Civil Reserve Air Fleet Program

The U.S. Department of Defense regulates the Civil Reserve Air Fleet (CRAF) and government charters. We have elected to participate in the CRAF program whereby we have agreed to make our Boeing 767 aircraft available to the federal government for use by the U.S. military under certain stages of readiness related to national emergencies. The program is a standby arrangement that lets the U.S. Department of Defense U.S. Transportation Command call on as many as four contractually committed Hawaiian aircraft and crews to supplement military airlift capabilities.

In February 2003, the U.S. Secretary of Defense authorized a Stage 1 mobilization of the CRAF program, the lowest activation level. We were required to make one passenger aircraft available as a result of this Stage 1 mobilization. Under the requirements of a Stage 2 mobilization, an additional passenger aircraft would be required. The remaining aircraft subject to the CRAF program would be mobilized under a Stage 3 mobilization, which for us would involve a total of four passenger aircraft. While the government would reimburse us for the use of these aircraft, the mobilization of aircraft under the CRAF program could have a significant adverse impact on our results of operations.

Other Regulations

Several aspects of airline operations are subject to regulation or oversight by federal agencies other than the FAA and the DOT. The federal antitrust laws are enforced by the U.S. Department of Justice.

The U.S. Postal Service has jurisdiction over certain aspects of the transportation of mail and related services provided by our cargo services. Labor relations in the air transportation industry are generally regulated under the Railway Labor Act. We and other airlines certificated prior to October 24, 1978 are also subject to preferential hiring rights granted by the Airline Deregulation Act to certain airline employees who have been furloughed or terminated (other than for cause). The Federal Communications Commission issues licenses and regulates use of all communications frequencies assigned to us and the airlines generally.

Additional laws and regulations are proposed from time to time, which could significantly increase the cost of airline operations by imposing additional requirements or restrictions. Laws and regulations also have been considered from time to time that would prohibit or restrict the ownership and/or transfer of airline routes or takeoff and landing slots. Also, the award of international routes to U.S. carriers (and their retention) is regulated by treaties and related agreements between the U.S. and foreign governments, which are amended from time to time. We cannot predict what laws and regulations will be adopted or what changes to international air transportation treaties will be adopted, if any, or how we will be affected by those changes.

ITEM 1A. RISK FACTORS.

In addition to the risks identified elsewhere in this report, the following risk factors apply to our business, results of operations and financial conditions:

Risks Relating to our Business

Our business is adversely affected by increases in fuel prices.

Aircraft fuel costs constitute a significant portion of Hawaiian s operating expenses, and our results are significantly impacted by changes in the cost of fuel. Fuel costs represented 27.3% and 24.6% of Hawaiian s operating expenses for the years ended December 31, 2006 and 2005, respectively. Based on gallons expected to be consumed in 2007, for every one cent change in the cost per gallon of jet fuel, Hawaiian s annual fuel expense increases or decreases by approximately $1.3 million. Fuel prices and supplies are influenced significantly by international political and economic circumstances, such as the war and post-war unrest in Iraq, as well as OPEC production curtailments, a disruption of oil imports, other conflicts in the Middle East, increasing demand from China, India and other developing countries, environmental concerns, weather and other unpredictable events. For example, during the third quarter of 2005, Hurricanes Katrina and Rita caused widespread disruption to oil production, refinery operations and pipeline capacity along the U.S. Gulf Coast. As a result of these disruptions, the price of jet fuel increased significantly and the availability of jet fuel supplies was diminished. Further increases in jet fuel prices or disruptions in fuel supplies, whether as a result of natural disasters or otherwise, could have a material adverse effect on our results of operations, financial position or liquidity.

Our business is highly dependent on tourism, and our financial results could suffer if there is a downturn in tourism levels.

Our principal base of operations is in Hawaii and our revenue is linked primarily to the number of travelers (mostly tourists) to, from and among the Hawaiian Islands. Hawaii tourism levels are affected by, among other things, the political and economic climate in Hawaii s main tourism markets, the availability of hotel accommodations, promotional spending by competing destinations, the popularity of Hawaii as a tourist destination relative to other vacation options, and other global factors, including natural disasters, safety and security. From time to time, various events and industry specific problems such as strikes have had a negative impact on tourism in Hawaii. In addition, the potential or actual occurrence of terrorist attacks, the wars in Afghanistan and Iraq, and the threat of other negative world events has had and may in the future again have a material adverse effect on Hawaii tourism. No assurance can be given that the level of passenger traffic to Hawaii will not decline in the future. A decline in the level of Hawaii passenger traffic could have a material adverse effect on our results of operations and financial condition.

