

**NEW ISSUE
BOOK-ENTRY ONLY**

**RATINGS: Moody's: Aaa
Fitch: AAA
(See "Ratings" herein)**

In the opinion of Orrick, Herrington & Sutcliffe LLP, Bond Counsel, based upon an analysis of existing laws, regulations, rulings and court decisions, and assuming, among other matters, compliance with certain covenants, interest on the Series 2003 Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, and all of the Series 2003 Bonds and the income therefrom are exempt from all taxation by the State of Hawaii or any County or other political subdivision thereof, except inheritance, transfer, estate and certain franchise taxes. In the further opinion of Bond Counsel, interest on the Series 2003 Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Bond Counsel observes that such interest is included in adjusted current earnings in calculating corporate alternative minimum taxable income. Bond Counsel expresses no opinion regarding any other tax consequences related to the ownership or disposition of, or the accrual or receipt of interest on, the Bonds. See "TAX MATTERS" in this Official Statement.

**\$218,400,000
City and County of Honolulu
Wastewater System Revenue Bonds
(Second Bond Resolution)
Junior Series 2003A-1 and 2003A-2 and
Junior Series 2003B-1 and 2003B-2
(Auction Rate Certificates)**

Dated: Date of Issuance

Price: 100%

Due: July 1, 2032

The Series 2003 Bonds are issuable in fully registered form and when issued will be registered initially in the name of Cede & Co., as nominee of The Depository Trust Company ("DTC"), New York, New York. So long as DTC or its nominee is the registered owner of the Series 2003 Bonds, purchases of the Series 2003 Bonds will be made in book-entry form only, through brokers and dealers who are, or who act through, DTC participants; beneficial owners of the Series 2003 Bonds will not receive physical delivery of Bond certificates; payment of the principal of and interest and any premium on the Series 2003A and 2003B Bonds will be made by BNY Western Trust Company, as Paying Agent, directly to DTC or its nominee; and disbursement of such payments to DTC participants will be the responsibility of DTC and disbursement of such payments to the beneficial owners will be the responsibility of DTC participants. Purchases of the Series 2003 Bonds may be made initially in the denomination of \$50,000 or any integral multiple thereof.

Each series of the Series 2003 Bonds will initially bear interest at rates determined prior to the issuance thereof, for the initial periods set forth on the inside cover hereof. Thereafter, each series of the Series 2003 Bonds will bear interest at auction rates determined as described herein, unless converted to bear interest at a different rate. Interest on the Series 2003 Bonds will be payable at the times and in the manner described herein. The Series 2003 Bonds are subject to redemption prior to the stated maturity thereof as described herein.

The proceeds of the Series 2003 Bonds will be used: (i) to fund the cost of certain additions and improvements to the Wastewater System owned by the City and County of Honolulu (the "City and County"); (ii) to provide for a reserve; and (iii) to pay the costs of issuance of the Series 2003 Bonds.

The Series 2003 Bonds will be issued by the City and County under a bond resolution, as supplemented (the "Bond Resolution"), pursuant to which the City and County has previously issued bonds and may issue additional bonds on a parity with the Series 2003 Bonds, as described herein (collectively with the Series 2003 Bonds, the "Bonds"). The Series 2003 Bonds are limited special obligations of the City and County payable solely from, and secured solely by, a pledge of proceeds of Bonds held or set aside under the Bond Resolution, the Net Revenues, and certain funds and accounts established by the Bond Resolution, on a parity with all other Bonds issued under the Bond Resolution. Such pledge of the Net Revenues is junior and subordinate to the pledge made by the City and County in respect of First Resolution Obligations which have been and may in the future be issued under the First Bond Resolution, as such terms are defined herein. **The Bonds are not a general or moral obligation of the State of Hawaii or any political subdivision thereof, including the City and County, and the faith and credit of the State of Hawaii or any political subdivision thereof, including the City and County, are not pledged to the payment of the principal of, premium, if any, or interest on the Bonds, and no holder of the Bonds shall have the right to compel the exercise of the taxing power of the State of Hawaii or any political subdivision thereof, including the City and County, in connection with any default with respect to the Bonds.**

Payment of the principal of and interest on the Series 2003 Bonds when due will be insured under a Financial Guaranty Insurance Policy to be issued by MBIA Insurance Corporation simultaneously with the delivery of the Series 2003 Bonds. See "BOND INSURANCE" herein and "Appendix F" hereto for further information.



This cover page contains certain information for quick reference only. It is not a summary of the bond issue. Prospective investors must read the entire Official Statement (including the Appendices) to obtain information essential to the making of an informed investment decision.

The Series 2003 Bonds are offered when, as and if issued and received by the Underwriters, and are subject to the approval of legality by Orrick, Herrington & Sutcliffe LLP, San Francisco, California, Bond Counsel to the City and County. Certain legal matters will be passed upon for the Underwriters by their counsel, McCarriston Miller Mukai MacKinnon LLP, Honolulu, Hawaii. It is expected that the Series 2003 Bonds in definitive form will be available for delivery to DTC, in New York, New York, on or about May 8, 2003.

UBS PaineWebber Inc.

Citigroup

Dated: May 1, 2003

\$218,400,000
City and County of Honolulu
Wastewater System Revenue Bonds
(Second Bond Resolution)
Junior Series 2003A-1 and 2003A-2 and
Junior Series 2003B-1 and 2003B-2
(Auction Rate Certificates)

	Principal Amount	First Auction Date	Length of Initial Period	First Interest Payment Date	Auction Date Generally	Interest Payment Date Generally
Series 2003A-1	\$54,600,000	June 12, 2003	36 days	June 13, 2003	Each 5 th Thursday	Each 5 th Friday
Series 2003A-2	54,600,000	June 26, 2003	50 days	June 27, 2003	Each 5 th Thursday	Each 5 th Friday
Series 2003B-1	54,600,000	June 12, 2003	36 days	June 13, 2003	Each 5 th Thursday	Each 5 th Friday
Series 2003B-2	54,600,000	June 26, 2003	50 days	June 27, 2003	Each 5 th Thursday	Each 5 th Friday

UBS PaineWebber will act as Broker-Dealer for the Series 2003A Bonds and Citigroup will act as Broker-Dealer for the Series 2003B Bonds.

City and County of Honolulu
State of Hawaii
(Incorporated 1907)

MAYOR

Jeremy Harris

CITY COUNCIL

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Chair and Presiding Officer

Ann H. Kobayashi
Vice-Chair

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DIRECTOR OF BUDGET AND FISCAL SERVICES

Ivan M. Lui-Kwan

ACTING DIRECTOR OF ENVIRONMENTAL SERVICES

Frank J. Doyle

CORPORATION COUNSEL

David Z. Arakawa

BOND COUNSEL

Orrick, Herrington & Sutcliffe LLP
San Francisco, California

The information contained in this Official Statement has been obtained from the City and County of Honolulu and other sources deemed reliable. No guaranty is made, however, as to the accuracy or completeness of such information. The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with, and as part of, their responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriters do 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 Series 2003 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 Series 2003 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.

THE SERIES 2003 BONDS HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, IN RELIANCE UPON AN EXEMPTION CONTAINED IN SUCH ACT. THE SERIES 2003 BONDS HAVE NOT BEEN REGISTERED OR QUALIFIED UNDER THE SECURITIES LAWS OF ANY STATE. IN CONNECTION WITH THIS OFFERING THE UNDERWRITERS MAY OVER-ALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE SERIES 2003 BONDS OFFERED HEREBY AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

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OFFICIAL STATEMENT

\$218,400,000

City and County of Honolulu Wastewater System Revenue Bonds (Second Bond Resolution)

\$54,600,000 Junior Series 2003A-1 and \$54,600,000 Junior Series 2003A-2
\$54,600,000 Junior Series 2003B-1 and \$54,600,000 Junior Series 2003B-2
(Auction Rate Certificates)

INTRODUCTORY STATEMENT

This Official Statement, which includes the cover page and the appendices, provides certain information in connection with the issuance by the City and County of Honolulu (the "City and County") of \$108,850,000 aggregate principal amount of Wastewater System Revenue Bonds (Second Bond Resolution), Junior Series 2003A (the "Series 2003A Bonds"), consisting of \$54,600,000 aggregate principal amount of Series 2003A-1 Bonds and \$54,600,000 aggregate principal amount of Series 2003A-2 Bonds (the "Series 2003A-1 Bonds" and the "Series 2003A-2 Bonds," respectively), and \$108,850,000 aggregate principal amount of Wastewater System Revenue Bonds (Second Bond Resolution), Junior Series 2003B (the "Series 2003B Bonds" and, together with the Series 2003A Bonds, the "Series 2003 Bonds"), consisting of \$54,600,000 aggregate principal amount of Series 2003B-1 Bonds and \$54,600,000 aggregate principal amount of Series 2003B-2 Bonds (the "Series 2003B-1 Bonds" and the "Series 2003B-2 Bonds," respectively). The Series 2003 Bonds are to be issued under and secured by the Second Wastewater Revenue Bond Resolution adopted by the City Council of the City and County on November 10, 1998 (the "Second Bond Resolution"), and the Series 2003 Resolution adopted by the City Council of the City and County on April 16, 2003 (the "Series 2003 Resolution"). The Second Bond Resolution, as amended and supplemented, is referred to herein as the "Bond Resolution." The Series 2003 Bonds are also to be issued under a certain Bond Series Certificate of the City and County dated the date of this Official Statement, relating to the Series 2003 Bonds (the "Series 2003 Certificate").