Our business is subject to substantial seasonal and cyclical volatility.

Our profitability and liquidity are sensitive to seasonal volatility primarily due to leisure and holiday travel patterns. Hawaii is a popular vacation destination. Demand is typically stronger during June, July, August and December and considerably weaker at other times of the year. During weaker demand periods, we may utilize discounted fare pricing strategies to increase our traffic volume. Our results of operations generally reflect this seasonality, but are also impacted by numerous other factors that are not necessarily seasonal. These factors include the extent and nature of fare changes and competition from other airlines, changing levels of operations, national and international events, fuel prices and general economic conditions, including inflation. Because a substantial portion of both personal and business airline travel is discretionary, the industry tends to experience adverse financial results in general economic downturns. Additionally, airlines generally require substantial liquidity to sustain continued operations under most conditions.

The concentration of our business in Hawaii, and between Hawaii and the western United States, provides little diversification of our revenue.

Most of our revenue is generated from air transportation between the islands of Hawaii and the western United States, or within the Hawaiian islands. Many of our competitors, particularly major network carriers with whom we compete in the transpacific business, enjoy greater geographical diversification of their revenue. A reduction in the level of demand for travel within Hawaii, or to Hawaii from the western United States or the U.S. mainland in general, or an increase in the level of industry capacity on these routes may reduce the revenue we are able to generate and adversely affect our financial results. As these routes account for a significantly higher proportion of our revenue than they do for many of our competitors, such a reduction would have a relatively more adverse impact on our financial results.

Our business is increasingly impacted by competition from low cost carriers.

Until recent years, Hawaiian has been largely insulated from direct competition from low cost carriers or LCCs. Most LCCs have lacked the fleet and infrastructure necessary to provide long-haul trans-oceanic service. The Hawaii market has, however, in recent years, seen growing LCC competition from carriers such as ATA and US Airways. ATA offers service to Hawaii from a number of West Coast markets and enjoys a marketing and code sharing relationship with Southwest Airlines providing access to Southwest s customer base and website. US Airways has positioned its business as a low cost carrier following its emergence from bankruptcy and combination with America West Airlines and commenced service to Hawaii at the end of 2005. Our interisland business also faces LCC competition following the entrance of *go!* (an operating division of Mesa Airlines) and the emergence of Aloha Airlines from bankruptcy in early 2006. We also face the threat of more LCC competition in the future. Furthermore, a more fundamental and immediate consequence for us of the proliferation of LCCs is the response from full service network carriers, which are meeting the competition from LCCs by significantly reducing costs and adjusting their route networks to divert resources to long-haul markets such as Hawaii, where LCC competition is less severe. The result is that the network carriers have at the same time reduced their costs of operation and increased capacity in the Hawaii market. Additional capacity to Hawaii, whether from network carriers or LCCs, could result in a decrease in our share of the markets in which we operate, a decline in our yields, or both, which could have a material adverse effect on our results of operations and financial condition.

Our competitors have reduced their operating costs, enabling them to compete successfully at lower fare levels.

In recent years, many of our competitors have dramatically reduced operating costs through a combination of operational restructuring, business simplification and vendor and labor negotiations. Several airlines, including United Airlines, Delta Air Lines, Northwest Airlines, US Airways, ATA and Aloha Airlines filed for bankruptcy protection since 2001, resulting in reduced labor costs, restructuring of debt and lease agreements and other financial improvements. Other carriers, including American Airlines and Continental Airlines, have also reduced operating costs outside of the bankruptcy process. With reduced costs, these competitors are more capable of operating profitably in an environment of reduced fares and may, as a result, increase service in our primary markets or reduce fares to attract additional customers. Because airline customers are price sensitive, we cannot assure that we will be able to attract a sufficient number of customers at sufficiently high fares levels to generate profitability, or that we will be able to reduce our operating costs sufficiently to remain competitive with these airlines.

Our business is impacted by the competitive advantages held by network carriers in the transpacific market.

In the transpacific market, most of our competition comes from network carriers such as United Airlines, American Airlines, Continental Airlines, Delta Air Lines, Northwest Airlines and US Airways. Network carriers have a number of competitive advantages relative to Hawaiian that historically have enabled them to obtain higher fares or attract higher customer traffic levels than Hawaiian:

- Network carriers generate passenger traffic from throughout the U.S. mainland. In contrast, Hawaiian lacks a comparable network to feed passengers to its transpacific flights and is therefore more reliant on passenger demand in the cities we serve.