The capitalization of any word herein not conventionally capitalized indicates that such word is defined in the Bond Resolution, in the Series 2003 Certificate or this Official Statement. A glossary of certain terms used in this Official Statement and the Bond Resolution is set forth in Appendix C under "Certain Definitions." Additional terms used in this Official Statement and the Series 2003 Certificate in connection with the determination of interest on the Series 2003 Bonds and related matters are defined in Appendix B hereto.

The proceeds of the Series 2003 Bonds will be used: (i) to fund the cost of certain additions and improvements to the Wastewater System of the City and County (including reimbursement to the General Fund of the City and County of the costs of certain recent improvements temporarily funded from the General Fund); (ii) to provide for a surety bond for funding of the Common Reserve Subaccount in an amount equal to the Common Reserve Subaccount Requirement; and (iii) to pay the costs of issuance of the Series 2003 Bonds.

The Series 2003 Bonds are the second and third series of bonds issued under and pursuant to the Bond Resolution (each a "Series" and collectively, the "Bonds") and will be secured by and entitled to the protection of the Bond Resolution on a parity with all Bonds heretofore issued and to be hereafter issued under and pursuant to the Bond Resolution. The Bonds are limited special obligations of the City and County payable solely from, and secured solely by a pledge of, proceeds of Bonds held or set aside under the Bond Resolution, the Net Revenues, and certain funds and accounts established by the Bond Resolution. Such pledge of the Net Revenues is junior and subordinate to the pledge of the Net Revenues to secure obligations issued under and pursuant to the First Bond Resolution, described below, but is senior and superior to the pledge of the Net Revenues to secure obligations issued under and pursuant to any other bond resolution. See "SECURITY FOR THE BONDS."

In 1998, the City and County issued \$264,152,890 of Bonds under the Bond Resolution (the “Junior Series 1998 Bonds”), and, as part of the same plan of finance, also issued \$55,300,000 principal amount of Wastewater System Revenue Bonds (First Bond Resolution), Senior Series 1998 (the “Senior Series 1998 Bonds”), under a First Wastewater Revenue Bond Resolution adopted by the City Council of the City and County on November 10, 1998 (as supplemented, the “First Bond Resolution”). In 2001 the City and County issued an additional \$136,020,000 of Wastewater System Revenue Bonds (First Bond Resolution), Senior Series 2001 (together with the Senior Series 1998 Bonds, the “Outstanding Senior Bonds”) under the First Bond Resolution. The Outstanding Senior Bonds are limited special obligations of the City and County payable solely from, and secured solely by a pledge of, the Net Revenues, proceeds of bonds held or set aside under the First Bond Resolution and certain funds and accounts established by the First Bond Resolution. Such pledge of the Net Revenues is senior and superior to the pledge of the Net Revenues to secure the Bonds issued under and pursuant to the Bond Resolution. The Series 2003 Bonds are considered to be Subordinate Obligations for purposes of the First Bond Resolution.

The Department of Environmental Services (the “Department”) has the full and complete authority to manage, control and operate the Wastewater System owned or managed and under the jurisdiction of the City and County, including all materials, supplies, equipment and properties used or useful in connection with the Wastewater System. The Department was created July 1, 1998, as part of a City-wide reorganization to streamline operations. Previously, the Department of Wastewater Management, created by a City Charter change effective July 1, 1993, provided operation, maintenance, planning, design and construction of wastewater facilities in the City and County. The City Charter and Chapter 49, Hawaii Revised Statutes (the “Act”) empower the City and County to issue revenue bonds in its name for the purposes of the Wastewater System. See “THE CITY AND COUNTY AND THE DEPARTMENT.”

The Wastewater System services approximately 136,000 separate accounts and a population of approximately 600,000, which is approximately 68% of the total population of the City and County. The service area covers nearly 500 square miles. The customer base includes the residential population, business and industrial, and other users located in the service area. Of the 136,000 accounts, 129,000 are residential, representing 70% of the total revenue from sewer service charges; and the remaining 7,000 are non-residential, representing approximately 30% of the total revenue from sewer service charges. The average total volume of wastewater processed by the City and County’s Wastewater System is 111 million gallons per day. A number of small private wastewater systems also serve some areas in the City and County. The average total volume of wastewater processed by all such private systems is 4.1 million gallons per day, or approximately 4% of the total wastewater processed in Honolulu. See “THE WASTEWATER SYSTEM.”

The additions and improvements to the Wastewater System which are to be financed from the proceeds of the Series 2003 Bonds are part of a five year capital improvement program adopted by the Department and approved by the City Council of the City and County (the “2003-2007 Capital Improvement Program”). The 2003-2007 Capital Improvement Program is projected to cost approximately \$744 million (actual dollars through 2004, inflated dollars thereafter) and is being undertaken for the purposes, among others, of meeting certain consent decrees entered into by the Department with Federal and State regulatory bodies and reliably serving projected growth in the number of customers served by the Wastewater System. The 2003-2007 Capital Improvement Program is a part of the 1998-2017 twenty year capital improvement program (the “1998-2017 Capital Improvement Program”) the Department has undertaken. The 1998-2017 Capital Improvement Program is projected to cost approximately \$2.3 billion (actual dollars through 2004, inflated dollars thereafter) and has been undertaken for the same basic purposes as the 2003-2007 Capital Improvement Program. The cost of the 1998-2017 Capital Improvement Program, including the 2003-2007 Capital Improvement Program, is expected to be financed primarily from (i) the proceeds of the Series 2003 Bonds and Bonds previously issued, (ii) proceeds of additional Bonds to be hereafter issued, (iii) proceeds of Outstanding Senior Bonds and additional First Resolution Obligations to be hereafter issued, (iv) proceeds of Reimbursable Obligations previously issued and currently available, (v) the Net Revenues of the Wastewater System, and (vi) Wastewater System Facilities Charges.

The Department has projected revenues, expenses and coverages for the Wastewater System for the Fiscal Years 2003-2012, inclusive. The projections are based on inflated dollars (*i.e.*, adjusted from 2003 dollars). The projections indicate that with respect to the Fiscal Years 2003-2012, inclusive, the City and County can (i) issue the Series 2003 Bonds to finance \$180 million of necessary additions and improvements to the Wastewater System, to fund the Common Reserve Subaccount in an amount sufficient to satisfy its requirement, and to pay the costs of

issuing the Series 2003 Bonds; (ii) finance an additional \$1.38 billion of improvements to the Wastewater System from proceeds of additional Bonds and First Resolution Obligations to be hereafter issued, proceeds of Reimbursable Obligations previously issued and currently available, proceeds of wastewater revenue bonds previously issued and currently available, the Net Revenues and Wastewater System Facility Charges over the nine year period; and (iii) fully meet all reserve funding and coverage requirements under the Bond Resolution and the First Bond Resolution by raising sewer rates and charges by 12% in Fiscal Year 2004-2005 and another 9% to 13% in each of the Fiscal Years thereafter, and by raising Wastewater System Facility Charges by 305% in Fiscal Year 2003-2004 and another 3% in each of the Fiscal Years thereafter. The average monthly residential wastewater charge is expected to increase from \$33.05 to \$60.67 (in inflated dollars) by 2010. The Wastewater System Facility Charge is expected to increase from \$1,146 to \$5,541 (in inflated dollars) by 2010.