- Most network carriers operate from hubs, which can provide a built-in market of passengers, depending on the economic strength of the hub city and the size of the customer group that frequent the airline. For example, United flows sufficient passenger traffic throughout the U.S. mainland to schedule approximately 12 flights a day, depending on seasonality, between San Francisco and the Hawaiian islands, which gives San Francisco residents wishing to travel to Hawaii a large number of United non-stop flight choices to Oahu, Maui, Kauai and the Big Island, while Hawaiian, without feed traffic, can offer only one flight per day. In contrast, Honolulu, the hub of our operations, does not originate much transpacific travel, nor does it have the city strength or potential customer franchise of a city such as Chicago or Dallas necessary to provide Hawaiian with a built-in market. Tickets to Hawaii are for the most part not sold in Honolulu, but rather on the mainland, making Honolulu primarily a destination rather than origin of passenger traffic.

Capacity in the interisland market has increased dramatically, including the entry of a new competitor in 2006, and price discounts have escalated.

Since June 2006, capacity on our primary interisland routes (measured in the number of daily seats offered for sale) has increased dramatically. Mesa Airlines, through its operating division *go!*, entered the interisland business in June, with a schedule of approximately 60 daily flights offered as of February 2007. Also in March, Hawaiian expanded its schedule of interisland flights to remain competitive with *go!* *s* schedule, particularly in the early morning and evenings. Aloha Airlines also expanded its schedule shortly thereafter. These capacity increases have been accompanied by significant downward pressure on interisland fare prices, including those charged by Hawaiian. In addition, in July 2007, the Superferry is expected to commence operations in Hawaii with daily interisland services between Oahu and Maui and Oahu and Kauai which will provide for transportation of passengers as well as vehicles.

The combination of increased capacity (seat availability) and price promotions as *go!* seeks to establish a customer following has resulted in a significant reduction in the revenue generated on our interisland routes since June 2006. We can offer no assurances that the competitive situation will change, or that we will be able to achieve cost reductions sufficient to offset the decline in revenue.

Demand for interisland service is declining, and is expected to decline for the foreseeable future.

The demand for interisland service has been steadily declining, as other airlines have increased direct service from the mainland to Oahu s neighbor islands, obviating the need for interisland transfers, and as the infrastructure, particularly the availability of goods and services, in the neighbor islands improves. The total size of the interisland market is, therefore, expected to continue to shrink for the foreseeable future. A decline in the level of interisland passenger traffic could have a material adverse effect on our results of operations and financial condition.

Our share price could be subject to extreme price fluctuations, and stockholders could have difficulty trading shares.

The market price for our common stock has been and may continue to be subject to significant price fluctuations. Price fluctuations could be in response to operating results, changes in the competitive activity in the markets we serve, changes in jet fuel prices, additional bankruptcy filings among airlines, increased government regulation and general market conditions. Additionally, the stock market in recent years has experienced extreme price and volume fluctuations that often have been unrelated to the operating performance of individual companies. These market fluctuations, as well as general economic conditions, may affect the price of our common stock.

In the past, securities class action litigation has often been instituted against a company following periods of volatility in the company s stock price. This type of litigation, if filed against us, could result in substantial costs and divert our management s attention and resources. In addition, the future sale of a substantial number of shares of common stock by us or by our existing stockholders may have an adverse impact on the market price of the shares of common stock. There can be no assurance that the trading price of our common stock will remain at or near its current level.

We are increasingly dependent on technology to operate our business.

We depend heavily on computer systems and technology, such as flight operations systems, communications systems, airport systems and reservations systems to operate our business. Any substantial or repeated failures of our computer or communications systems could impact our customer service, compromise the security of customer information, result in the loss of important data, loss of revenue, and increased costs, and generally harm our business. Like all companies, our computer and communication systems may be vulnerable to disruptions due to events beyond our control, including natural disasters, power or equipment failures, terrorist attacks, equipment or software failures, computer viruses and hackers. Although we have implemented various technology security initiatives and taken measures in an effort to reduce the adverse effects of certain potential failures or disruption, there can be no assurance that these measures are adequate to prevent or remedy disruptions of our systems.

We are subject to various risks as a result of our fleet concentration in Boeing 717s.