Pursuant to the Act and the City Charter, the City Council has the power to impose, prescribe and collect rates, rentals, fees or charges for the use and services of, and the facilities furnished by, the Wastewater System so that the Wastewater System will be and remain self-sustaining. The rates, rentals, fees or charges imposed and prescribed are required to produce revenues which will be at least sufficient to pay debt service on all revenue bonds issued for the purposes of the Wastewater System, including the Bonds and the First Resolution Obligations, to provide reserves therefor, to pay the costs of operation, maintenance and repair of the Wastewater System, and to carry out the covenants of all resolutions authorizing the issuance of revenue bonds for the purposes of the Wastewater System, including the Bond Resolution and the First Bond Resolution. The rates and charges fixed and imposed by the City Council are not subject to approval by any federal or state regulatory bodies. See discussion under "HISTORICAL AND PROJECTED REVENUES, EXPENSES AND COVERAGES – General."

APPLICATION OF PROCEEDS

The proceeds of the Series 2003 Bonds, in an amount equal to the principal thereof less Underwriters' discount, will be applied to make the following deposits:

Improvement Second Account*	\$200,469,264.32
Common Reserve Subaccount**	297,055.66
Series 2003 Improvement Second Interest Subaccount.....	15,060,722.76
Wastewater General Account for Costs of Issuance***	1,194,000.00
Total Uses	<u><u>\$217,021,042.74</u></u>

* Includes reimbursement of General Fund.

** Cost of surety bond premium.

*** Includes bond insurance premium, and insurer legal fees.

THE SERIES 2003 BONDS

General

The Series 2003 Bonds are being issued initially as Bonds bearing interest at an Auction Rate. Each Series 2003 Bond will be dated as of the date of its initial delivery and will bear interest from that date until its initial Auction Date at the initial rates established in connection with the initial offering and thereafter at the applicable Auction Rate established for such Series 2003 Bond, as set forth in the Series 2003 Certificate and summarized in Appendix B hereto. The initial Auction Date for the Series 2003A-1 Bonds and Series 2003B-1 Bonds will be June 12, 2003, and the initial Auction Date for the Series 2003A-2 Bonds and Series 2003B-2 Bonds will be June 26, 2003. The initial Interest Payment Date for the Series 2003A-1 Bonds and Series 2003B-1 Bonds will be June 13, 2003, and the initial Interest Payment Date for the Series 2003A-2 Bonds and Series 2003B-2 Bonds will be June 27, 2003. Each Initial Auction Period will be from the date of delivery of the Series 2003 Bonds through the day prior to the applicable initial Interest Payment Date. Interest Payment Dates and Auction Dates will generally occur each 35 days after the initial Interest Payment Date and the initial Auction Date, respectively, subject to adjustment pursuant to the provisions of the Series 2003 Certificate as described in Appendix B. The Series 2003 Bonds will mature, subject to the redemption provisions described below, in the amounts and on the dates set forth on the cover of this Official Statement. The Series 2003 Bonds while bearing interest at an Auction Rate are issuable in denominations of \$50,000 or integral multiples thereof.

The beneficial owner of a Series 2003 Bond bearing interest at an Auction Rate may sell, transfer or dispose of such Bond only pursuant to a Bid or Sell Order in accordance with the Auction Procedures or through a Broker-Dealer. *See* Appendix B – Multi-Mode Provisions. The ability to sell Series 2003 Bonds in an Auction may be adversely affected if there are not sufficient buyers willing to purchase all such Bonds at a rate equal to or less than the applicable rate. The Broker-Dealers have advised the City and County that they intend initially to make a market in the Series 2003 Bonds between Auctions; however, the Broker-Dealers are not obligated to make such markets, and no assurance can be given that secondary markets thereof will develop.

For a further description the terms applicable to the Series 2003 Bonds while they bear interest at an Auction Rate and a description of the provisions for conversion to a different interest rate mode, see Appendix B – “Multi-Mode Provisions.”

Principal of the Series 2003 Bonds will be payable at the office of BNY Western Trust Company, as paying agent (the “Paying Agent”). Interest on the Series 2003 Bonds will be payable to Holders thereof registered as of the close of business on the Record Date, which, for Series 2003 Bonds bearing interest at an Auction Rate is the second Business Day preceding each Interest Payment Date, as described in Appendix B.

Optional Redemption

The Series 2003 Bonds which then bear an Auction Rate are subject to optional redemption prior to maturity, upon the exercise by the City and County of its option to prepay all or a portion of the Series 2003 Bonds, during any Auction Period, on any Interest Payment Date in whole or in part, at a Redemption Price equal to 100% of the principal amount of the Series 2003 Bonds to be redeemed. If interest on any Series 2003 Bonds is converted to a different Variable Rate or a Fixed Rate, such Bonds will be subject to redemption as described in the Series 2003 Certificate.

Mandatory Redemption

The Series 2003A Bonds and the Series 2003B Bonds, respectively, are also subject to redemption, in part, on each of the dates and in the respective principal amounts set forth below, at a Redemption Price of 100% of the principal amount thereof, plus accrued interest to the date of redemption, from mandatory Sinking Fund Installments which are required to be made in amounts sufficient to redeem the principal amount of Series 2003 Bonds specified for July 1 of each of the years shown below:

Series 2003A-1 Bonds

<u>Year (July 1)</u>	<u>Principal Amount</u>
2007	\$1,250,000
2008	1,250,000
2009	1,350,000
2010	1,350,000
2011	1,450,000
2012	1,500,000
2013	1,550,000
2014	1,600,000
2015	1,700,000
2016	1,750,000
2017	1,800,000
2018	1,900,000
2019	2,000,000
2020	2,050,000
2021	2,100,000
2022	2,250,000
2023	2,300,000
2024	2,400,000
2025	2,500,000
2026	2,600,000
2027	2,700,000
2028	2,800,000
2029	2,950,000
2030	3,050,000
2031	3,150,000
2032†	3,300,000

Series 2003A-2 Bonds

<u>Year (July 1)</u>	<u>Principal Amount</u>
2007	\$1,250,000
2008	1,250,000
2009	1,350,000
2010	1,350,000
2011	1,450,000
2012	1,500,000
2013	1,550,000
2014	1,600,000
2015	1,700,000
2016	1,750,000
2017	1,800,000
2018	1,900,000
2019	2,000,000
2020	2,050,000
2021	2,100,000
2022	2,250,000
2023	2,300,000
2024	2,400,000
2025	2,500,000
2026	2,600,000
2027	2,700,000
2028	2,800,000
2029	2,950,000
2030	3,050,000
2031	3,150,000
2032†	3,300,000

† Final maturity

<u>Series 2003B-1 Bonds</u>		<u>Series 2003B-2 Bonds</u>	
<u>Year (July 1)</u>	<u>Principal Amount</u>	<u>Year (July 1)</u>	<u>Principal Amount</u>
2007	\$1,200,000	2007	\$1,200,000
2008	1,300,000	2008	1,300,000
2009	1,300,000	2009	1,300,000
2010	1,400,000	2010	1,400,000
2011	1,400,000	2011	1,400,000
2012	1,500,000	2012	1,500,000
2013	1,550,000	2013	1,550,000
2014	1,650,000	2014	1,650,000
2015	1,650,000	2015	1,650,000
2016	1,750,000	2016	1,750,000
2017	1,850,000	2017	1,850,000
2018	1,900,000	2018	1,900,000
2019	1,950,000	2019	1,950,000
2020	2,050,000	2020	2,050,000
2021	2,150,000	2021	2,150,000
2022	2,200,000	2022	2,200,000
2023	2,300,000	2023	2,300,000
2024	2,400,000	2024	2,400,000
2025	2,500,000	2025	2,500,000
2026	2,600,000	2026	2,600,000
2027	2,700,000	2027	2,700,000
2028	2,850,000	2028	2,850,000
2029	2,900,000	2029	2,900,000
2030	3,050,000	2030	3,050,000
2031	3,200,000	2031	3,200,000
2032†	3,300,000	2032†	3,300,000

† Final maturity.

Notice of Redemption

The Paying Agent will mail notice of redemption not less than 30 days prior to the redemption date by registered, certified or regular first-class mail, to the registered owners of any of the Series 2003 Bonds or portions of the Series 2003 Bonds which are to be redeemed, at their last addresses appearing upon the Bond Registry. The City and County may also but is not required to cause such notice to be published at least once in such newspapers as provided in the Bond Resolution not less than 30 days prior to the date fixed for redemption date. Failure of the City and County to publish any such notice shall not affect the validity of the proceedings for the redemption of such Series 2003 Bonds. See “Book-Entry System” below.

Effect of Redemption

If, on the redemption date, moneys for the redemption of all the Series 2003 Bonds or portions thereof of any maturity to be redeemed, together with interest to the redemption date, shall be held by the City and County or Paying Agent so as to be available therefor on said date and if notice of redemption shall have been given as provided in the Bond Resolution, then, from and after the redemption date, interest on the Series 2003 Bonds or portions thereof of such maturity so called for redemption shall cease to accrue and become payable. If such moneys shall not be so available on the redemption date, such Series 2003 Bonds or portions thereof shall continue to bear interest until paid at the same rate as they would have borne had they not been called for redemption.

Selection for Redemption

So long as the book-entry system for the Series 2003 Bonds is in effect, if less than all of the Series 2003 Bonds of any one maturity are to be redeemed, the particular Series 2003 Bonds or portions of Series 2003 Bonds of such maturity to be redeemed will be selected by DTC and its Participants in such manner as DTC and its Participants may determine. If the book-entry system for the Series 2003 Bonds is no longer in effect, selection for redemption of less than all Series 2003 Bonds of any one maturity will be made by the Paying Agent by lot as provided in the Bond Resolution.

Conversion Provisions

At the option of the City and County, all or any part of either the Series 2003A Bonds or the Series 2003B Bonds bearing interest at an Auction Rate may be converted to bear interest at an Adjustable Rate or a Fixed Rate prior to their maturity (each, a "Conversion"), subject to the conditions set forth in the Series 2003 Certificate. On the date of any such Conversion, such Bonds will be subject to mandatory tender at a purchase price equal to the principal amount thereof, plus accrued interest, if any, to (but not including) the purchase date, but only if the conditions to such Conversion are satisfied, all as more fully set forth in Appendix B hereto.

Book-Entry System

The Depository Trust Company ("DTC"), New York, New York, will act as securities depository for the Series 2003 Bonds. The Series 2003 Bonds will be issued as fully-registered securities in the name of Cede & Co. (DTC's partnership nominee). One fully-registered Series 2003 Bond certificate will be issued for each maturity of each Series of the Series 2003 Bonds, each in the aggregate principal amount of such maturity of such series, and will be deposited with DTC.

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

Purchases of Series 2003 Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Series 2003 Bonds on DTC's records. The ownership interest of each actual purchaser of each Series 2003 Bond ("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 Series 2003 Bonds are to be accomplished by entries made on the books of Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Series 2003 Bonds, except in the event that use of the book-entry system for the Series 2003 Bonds is discontinued.

To facilitate subsequent transfers, all Series 2003 Bonds deposited by Participants with DTC and their registration in the name of Cede & Co. or other nominee of DTC effect no change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Series 2003 Bonds; DTC's records reflect only the identity of

the Direct Participants to whose accounts such Series 2003 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.

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 Bonds within a maturity of a Series of the Series 2003 Bonds are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such maturity to be redeemed.

Neither DTC nor any nominee will consent or vote with respect to Series 2003 Bonds. Under its usual procedures, DTC mails an omnibus proxy (the "Omnibus Proxy") to the City and County 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 Series 2003 Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

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

The City and County and the Paying Agent may treat DTC (or its nominee) as the sole and exclusive registered owner of the Series 2003 Bonds for the purpose of payment of the principal and redemption premium, if any, of, or interest on, the Series 2003 Bonds, giving any notice permitted or required to be given to registered owners under the Bond Resolution, registering the transfer of the Series 2003 Bonds, or other action to be taken by registered owners and for all other purposes whatsoever. The City and County and the Paying Agent shall not have any responsibility or obligation to any Participant, any person claiming a beneficial ownership interest in the Series 2003 Bonds under or through DTC or any Participant, or any other person which is not shown on the registration books of the City and County (kept by the Paying Agent) as being a registered owner, with respect to the accuracy of any records maintained by DTC or any Participant; the payment by DTC or any Participant of any amount in respect of the principal, redemption premium, if any, or interest on the Series 2003 Bonds; any notice which is permitted or required to be given to registered owners thereunder or under the conditions to transfers or exchanges adopted by the City and County; or other action taken by DTC as registered owner. Interest, redemption premium, if any, and principal will be paid by the Paying Agent to DTC, or its nominee. Disbursement of such payments to the Participants is the responsibility of DTC and disbursement of such payments to the Beneficial Owners is the responsibility of the Participants or the Indirect Participants.

For every transfer and exchange of beneficial ownership of any of the Series 2003 Bonds, a Beneficial Owner may be charged a sum sufficient to cover any tax, fee or other governmental charge that may be imposed in relation thereto.

DTC may discontinue providing its service with respect to the Series 2003 Bonds at any time by giving notice to the City and County and discharging its responsibilities with respect thereto under applicable law, or the City and County may terminate its participation in the system of book-entry transfer through DTC at any time by giving notice to DTC. In either event, the City and County may retain another securities depository for the Series 2003 Bonds or may direct the Paying Agent to deliver bond certificates in accordance with instructions from DTC or its successor. If the City and County directs the Paying Agent to deliver such bond certificates, such Series 2003 Bonds may thereafter be exchanged for an equal aggregate principal amount of Series 2003 Bonds in any other

authorized denominations and of the same maturity as set forth in the Bond Resolution, upon surrender thereof at the principal corporate trust office of the Paying Agent, who will then be responsible for maintaining the registration books of the City and County.

Unless otherwise noted, certain of the information contained in the preceding paragraphs of this subsection "Book-Entry Only System" has been extracted from information provided by DTC. Neither the City and County, the Paying Agent nor the Underwriters make any representation as to the completeness or the accuracy of such information or as to the absence of material adverse changes in such information subsequent to the date hereof.

Neither the City and County nor the Paying Agent will have any responsibility or obligations to such DTC Participants, Indirect Participants, or the persons for whom they act as nominees with respect to the payments to or the providing of notice for such DTC Participants, Indirect Participants, or the Beneficial Owners. Payments made to DTC or its nominee shall satisfy the City and County's obligation under the Bond Resolution to the extent of such payments.

So long as Cede & Co. is the registered owner of the Series 2003 Bonds, as nominee for DTC, references herein to the Bondholders or registered owners of the Series 2003 Bonds (other than under the captions "TAX MATTERS" and "CONTINUING DISCLOSURE" herein) shall mean Cede & Co., as aforesaid, and shall not mean the Beneficial Owners of the Series 2003 Bonds.

SECURITY FOR THE BONDS

General

The Bonds issued under and pursuant to the Bond Resolution, including the Series 2003 Bonds, are limited special obligations of the City and County. Pursuant to the Bond Resolution, there has been pledged, as security for the payment of the debt service on the Bonds, proceeds of the Bonds held or set aside under the Bond Resolution, the Net Revenues, and all Funds and Accounts established by the Bond Resolution other than the Rebate Account, the Third Lien Obligation Subaccount and, in certain instances pursuant to the Bond Resolution, the Common Reserve Subaccount or Separate Series Reserve Subaccounts. The Bonds are equally and ratably payable and secured under the Bond Resolution except that the City and County has reserved the right under the Bond Resolution to afford a particular Series of Bonds or particular Bonds additional or different security through a Support Facility, escrow funds, or the establishment of separate funds and accounts with respect to a particular Series of Bonds funded from sources other than the Net Revenues.

Under the Bond Resolution, Net Revenues means, with respect to any period, the Revenues during such period less amounts required to pay Operation and Maintenance Expenses. Revenues means (i) the Revenues under the First Bond Resolution; (ii) all income from investments of moneys held under the Bond Resolution except the Rebate Subaccount and the Third Lien Obligation Subaccount; and (iii) all payments made by Counterparties pursuant to Interest Rate Exchange Agreements. Revenues under the First Bond Resolution means the moneys, including any moneys collected from the City and County or any department thereof other than the Department, derived by the Department from the rates, rentals, fees and charges prescribed for the use and services of, and the facilities and commodities furnished by, the Wastewater System. Revenues under the First Bond Resolution include (i) all income, receipts, profits, and other moneys derived from the furnishing or supplying of the services, facilities and commodities through the Wastewater System; (ii) all income from investments of moneys held under the Bond Resolution except the Rebate Account, the Subordinate Obligation Account or the Reimbursable Obligation Account; (iii) all payments made by Counterparties pursuant to Interest Rate Exchange Agreements; and (iv) moneys and Investment Securities transferred from the Rate Stabilization Account to the Sewer Fund within 90 days following the end of a Fiscal Year. Certain items do not constitute Revenues under the Bond Resolution, including certain deposits subject to refund, certain contributions in-aid-of construction and assessment, impact and other similar fees imposed and collected by the City and County, income, fees, charges, receipts, profits or other moneys derived by the Department from the ownership or operation of any separate utility system, and certain gifts, grants and donations, moneys and Investment Securities transferred from the Sewer Fund to the Rate Stabilization Account within 90 days following the end of a Fiscal Year, or Wastewater System Facility Charges.