Our interisland fleet consists entirely of Boeing 717 aircraft. In January 2005, Boeing Commercial Airplanes (Boeing) announced it would discontinue the production of that aircraft model in 2006. As a result, the availability of parts and maintenance support for Boeing 717 aircraft may become limited in future years. Additionally, we may experience increased costs in later years associated with parts acquisition for and/or maintenance support of this aircraft. Other carriers operating with a more diversified fleet may be better able to withstand such an event, if such an event occurred in the future.

We may experience delays in introducing our recently acquired Boeing 767-300 aircraft into revenue service.

We purchased four used Boeing 767-300 aircraft with the intention of introducing all four aircraft into service during 2006. However, due to unanticipated delays in obtaining FAA approval on our interior modifications, one aircraft was placed into service during September 2006 and one each in January and March 2007. We expect to have the remaining Boeing 767-300 aircraft available for revenue service by the end of the second quarter of 2007. However, due to possible further delays in the timely completion of the overhauls and modifications of the remaining aircraft, there are no assurances that the aircraft will be available by its revised scheduled induction.

As a result of the delays in operating these aircraft, we have incurred costs related to accommodating displaced passengers on other airlines and at costs exceeding the fares we collect for such canceled flights. Additionally, until the aircraft are in revenue service, there will be no direct incremental revenue to fund the fixed costs associated with our ownership and operation of these aircraft, including the wages and benefits for the additional flight crews and ground personnel we hired to accommodate the growth in our Boeing 767 aircraft fleet and the debt-service costs related to the increased debt we incurred in the first quarter of 2006 to help fund our acquisition of these aircraft. We have sold and are selling tickets for future travel on certain of our transpacific flights that are scheduled to be operated by the two remaining aircraft. Further delays to the availability of the aircraft and resultant cancellation of the flights they are scheduled to operate may result in further costs and lost incremental revenue.

We are highly reliant on third-party contractors to provide certain facilities and services for our operations, and termination of our third-party agreements could have a potentially adverse effect on our financial results.

We have agreements with Alaska Airlines, US Airways, American Airlines, Continental Airlines, Delta Air Lines, Northwest Airlines, Island Air, and certain other contractors, to provide certain facilities and services required for our operations. These facilities and services include aircraft maintenance, code sharing, reservations, computer services, frequent flyer programs, passenger processing, ground facilities, baggage and cargo handling and personnel training. Our reliance on these third parties to continue to provide these important aspects of our business impacts our ability to conduct our business effectively.

- *Maintenance agreements.* We have maintenance agreements with Delta Air Lines, Goodrich Aviation Technical Services, the Pratt & Whitney division of United Technologies Corporation, Rolls Royce, Honeywell and others to provide maintenance services for our aircraft, engines, parts and equipment. If one or more of our maintenance providers terminate their respective agreements, we would have to seek alternative sources of maintenance service or undertake the maintenance of these aircraft or components ourselves. We cannot assure you that we would be able to do so on a basis that is as cost-effective as our current maintenance arrangements.

- *Code sharing agreements.* We have code sharing agreements with Alaska Airlines, American Airlines, American Eagle, Continental Airlines, Harmony Airways, Island Air, Korean Air, Northwest Airlines and US Airways. We also participate in the frequent flyer programs of Alaska Airlines, American Airlines, American Eagle, Continental Airlines, Island Air, Northwest Airlines, US Airways, Virgin Atlantic Airways and Virgin Blue. Although these agreements increase our ability to be more competitive, they also increase our reliance on third parties.

- *Fuel agreements.* We have entered into a jet fuel sale and purchase contract to provide us with a substantial amount of jet fuel, which we anticipate will be sufficient to meet all of our jet fuel needs for flights originating in Honolulu during 2007. If the fuel provider terminates its agreement with us, we would have to seek an alternative source of jet fuel. We cannot assure you that we would be able to do so on a basis that is as cost-effective as our current arrangement. We have agreements with vendors at all airports we serve to provide us with fuel. Should any of these vendors cease to provide service to Hawaiian for whatever reason, our operations could be adversely affected.

• *Travel agency and wholesale agreements.* In 2006, passenger ticket sales from travel agencies and wholesalers constituted approximately 24% of our total operating revenue. Travel agents and wholesalers generally have a choice between one or more airlines when booking a customer s flight. Accordingly, any effort by travel agencies or wholesalers to favor another airline or to disfavor us could adversely affect our revenue. Although we intend to maintain favorable relations with travel agencies and wholesalers, there can be no assurance that they will continue to do business with us. The loss of any one or several travel agencies and or wholesalers may have a material adverse effect on operations.

We are subject to various risks associated with our labor outsourcing initiatives.