The pledge of the Net Revenues for the security and payment of the Bonds under the Bond Resolution is (i) junior and subordinate to the pledge made in the First Bond Resolution for the security and payment of the First

Resolution Obligations; and (ii) prior and superior to the pledge made in the First Bond Resolution for the security and payment of the Reimbursable Obligations authorized to be issued pursuant to the First Bond Resolution and in the Bond Resolution for the security and payment of Third Lien Obligations authorized to be issued pursuant to the Bond Resolution. "Reimbursable Obligations" are reimbursable general obligation bonds issued and delivered or to be issued and delivered by the City and County to finance certain costs related to the Wastewater System. The debt service on Reimbursable Obligations is paid from moneys in the City and County's general fund. Pursuant to State law, the amount of such debt service may be reimbursed from the Net Revenues. There are currently \$67,644,502 principal amount of Reimbursable Obligations outstanding. "Third Lien Obligations" are any obligations of the City and County payable from the Revenues, other than the First Resolution Obligations, the Bonds and the Reimbursable Obligations, issued in compliance with the provisions of the First Bond Resolution or the Bond Resolution, as applicable. There are currently no Third Lien Obligations outstanding.

The Series 2003 Bonds will constitute Bonds under the Bond Resolution. The Series 2003 Bonds are the second and third Series of Bonds to be issued under the Bond Resolution. The City and County expects to issue additional Bonds under the Bond Resolution on a parity with the Series 2003 Bonds.

The Bonds are not a general or moral obligation of the State of Hawaii or any political subdivision thereof, including the City and County, and the faith and credit of the State of Hawaii or any political subdivision thereof, including the City and County, are not pledged to the payment of the principal of, redemption price of, if any, or interest on, the Bonds, and no holder of the Bonds shall have the right to compel the exercise of the taxing power of the State of Hawaii or any political subdivision thereof, including the City and County, in connection with any default with respect to the Bonds.

Funds and Accounts

The various funds and accounts established under or pledged by the Bond Resolution, the flow of Revenues through such funds and accounts, the rights and remedies of Bondholders under the Bond Resolution and other related matters are summarized in Appendix C, "Summary of Certain Provisions of the Bond Resolution."

The City and County has established the Sewer Fund by ordinance. Revenues are deposited in the Sewer Fund. The First Bond Resolution establishes various accounts in the Sewer Fund, none of which except the Subordinate Obligation Account is pledged as security for the payment of debt service on the Bonds. Such pledge of the Subordinate Obligation Account is subject to the terms and provisions of and the exceptions provided in the First Bond Resolution and the Bond Resolution. Under the First Bond Resolution, the Department will, in each month, transfer from the Sewer Fund to the Subordinate Obligation Account a sufficient amount required by the Bond Resolution to pay all accrued and unpaid amounts and amounts to accrue and become payable during the succeeding calendar month which are payable from the Subordinate Obligation Account, but only (i) after making the transfer, if any, to the Wastewater System Facility Charge Account of all moneys received as Wastewater System Facility Charges, (ii) after paying or setting aside a sufficient amount to pay the Operating and Maintenance Expenses, (iii) after making the transfer to the Rebate Account under the First Bond Resolution, (iv) after transferring a sufficient amount to the Debt Service Account under the First Bond Resolution to pay debt service on First Resolution Obligations, and (v) after transferring a sufficient amount to the Common Reserve Account and each Separate Series Reserve Account under the First Bond Resolution to eliminate any deficiency therein, and (vi) after maintaining in the Sewer Fund a reasonable and necessary amount for working capital and operating reserves.

The Bond Resolution establishes in the Subordinate Obligation Account a Debt Service Subaccount. The Debt Service Subaccount is pledged as security for the payment of debt service on all Bonds subject to the terms and provisions of and the exceptions provided in the Bond Resolution. The Bond Resolution also establishes a Common Reserve Subaccount in the Subordinate Obligation Account and permits the establishment in the Subordinate Obligation Account of one or more Separate Series Reserve Subaccounts. The Common Reserve Subaccount is pledged as additional security for the payment of debt service on the Bonds of such Series designated by the City and County to be entitled to the benefit of the Common Reserve Subaccount. Each Separate Series Reserve Subaccount is pledged as additional security for the payment of debt service on the Bonds of such individual Series designated by the City and County to be entitled to the benefit of such Separate Series Reserve Subaccount.

The debt service on and redemption price of the Bonds are payable from the Debt Service Subaccount in the Subordinate Obligation Account. In the event of a deficiency in the Debt Service Subaccount, the debt service on and redemption price of particular Bonds are payable from the Common Reserve Subaccount or the Separate Series Reserve Subaccounts, as applicable, but only if such Bonds are entitled to the benefit of such Reserve Subaccounts.

Under the First Bond Resolution, moneys deposited and retained in the Sewer Fund may be maintained in an amount which is reasonable and necessary for working capital and reserves. The First Bond Resolution establishes, among other accounts, the Rate Stabilization Account, the Renewal and Replacement Account and the Wastewater General Account. Such accounts are not pledged as security for the payment of debt service on and redemption price of the Bonds. However, moneys in such accounts may be transferred to the Subordinate Obligation Account on the terms and conditions as provided in the First Bond Resolution. The Rate Stabilization Account is to be used to stabilize the rates and charges of the Wastewater System. The Rate Stabilization Account is to be maintained in an amount as provided in the Annual Budget and is to be funded as provided in the Annual Budget from (i) the Revenues but only after paying the Operation and Maintenance Expenses and after transferring required amounts to other funds and accounts as provided in the First Bond Resolution, and (ii) transfers from the Wastewater General Account. The Renewal and Replacement Account is to be used to pay the costs of improvements to or reconstruction of the Wastewater System, repairs, major or extraordinary repairs and renewals or replacements of the Wastewater System and under certain conditions, as set forth in the Bond Resolution, to meet deficiencies in the Debt Service Subaccount, the Common Reserve Account, Separate Series Reserve Accounts, if any, the Subordinate Obligation Account, including the Debt Service Subaccount, the Common Reserve Subaccount and all Separate Series Subaccounts, and the Reimbursable Obligation Account, and will be maintained in an amount provided for in the Annual Budget. The Wastewater General Account may be used for any lawful purpose of the City and County, including funding of the Rate Stabilization Account, and under certain conditions, may be used to meet deficiencies in the Sewer Fund, the Common Reserve Account, Separate Series Reserve Accounts, if any, the Renewal and Replacement Account, the Rebate Account, the Subordinate Obligation Account and the Reimbursable Obligation Account.

The Bond Resolution also establishes in the Subordinate Obligation Account a Rebate Subaccount and a Third Lien Obligation Subaccount. Such accounts are not pledged as security for the Series 2003 Bonds, or any other Bonds. The funds in the Third Lien Obligation Subaccount are to be used to pay debt service on and redemption price of Third Lien Obligations, provide necessary debt service reserves and other reserves and pay other costs related to Third Lien Obligations. The funds in the Rebate Subaccount are to be used to pay required rebates to the United States Treasury Department incurred in respect of the Bonds.

The First Bond Resolution also establishes in the Sewer Fund, the Wastewater System Facility Charge Account. Wastewater System Facility Charges collected by the Department are deposited in the Wastewater System Facility Charge Account. The Wastewater System Facility Charge Account is pledged under the First Bond Resolution as security for the payment of debt service on and redemption price of the First Resolution Obligations but not for the Bonds. If any amounts are used to pay the debt service on or redemption price of First Resolution Obligations, the Wastewater System Facility Charge Account must be reimbursed from the Net Revenues with the priority set forth in the First Bond Resolution. The Wastewater System Facility Charges are not considered to be Revenues under the First Bond Resolution.

The City and County has also established by ordinance the Improvement Fund. The Bond Resolution establishes in the Improvement Fund an Improvement Second Account and permits the establishment within the Improvement Second Account of one or more Series Improvement Second Subaccounts and one or more Series Improvement Second Interest Subaccounts. Proceeds of Bonds issued under the Bond Resolution are to be deposited in the Improvement Second Account or a Series Improvement Second Subaccount pending application to pay the Costs of Improvements. Proceeds of Bonds issued under the Bond Resolution which are to be used to pay capitalized interest on the Bonds of a Series during the period of construction of an Improvement and for six months thereafter must be deposited in a Series Improvement Second Interest Subaccount. The Improvement Second Account, each Series Improvement Second Subaccount and each Series Improvement Second Interest Subaccount (but not the Improvement Fund) are pledged under the Bond Resolution as security for the payment of debt service on and redemption price of the Bonds.

Common Reserve Subaccount and Separate Series Reserve Subaccounts

Common Reserve Subaccount. The Bond Resolution establishes a Common Reserve Subaccount. Under the Bond Resolution, the City and County may designate one or more Series of Bonds to be entitled to the benefit of the Common Reserve Subaccount. The Series 2003 Bonds are entitled to the benefit of the Common Reserve Subaccount. The moneys held in the Common Reserve Subaccount are to be used to pay debt service on the Bonds entitled to the benefit of the Common Reserve Subaccount in the event of a deficiency in the Debt Service Subaccount to pay such debt service. The Common Reserve Subaccount is to be maintained in an amount not less than the Common Reserve Subaccount Requirement. The Common Reserve Subaccount Requirement is an amount that is equal to the greatest amount of Aggregate Debt Service for the then current or any future Fiscal Year on all Outstanding Bonds entitled to the benefit of the Common Reserve Subaccount; provided, however, that if upon the issuance of a Series of Bonds entitled to the benefit of the Common Reserve Subaccount, such amount would require moneys credited to the Common Reserve Subaccount from the proceeds of such Bonds in an amount in excess of the maximum amount permitted under the Code, the Common Reserve Subaccount Requirement will then be the Common Reserve Subaccount Requirement immediately preceding the issuance of such Bonds and the maximum amount permitted under the Code to be deposited from the proceeds of such Bonds, as certified by an Authorized Officer. The Bond Resolution provides that the Aggregate Debt Service is to be computed with respect to each Variable Rate Bond entitled to the benefit of the Common Reserve Subaccount by using the Assumed Long-Term Fixed Rate.

In lieu of cash or securities, the Bond Resolution permits the Department to satisfy the Common Reserve Subaccount Requirement in part or in whole by causing to be deposited into the Common Reserve Subaccount a Support Facility (which may be an irrevocable letter of credit, surety bond, loan agreement, standby bond purchase agreement, or other agreement facility or insurance or guaranty agreement issued by a bank or banks, or other financial institution or institutions, or any combination of the foregoing) in an amount equal to the difference between the Common Reserve Subaccount Requirement and the sums then on deposit in the Common Reserve Subaccount, if any. The Support Facility must be payable (upon the giving of notice as required thereunder) on or before any interest payment date on which moneys will be required to be withdrawn from the Common Reserve Subaccount and applied to the payment of principal or redemption price of or interest on any Bonds and such withdrawal cannot be met by amounts on deposit in the Common Reserve Subaccount or provided from any other available Fund under the Bond Resolution. Any Support Facility deposited in the Common Reserve Subaccount or the long-term debt of the issuer of any Support Facility deposited in the Common Reserve Subaccount must, in each case, be rated in the highest rating category by each Rating Agency and, if rated by A.M. Best & Company, must also be rated in the highest rating category by A.M. Best & Company or its successors. In the event any Support Facility deposited in the Common Reserve Subaccount or the long-term debt of the issuer of any Support Facility deposited in the Common Reserve Subaccount falls below the second highest rating category of each Rating Agency, and A.M. Best & Company, if rated by A.M. Best & Company, the City and County must, within 120 days, obtain a new Support Facility which, or which the long-term debt of the issuer of such new Support Facility, is rated in the highest rating category of such rating agencies; provided, however, that if the new Support Facility is not obtained within 120 days, the City and County must deposit in the Common Reserve Subaccount Net Revenues in the amount provided in the Bond Resolution. If a disbursement is made pursuant to a Support Facility deposited in the Common Reserve Subaccount, the City and County must: first, reinstate the full amount of such Support Facility; and second, if necessary, deposit Net Revenues in the Common Reserve Subaccount in the amount of the disbursement made under such Support Facility, in either case such that the amount in the Common Reserve Subaccount will equal the Common Reserve Subaccount Requirement within a period of time not longer than would be required to restore the Common Reserve Subaccount by application of moneys in the Sewer Fund as required by the Bond Resolution. The City and County may at any time deposit cash or Investment Securities as replacement for one or more Support Facilities.

The City and County has arranged for the delivery of a Support Facility in the form of a surety bond in an amount equal to the full amount of the Common Reserve Subaccount Requirement, replacing the Investment Securities previously on deposit therein, as well as funding the additional requirement for the Series 2003 Bonds.

Separate Series Reserve Subaccounts. The Bond Resolution permits the establishment of a Separate Series Reserve Subaccount to provide additional security for the Bonds of a Series which are not entitled to the benefit of the Common Reserve Subaccount. In the event of a deficiency in the Debt Service Subaccount to pay debt service

on the Bonds of a Series entitled to the benefit of a Separate Series Reserve Subaccount, the amounts held in such Separate Series Reserve Subaccount are to be used exclusively to pay such debt service. The amount to be maintained in any such Separate Series Reserve Subaccount for a Series of Bonds is to be determined at the time such Bonds are authorized or sold. The credit quality of a Support Facility to be deposited in any Separate Series Reserve Subaccount for a Series of Bonds is also to be determined at the time such Bonds are authorized or sold. No Separate Series Reserve Subaccount has been established for the Series 2003 Bonds.

Transfers to Reserve Subaccounts. The Bond Resolution requires that in each month, after transferring to the Debt Service Subaccount an amount sufficient to pay debt service on the Bonds to accrue in such month, moneys in the Subordinate Obligation Account are to be transferred pro rata to the Common Reserve Subaccount and each Separate Series Reserve Subaccount in such amounts as are required so that the balances in the Common Reserve Subaccount and each Separate Series Reserve Subaccount are equal to their respective requirements, or at the election of the Department; so that at least one-sixth of any deficiency in the Common Reserve Subaccount or each Separate Series Reserve Subaccount is eliminated.

Rate Covenant

The City and County is required by the Bond Resolution, among other things, to fix, charge and collect such rates and other charges as shall be required in order that in each Fiscal Year the Net Revenues shall not be less than the Net Revenue Requirement for such Fiscal Year. The Net Revenue Requirement means with respect to any Fiscal Year or any period, an amount equal to the greater of: (i) the sum of (a) the Aggregate Debt Service under the First Bond Resolution and the Aggregate Debt Service in such Fiscal Year or such period and (b) the Required Deposits for such Fiscal Year or such period; or (ii) 1.10 times the Aggregate Debt Service (as defined in the First Bond Resolution) under the First Bond Resolution and 1.10 times the Aggregate Debt service in such Fiscal Year or such period plus 1.00 times the aggregate Support Facility Reimbursement Obligations outstanding as of the end of such Fiscal Year or such period. Net Revenues means, with respect to any period, the Revenues during such period less amounts required to pay Operation and Maintenance Expenses. Required Deposits means, for any period, (i) the Required Deposits under the First Bond Resolution exclusive of transfers from the Sewer Fund to the Subordinate Obligation Account; and (ii) the amounts, if any, required: (a) to be paid into the Rebate Subaccount, the Common Reserve Subaccount, each Separate Series Reserve Subaccount, and the Third Lien Obligation Subaccount, and (b) to pay Support Facility Reimbursement Obligations. Required Deposits under the First Bond Resolution means, for any period, the amounts, if any, required: (i) to be paid into the Common Reserve Account, each Separate Series Reserve Account, the Subordinate Obligation Account and the Reimbursable Obligation Account under the First Bond Resolution; and (ii) to pay Support Facility Reimbursement Obligations under the First Bond Resolution. Aggregate Debt Service means, for any period and as of any date of computation, the sum of the amounts of Debt Service for such period with respect to all Series of Bonds or all First Resolution Obligations, as applicable. Support Facility Reimbursement Obligations are obligations of the City and County to directly reimburse the Support Facility Provider of a Support Facility for amounts paid thereunder or a Counterparty under an Interest Rate Exchange Agreement for amounts paid, whether or not such obligation to reimburse is evidenced by a promissory note or similar instrument.