In July 2006, we reached an agreement with one of our largest labor unions allowing the outsourcing of various clerical and back-office functions including our reservation call center and certain accounting and information technology positions. In exchange for our ability to consider outsourcing as a strategy to reduce future labor and benefit costs, we provided furlough protection to the affected employees and allowed the transfer to other positions at same or higher pay scales. Our future agreements with third-party providers, including overseas third-party providers, may materially fail to meet our service level and performance standards and commitments to our customers. The failure of these providers to adequately perform their service obligations, or other unexpected interruptions of services, may reduce our revenues and increase our expenses, or prevent us from operating our flights profitably and providing other services to our customers. In addition, our business and financial performance could be materially harmed if our customers believe that our services are unreliable or unsatisfactory. In addition, to the extent we are unable to maintain the outsourcing or subcontracting of certain services for our business, we would incur substantial costs, including costs associated with hiring new employees, in order to return these services in-house.

We are dependent on satisfactory labor relations.

Labor costs are a significant component of airline expenses and can substantially impact an airline s results. Labor and related benefit costs represented approximately 25.8% and 27.7% of Hawaiian s operating expenses for the years ended December 31, 2006 and 2005, respectively. We may experience pressure to increase wages and benefits for our employees in the future. We may make strategic and operational decisions that require the consent of one or more of our labor unions. We cannot assure you that these labor unions will not require additional wages or benefits in return for their consent. In addition, we have entered into collective bargaining agreements with our pilots, mechanical group employees, clerical group employees, flight attendants, dispatchers and network engineers which are amendable in less than two years. We cannot assure you that future agreements with our employees unions will be on terms in line with our expectations or comparable to agreements entered into by our competitors, and any future agreements may increase our labor costs or otherwise adversely affect us. If we are unable to reach an agreement with any unionized work group, we may be subject to future work interruptions and/or stoppages, which may hamper or halt operations.

Our operations may be adversely affected if we are unable to attract and retain key executives, including our Chief Executive Officer.

We are dependent on our ability to attract and retain key executives, particularly Mark B. Dunkerley, our Chief Executive Officer, with whom we entered into a three-year employment agreement on August 18, 2005. Competition for such personnel in the airline industry is highly competitive, and we cannot be certain that we will be able to retain our Chief Executive Officer or other key executives or that we can attract other qualified personnel in the future. Any inability to retain our Chief Executive Officer and other key executives, or attract and retain additional qualified executives, could have a negative impact on our operations.

Our substantial debt could adversely affect our financial condition.

As of December 31, 2006, we had substantial indebtedness, including $126.0 million of debt related to the acquisition in December 2006 of three previously leased Boeing 767-300ER aircraft, $55.0 million of the Term A Credit Facility scheduled to mature in December 2010, a $62.5 million Term B Credit Facility scheduled to mature in March 2011 and $23.0 million of notes payable to the Internal Revenue Service (IRS) that mature in June 2011. See Management s Discussion and Analysis of Financial Condition and Results of Operations Liquidity and Capital Resources.

The requirement to service our debt makes us more vulnerable to general adverse economic conditions, requires us to dedicate a substantial portion of our cash flow from operations to payments on our debt, thereby reducing the availability of our cash flow for operations and other purposes, limits our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate, and places us at a competitive disadvantage compared to any other competitor that has less debt than we do.

Certain of our financing agreements and our credit card processing agreement include financial covenants that impose substantial restrictions on our financial and business operations.

The terms of our Term A and Term B Credit Facilities with Wells Fargo Foothill, Inc. and Canyon Capital Advisors, LLC, respectively, restrict our ability to, among other things, incur additional indebtedness, pay dividends or make other payments on investments, consummate asset sales or similar transactions, create liens, merge or consolidate with any other person, or sell, assign, transfer, lease, convey or otherwise dispose of all or substantially all of our assets. The terms of the agreements contain covenants that require us to meet certain financial tests to avoid a default that might lead to early termination of the facilities. Moreover, these agreements contain covenants that require us to meet certain financial tests. If we were not able to comply with these covenants, our outstanding obligations under these facilities could be accelerated and become due and payable immediately.