Failure by the City and County to comply with the foregoing rate covenant in any Fiscal Year will not constitute an Event of Default under the Bond Resolution so long as the provisions of the Bond Resolution described below are complied with. Prior to the end of each Fiscal Year the Director of Environmental Services or the Director of Budget and Fiscal Services if requested by the Director of Environmental Services is required by the Bond Resolution to complete a review of the financial condition of the Department for the purpose of estimating whether the Net Revenues for such Fiscal Year and for the next succeeding Fiscal Year will be sufficient to comply with the foregoing rate covenant and to make a written certification with respect to compliance or noncompliance. Such review is to take into consideration the completion of any uncompleted Improvements and the issuance of future Series of Bonds if necessary to finance the completion of such Improvements. Such written certification is to set forth a reasonably detailed statement of the actual and estimated Revenues, Operation and Maintenance Expenses, Aggregate Debt Service, and any other estimates or assumptions upon which such determination was based, shall be filed with the City Clerk on or before July 1 in each year. If it is determined in such written certification that the Revenues may not be so sufficient, the Director of Environmental Services or the Director of Budget and Fiscal Services if requested by the Director of Environmental Services must forthwith make a study for the purpose of determining a schedule of fees, rates and charges which, in the opinion of the Director of

Environmental Services or the Director of Budget and Fiscal Services, will cause sufficient Revenues to be collected in the following Fiscal Year to comply with such rate covenant, or the Director of Environmental Services or the Director of Budget and Fiscal Services may elect to cause the Consulting Engineer to make such a study and render such certification. The City Council, as promptly as practicable but no later than 120 days following such determination by the Director of Environmental Services or the Director of Budget and Fiscal Services, or receipt of the Consulting Engineer's recommendation, is required to adopt and place in effect a schedule of fees, rates and charges as so determined or recommended. See "CERTAIN FINANCIAL, OPERATING AND OTHER INFORMATION AND STATISTICS - Summary of Current Sewer Rate Ordinance" for current sewer charges, "HISTORICAL AND PROJECTED REVENUES, EXPENSES AND COVERAGES" for a discussion of the Department's projected rates, revenues and expenses, and "THE CITY AND COUNTY AND THE DEPARTMENT - Purpose and Powers" for a discussion of the rate making powers of the City Council.

Additional Bonds and Refunding Bonds

The Bond Resolution permits the issuance of additional Series of Bonds (exclusive of refunding Bonds) on a parity with the Bonds then Outstanding ("Additional Bonds") for any lawful use or purpose relating to the Wastewater System, including, without limitation, payment of all or a portion of the Costs of Improvements, but only upon compliance as to each such Series with the conditions set forth in the Bond Resolution. The Series 2003 Bonds are being issued as Additional Bonds under the Bond Resolution and their issuance is subject to compliance with such conditions, which include delivery to the Director of Budget and Fiscal Services of the following documents or moneys or securities:

1. A written certificate of the City and County stating the amount required to be in the Common Reserve Subaccount after issuance of the Bonds then to be issued and that the amounts deposited will not be less than the Common Reserve Subaccount Requirement.

2. A written certificate of the City and County stating the amount required to be in the Separate Series Reserve Subaccount established for the Bonds of such Series after issuance of the Bonds then to be issued and that the amounts deposited will not be less than the Separate Series Reserve Subaccount Requirement for the Bonds of such Series.

3. Either:

(I) a written certificate of the City and County based: (i) on audited figures or (ii) to the extent audited figures are not available, on figures taken by an independent certified public accountant from the Department's books and records, showing that the Net Revenues for: (a) the most recent Fiscal Year, or (b) any consecutive 12-month period out of 24 months immediately preceding the month in which such Bonds are issued were not less than the greater of: (x) the sum of (1) the maximum of the sum of the Aggregate Debt Service on all First Resolution Obligations issued and outstanding under and pursuant to the First Bond Resolution and the Aggregate Debt Service on all Bonds then Outstanding and on the proposed Series of Bonds in any Fiscal Year and the 12-month period selected and (2) the Required Deposits for such Fiscal Year or the 12-month period selected; and (y) the sum of (1) 1.10 times the maximum sum of the Aggregate Debt Service on all First Resolution Obligations issued and outstanding under and pursuant to the First Bond Resolution and the Aggregate Debt Service on all Bonds then Outstanding and on the proposed Series of Bonds in any Fiscal Year and the 12-month period selected, and (2) 1.00 times the aggregate Support Facility Reimbursement Obligations outstanding under the First Bond Resolution and the Bond Resolution as of the date of the written certificate of the City and County; or

(II) a written certificate of the City and County or Certificate of the Consulting Engineer that the Net Revenues to be derived in each of the five (5) Fiscal Years following the earlier of: (i) the end of the period during which interest is capitalized or, if no interest is to be capitalized, the Fiscal Year in which the proposed Series of Bonds are issued, and (ii) the date on which substantially all Improvements to be financed with the proceeds of the proposed Series of Bonds are expected to commence operations, or, if the proceeds of such Series of Bonds will not be used to fund the Costs of Improvements, the Fiscal Year in which the proposed Series of Bonds are issued, are estimated to be not less than the greater of: (x) the sum of (1) the maximum of the sum of the Aggregate Debt Service on all First Resolution Obligations issued under and pursuant to the First Bond Resolution and the Aggregate Debt

Service on all Bonds then Outstanding and on the proposed Series of Bonds in any such Fiscal Year, and (2) the Required Deposits for any such Fiscal Year; and (y) the sum of (1) 1.10 times the maximum of the sum of the Aggregate Debt Service on all First Resolution Obligations issued under and pursuant to the First Bond Resolution and the Aggregate Debt Service on all Bonds then Outstanding and on the proposed Series of Bonds in any such Fiscal Year, and (2) 1.00 times the aggregate Support Facility Reimbursement Obligations outstanding under the First Bond Resolution and the Bond Resolution as of the date of such written certificate of the City and County or certificate of the Consulting Engineer, as the case may be.

In determining Net Revenues for purposes of the certificates described above, the City and County or the Consulting Engineer, as the case may be, is permitted, and in certain instances is required, to make certain adjustments as provided in the Bond Resolution. In addition, the Bond Resolution requires that certain other adjustments to Net Revenues derived from Debt Service on Variable Rate Bonds and debt service on Bond Anticipation Notes and short-term Third Lien Obligations and Reimbursable Obligations be made for purposes of the written certificates described above. See Appendix C, "Summary of Certain Provisions of the Bond Resolution."

Bonds may be issued as variable rate bonds, fixed rate bonds, bonds providing for the right of the owner thereof to present the Bond for redemption or purchase prior to maturity, zero interest rate or deep discount bonds, bonds providing for the compounding of interest, or any combination thereof. Bonds may be issued or outstanding from time to time with or without credit enhancement provisions. See Appendix C, "Summary of Certain Provisions of the Bond Resolution."

The Bond Resolution also permits the issuance of Bonds ("Refunding Bonds") on a parity with the Bonds then Outstanding to refund all or any part of: (i) a Series of Outstanding Bonds; (ii) Third Lien Obligations; or (iii) Reimbursable Obligations. Refunding Bonds may only be issued by the City and County upon satisfaction of certain conditions set forth in the Bond Resolution.

A more detailed description of the requirements relating to the issuance of Additional Bonds or Refunding Bonds is set forth in Appendix C under "Additional Bonds and Refunding Bonds."

The Bond Resolution also permits the issuance of notes in anticipation of a Series of Bonds if the City and County has theretofore authorized the issuance of such Bonds. The interest on such notes (and any renewal thereof) shall be payable from the proceeds of such notes or other notes or from the proceeds of the sale of the Bonds in anticipation of which such notes are issued. A more detailed description of the provisions for security for payment of such notes and other requirements relating to the issuance of notes is set forth in Appendix C under "Bond Anticipation Notes."

BOND INSURANCE

The following information has been furnished by MBIA Insurance Corporation (the "Bond Insurer") for use in this Official Statement. Reference is made to Appendix F for a specimen of the bond insurance policy (the "Policy") which has been provided for use herein.

The Policy unconditionally and irrevocably guarantees the full and complete payment required to be made by or on behalf of the City and County to the Paying Agent or its successor of an amount equal to (i) the principal of (either at the stated maturity or by an advancement of maturity pursuant to a mandatory sinking fund payment) and interest on, the Series 2003 Bonds as such payments shall become due but shall not be so paid (except that in the event of any acceleration of the due date of such principal by reason of mandatory or optional redemption or acceleration resulting from default or otherwise, other than any advancement of maturity pursuant to a mandatory sinking fund payment, the payments guaranteed by the Policy shall be made in such amounts and at such times as such payments of principal would have been due had there not been any such acceleration); and (ii) the reimbursement of any such payment which is subsequently recovered from any owner of the Series 2003 Bonds pursuant to a final judgment by a court of competent jurisdiction that such payment constitutes an avoidable preference to such owner within the meaning of any applicable bankruptcy law (a "Preference").