Under our bank-issued credit card processing agreement, our credit card processor holds back proceeds from advance ticket sales to serve as collateral to cover any possible chargebacks or other disputed charges that may occur. These holdbacks, which are included in restricted cash in our consolidated balance sheet, totaled $53.7 million at December 31, 2006. Funds are subsequently made available to us as air travel is provided. The agreement also contains financial covenants which require, among other things, that we maintain a minimum amount of unrestricted cash and maintain certain levels of debt service coverage and operating income. Although we are currently in compliance with all of these covenants, failure to maintain compliance would result in our credit card processor being able to hold back additional proceeds from advance ticket sales, which would adversely affect our liquidity. Depending on our unrestricted cash balance at the time, the holdback of a significant amount of cash collateral could cause our unrestricted cash and short term investments balance to fall below the minimum balance requirement under our Term A Credit Facility, resulting in a default under that facility.

Our business has substantial financial and operating leverage.

The airline industry operates on low gross profit margins and revenue that varies substantially in relation to fixed operating costs. Due to high fixed costs, the expenses of each flight do not vary proportionately with the number of passengers carried, but the revenue generated from a particular flight is directly related to the number of passengers carried. Accordingly, while a decrease in the number of passengers carried would cause a corresponding decrease in revenue (if not offset by higher fares), it may result in a disproportionately greater decrease in profits. An increase in the number of passengers carried would have the opposite effect.

Our obligations for funding our defined benefit pension plans are significant and are affected by factors beyond our control.

Hawaiian sponsors three defined benefit pension plans. Although two of the plans were frozen effective October 1, 1993 and Hawaiian s collective bargaining agreement with our pilots provides that benefit accruals for certain pilots will be frozen effective January 1, 2008, our unfunded pension obligation was $74.0 million as of December 31, 2006. Hawaiian made scheduled contributions of $10.9 million and $23.3 million for 2006 and 2005, respectively, and anticipates contributing $8.7 million to the defined benefit pension plans during 2007. The timing and amount of funding requirements depend upon a number of factors, including labor negotiations and changes to pension plan benefits as well as factors outside our control, such as asset returns, interest rates and changes in pension laws.

Risks Relating to the Airline Industry

The continued threat of terrorist attacks may adversely impact our business.

Since the terrorist attacks of September 11, 2001, the airline industry has experienced profound changes, including substantial revenue declines and cost increases, which have resulted in industry-wide liquidity issues. Additional terrorist attacks, even if not made directly on the airline industry, or the fear of such attacks (including elevated national threat warnings or selective cancellation or redirection of flights due to terror threats such as the August 2006 terrorist plot targeting multiple U.S. airlines), could further adversely impact us and the airline industry. Increased regulation governing carry-on baggage and passenger travel may further increase passenger inconvenience and reduce the demand for air travel. In addition, other world events and developments may further decrease demand for air travel, and could result in further increased costs for us and the airline industry. We are currently unable to estimate the impact of any future terrorist attacks. However, any future terrorist attacks could have a material adverse impact on our business, financial condition and results of operations, and on the airline industry in general.

The airline industry is highly competitive, and if we cannot successfully compete in the marketplace, our financial condition and results of operations will be adversely affected.

The airline industry is highly competitive, and many of our competitors are larger and have substantially greater financial resources than we do. The commencement of, or increase in, service on our routes by existing or new carriers could negatively impact our operating results. In the past, competing airlines have reduced fares and increased capacity beyond market demand on routes served by us in order to maintain or generate additional revenue. Further fare reductions and capacity increases by competing airlines could force us to reduce fares or adjust our capacity to levels that may adversely affect our operations and profitability. Many of our competitors have larger customer bases, greater brand recognition and significantly greater financial and marketing resources than we do. Either aggressive marketing tactics or a prolonged fare war initiated by one or more of these competitors could adversely impact our financial resources and affect our ability to compete in these markets.

Vigorous price competition exists in the airline industry, with competitors frequently offering discounted fares and other promotions to stimulate traffic during weaker demand periods, generate cash flow or increase relative market share in selected markets. Airline profit levels are highly sensitive to changes in fuel costs, fare levels and passenger demand. Passenger demand and fare levels are influenced by, among other things, the state of the global economy, domestic and international events, airline capacity and pricing actions taken by carriers. The September 11, 2001 terrorist attacks, turbulent international events (including the war and post-war unrest in Iraq), high fuel prices and extensive price discounting by carriers have resulted in significant losses for the airline industry. The introduction of broadly available, deeply discounted fares by a U.S. airline could result in lower yields for the entire industry and could have a material adverse effect on our operating results.

The airline industry is subject to extensive government regulation, and new regulations could have an adverse effect on our financial condition and results of operations.

Airlines are subject to extensive regulatory requirements that result in significant costs. Additional laws, regulations, taxes and airport rates and charges have been proposed from time to time that could significantly increase the cost of airline operations or reduce revenue. For example, the ATSA, which became law in November 2001, mandates the federalization of certain airport security procedures and imposes additional security requirements on airlines. The FAA from time to time issues directives and other regulations relating to the maintenance and operation of aircraft that require significant expenditures. Some FAA requirements cover, among other things, retirement of older aircraft, security measures, collision avoidance systems, airborne windshear avoidance systems, noise abatement and other environmental concerns, commuter aircraft safety and increased inspections and maintenance procedures to be conducted on older aircraft. We expect to continue incurring expenses to comply with the FAA s regulations.

Many aspects of airlines operations also are subject to increasingly stringent federal, state, local and foreign laws protecting the environment. Future regulatory developments in the U.S. and abroad could adversely affect operations and increase operating costs in the airline industry. For example, potential future actions that may be taken by the U.S. government, foreign governments, or the International Civil Aviation Organization to limit the emission of greenhouse gases by the aviation sector are unknown at this time, but the effect on us and our industry is likely to be adverse and could be significant. In addition, the ability of U.S. carriers to operate international routes is subject to change because the applicable arrangements between the U.S. and foreign governments may be amended from time to time, or because appropriate slots or facilities are not available. We cannot provide assurance that laws or regulations enacted in the future will not adversely affect us.

Our operations may be adversely impacted by increased security measures mandated by regulatory authorities.

Because of significantly higher security and other costs incurred by airports since September 11, 2001, many airports significantly increased their rates and charges to air carriers, including us, and may do so again in the future. Additionally, since September 11, 2001, the DHS and the TSA and other agencies within the DHS have implemented numerous security measures that affect airline operations and costs, and are likely to implement additional measures in the future. The DHS has announced greater use of passenger data for evaluating security measures to be taken with respect to individual passengers, expanded use of federal air marshals on flights (thus displacing revenue passengers), investigating a requirement to install aircraft security systems (such as active devices on commercial aircraft as countermeasures against portable surface to air missiles) and expanded cargo and baggage screening. The TSA has imposed additional measures affecting the contents of baggage that may be carried on an aircraft in response to the discovery in August 2006 of a terrorist plot targeting several U.S. airlines. The TSA and other security regulators may impose other measures as necessary to respond to future threats. A large part of the costs of these security measures is borne by the airlines and their passengers, and we believe that these and other security measures have the effect of increasing the inconvenience of air transportation and thus decreasing traffic. Security measures imposed by the U.S. and foreign governments subsequent to September 11, 2001 have increased our costs, and additional measures taken in the future may result in similar adverse effects. We cannot provide assurance that additional security requirements or security-related fees enacted in the future will not adversely affect us.

Our insurance costs have increased substantially in recent years and further increases in insurance costs or reductions in coverage could have an adverse effect on our financial results.

We carry types and amounts of insurance customary in the airline industry, including coverage for general liability, passenger liability, property damage, aircraft loss or damage, baggage and cargo liability and workers compensation. We are required by the DOT to carry liability insurance on each of our aircraft. We currently maintain commercial airline insurance with a major group of independent insurers that regularly participate in world aviation insurance markets including public liability insurance and coverage for losses resulting from the physical destruction or damage to our aircraft. However, there can be no assurance that the amount of such coverage will not be changed, or that we will not bear substantial losses from accidents. We could incur substantial claims resulting from an accident in excess of related insurance coverage that could have a material adverse effect on our results of operations and financial condition.

After the events of September 11, 2001, aviation insurers significantly reduced the maximum amount of insurance coverage available to commercial air carriers for liability to persons other than employees or passengers for claims resulting from acts of terrorism, war or similar events (war-risk coverage). At the same time, they significantly increased the premiums for such coverage as well as for aviation insurance in general. As a result, war-risk insurance in amounts necessary for our operations, and at premiums that are not excessive, is not currently available in the commercial insurance market and we have therefore purchased from the U.S. government third-party war-risk insurance coverage. This coverage has been extended by the FAA under the Homeland Security Act to September 30, 2007, after which time it is anticipated that the federal policy will be extended unless insurance for war-risk coverage in necessary amounts is available from independent insurers or a group insurance program is instituted by the U.S. carriers and the DOT. However, there can be no assurance that the federal policy will be renewed or an alternative policy can be obtained in the commercial market at a reasonable cost. Although our overall hull and liability insurance costs have been reduced since the post-2001 increases, there can be no assurances that these reductions would be maintained in the event of future increases in the risk, or perceived risk, of air travel by the insurance industry, or a reduction of capital flows into the aviation insurance market.

We are at risk of losses and adverse publicity in the event of an aircraft accident.

We are exposed to potential losses that may be incurred in the event of an aircraft accident. Any such accident could involve not only the repair or replacement of a damaged aircraft and its consequential temporary or permanent loss of revenue, but also significant potential claims of injured passengers and others. In addition, any aircraft accident or incident could cause a public perception that we are less safe or reliable than other airlines, which would harm our business.

We are at risk of losses in the event of an outbreak of diseases.

Public health threats, such as avian influenza (the Bird Flu), Severe Acute Respiratory Syndrome (SARs) and other highly communicable diseases, outbreaks of which have already occurred in various parts of the world, could adversely impact our operations and the worldwide demand for air travel. In 2003, there was an outbreak of SARS, which primarily had an adverse impact on our Pacific operations. If there were another outbreak of a disease (such as SARS or the Bird Flu) that adversely affects travel behavior, it could have a material adverse impact on our operations.

ITEM 1B. UNRESOLVED STAFF COMMENTS.

None.

ITEM 2. PROPERTIES.

Aircraft

As of December 31, 2006, our operating fleet consisted of 14 Boeing 767-300ER and one Boeing 767-300 aircraft to service our transpacific, South Pacific and substantially all of our charter routes, and 11 Boeing 717-200 aircraft to service our interisland routes. The following table summarizes our total fleet as of December 31, 2006:

Aircraft Type	Leased	Owned	Seating Capacity (Per Aircraft)	Simple Average Age (In Years)
767-300ER	11	3	252-264	8
767-300(a)		4	264	20
717-200	11		123	6
Total	22	7		

(a) Three of the four Boeing 767-300 aircraft were not yet in service as of December 31, 2006.

See Note 7 to our consolidated financial statements for additional information regarding our aircraft lease agreements.

Ground Facilities

Hawaiian s principal terminal facilities, cargo facilities, hangar and maintenance facilities are located at the Honolulu International Airport (HNL). The majority of the facilities at HNL are leased on a month-to-month basis. Hawaiian is also charged for the use of terminal facilities at the five major interisland airports owned by the State of Hawaii. Some terminal facilities, including gates and holding rooms, are considered by the State of Hawaii to be common areas and thus are not exclusively controlled by Hawaiian. Other facilities, including station managers offices, Premier Club lounges and operations support space, are considered exclusive-use space by the State of Hawaii.

Hawaiian has signatory agreements with the Port of Portland and McCarran International Airport, and a facilities sharing agreement with the City of Phoenix for terminal space, and operating agreements with the Port of San Diego, McCarran International Airport in Las Vegas, Nevada, the City of Los Angeles, the County of Sacramento and Societe D Equipment De Tahiti Et Des Iles (SETIL) for Faa a International Airport in Papeete, French Polynesia. Hawaiian has a right of entry agreement with the Ted Stevens Anchorage International Airport. Hawaiian is a shareholder in LAX Two in Los Angeles. Hawaiian has ground handling agreements which include office space leases with Delta Air Lines in Portland, Oregon, San Francisco and Sacramento, California; American Airlines in San Jose, California; United Airlines in Anchorage, Alaska; and Penauille Servisair in Las Vegas, Nevada. Hawaiian has a License Agreement with Jet Blue Airlines in San Diego, California and Phoenix, Arizona, for the use of ticket counter space and other operational areas. Hawaiian has lease agreements with the Government of American Samoa in Pago Pago, and Sydney Airport Corporation, Limited, in Sydney, Australia. Hawaiian also has agreements in place for alternate landing sites with the Port of Moses Lake, King County (Boeing Field) in Seattle, Ontario International Airport in California and Fairbanks International Airport in Alaska.

The table below sets forth the airport locations Hawaiian utilizes pursuant to various lease agreements:

Name of Airport	**Location**	
Ted Stevens Anchorage International Airport	Anchorage	Alaska
Phoenix Sky Harbor International Airport	Phoenix	Arizona
Los Angeles International Airport	Los Angeles	California
Sacramento International Airport	Sacramento	California
San Diego International Airport	San Diego	California
San Francisco International Airport	San Francisco	California
Hilo International Airport	Hilo	Hawaii
Norman Y. Mineta San Jose International Airport	San Jose	California
Honolulu International Airport	Honolulu	Hawaii
Kahului Airport	Kahului	Hawaii
Kona International Airport	Kona	Hawaii
Lihue Airport	Lihue	Hawaii