The Policy does not insure against loss of any prepayment premium which may at any time be payable with respect to any Series 2003 Bonds. The Policy does not, under any circumstance, insure against loss relating to: (i) optional or mandatory redemptions (other than mandatory sinking fund redemptions); (ii) any payments to be

made on an accelerated basis; (iii) payments of the purchase price of Series 2003 Bonds upon tender by an owner thereof; or (iv) any Preference relating to (i) through (iii) above. The Policy also does not insure against nonpayment of principal of or interest on the Series 2003 Bonds resulting from the insolvency, negligence or any other act or omission of the Paying Agent or any other paying agent for the Series 2003 Bonds.

Upon receipt of telephonic or telegraphic notice, such notice subsequently confirmed in writing by registered or certified mail, or upon receipt of written notice by registered or certified mail, by MBIA from the Paying Agent or any owner of a Series 2003 Bonds the payment of an insured amount for which is then due, that such required payment has not been made, MBIA on the due date of such payment or within one business day after receipt of notice of such nonpayment, whichever is later, will make a deposit of funds, in an account with U.S. Bank Trust National Association, in New York, New York, or its successor, sufficient for the payment of any such insured amounts which are then due. Upon presentment and surrender of such Series 2003 Bonds or presentment of such other proof of ownership of the Series 2003 Bonds, together with any appropriate instruments of assignment to evidence the assignment of the insured amounts due on the Series 2003 Bonds as are paid by MBIA, and appropriate instruments to effect the appointment of MBIA as agent for such owners of the Series 2003 Bonds in any legal proceeding related to payment of insured amounts on the Series 2003 Bonds, such instruments being in a form satisfactory to U.S. Bank Trust National Association, U.S. Bank Trust National Association shall disburse to such owners or the Paying Agent payment of the insured amounts due on such Series 2003 Bonds, less any amount held by the Paying Agent for the payment of such insured amounts and legally available therefor.

MBIA

MBIA Insurance Corporation (“MBIA”) is the principal operating subsidiary of MBIA Inc., a New York Stock Exchange listed company (the “Company”). The Company is not obligated to pay the debts of or claims against MBIA. MBIA is domiciled in the State of New York and licensed to do business in and subject to regulation under the laws of all 50 states, the District of Columbia, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, the Virgin Islands of the United States and the Territory of Guam. MBIA has three branches, one in the Republic of France, one in the Republic of Singapore and one in the Kingdom of Spain. New York has laws prescribing minimum capital requirements, limiting classes and concentrations of investments and requiring the approval of policy rates and forms. State laws also regulate the amount of both the aggregate and individual risks that may be insured, the payment of dividends by MBIA, changes in control and transactions among affiliates. Additionally, MBIA is required to maintain contingency reserves on its liabilities in certain amounts and for certain periods of time.

MBIA does not accept any responsibility for the accuracy or completeness of this Official Statement or any information or disclosure contained herein, or omitted herefrom, other than with respect to the accuracy of the information regarding the policy and MBIA set forth under the heading “BOND INSURANCE.” Additionally, MBIA makes no representation regarding the Series 2003 Bonds or the advisability of investing in the Series 2003 Bonds.

MBIA Information

The following documents filed by the Company with the Securities and Exchange Commission (the “SEC”) are incorporated herein by reference:

- (1) The Company’s Annual Report on Form 10-K for the year ended December 31, 2001; and
- (2) The Company’s Quarterly Report on Form 10-Q for the quarter ended September 30, 2002.

Any documents filed by the Company pursuant to Sections 13(a), 13(c), 14 or 15(d) of the Exchange Act of 1934, as amended, after the date of this Official Statement and prior to the termination of the offering of the Series 2003 Bonds offered hereby shall be deemed to be incorporated by reference in this Official Statement and to be a part hereof. Any statement contained in a document incorporated or deemed to be incorporated by reference herein, or contained in this Official Statement, shall be deemed to be modified or superseded for purposes of this Official Statement to the extent that a statement contained herein or in any other subsequently filed document which also is

or is deemed to be incorporated by reference herein modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Official Statement.

The Company files annual, quarterly and special reports, information statements and other information with the SEC under File No. 1-9583. Copies of the SEC filings (including (1) the Company's Annual Report on Form 10-K for the year ended December 31, 2002, and (2) the Company's Quarterly Report on Form 10-Q for the quarters ended March 31, 2002, July 30, 2002 and September 30, 2002), are available (i) over the Internet at the SEC's web site at <http://www.sec.gov>; (ii) at the SEC's public reference room in Washington D.C.; (iii) over the Internet at the Company's web site at <http://www.mbia.com>; and (iv) at no cost, upon request to MBIA Insurance Corporation, 113 King Street, Armonk, New York 10504. The telephone number of MBIA is (914) 273-4545.

As of December 31, 2001, MBIA had admitted assets of \$8.5 billion (audited), total liabilities of \$5.6 billion (audited), and total capital and surplus of \$2.9 billion (audited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities. As of December 31, 2002, MBIA had admitted assets of \$9.2 billion (audited), total liabilities of \$6.0 billion (audited), and total capital and surplus of \$3.1 billion (audited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities.

Financial Strength Ratings of MBIA

Moody's Investors Service, Inc. rates the financial strength of MBIA "Aaa."

Standard & Poor's, a division of The McGraw-Hill Companies, Inc. rates the financial strength of MBIA "AAA."

Fitch Ratings rates the financial strength of MBIA "AAA."

Each rating of MBIA should be evaluated independently. The ratings reflect the respective rating agency's current assessment of the creditworthiness of MBIA and its ability to pay claims on its policies of insurance. Any further explanation as to the significance of the above ratings may be obtained only from the applicable rating agency.

The above ratings are not recommendations to buy, sell or hold the Series 2003 Bonds, and such ratings may be subject to revision or withdrawal at any time by the rating agencies. Any downward revision or withdrawal of any of the above ratings may have an adverse effect on the market price of the Series 2003 Bonds. MBIA does not guaranty the market price of the Series 2003 Bonds nor does it guaranty that the ratings on the Series 2003 Bonds will not be revised or withdrawn.

Surety Bond

Application has been made to the MBIA Insurance Corporation (the "Insurer") for a commitment to issue a surety bond (the "Debt Service Reserve Fund Surety Bond"). The Debt Service Reserve Fund Surety Bond will provide that upon notice from the Paying Agent to the Insurer to the effect that insufficient amounts are on deposit in the Debt Service Subaccount to pay the principal of (at maturity or pursuant to mandatory redemption requirements) and interest on the Series 2003 Bonds and the Junior Series 1998 Bonds (the "Obligations"), the Insurer will promptly deposit with the Paying Agent an amount sufficient to pay the principal of and interest on the Obligations or the available amount of the Debt Service Reserve Fund Surety Bond, whichever is less. Upon the later of: (i) three (3) days after receipt by the Insurer of a Demand for Payment in the form attached to the Debt Service Reserve Fund Surety Bond, duly executed by the Paying Agent; or (ii) the payment date of the Obligations as specified in the Demand for Payment presented by the Paying Agent to the Insurer, the Insurer will make a deposit of funds in an account with U.S. Bank Trust National Association, in New York, New York, or its successor, sufficient for the payment to the Paying Agent, of amounts which are then due to the Paying Agent (as specified in the Demand for Payment) subject to the Surety Bond Coverage.

The available amount of the Debt Service Reserve Fund Surety Bond is the initial face amount of the Debt Service Reserve Fund Surety Bond less the amount of any previous deposits by the Insurer with the Paying Agent which have not been reimbursed by the City and County. The City and County and the Insurer will enter into a Financial Guaranty Agreement dated the date of delivery of the Series 2003 Bonds (the "Agreement"). Pursuant to the Agreement, the City and County is required to reimburse the Insurer, within one year of any deposit, the amount of such deposit made by the Insurer with the Paying Agent under the Debt Service Reserve Fund Surety Bond. Such reimbursement shall be made only after all required deposits to the Wastewater General Account and the Renewal and Replacement Account have been made.

Under the terms of the Agreement, the Paying Agent is required to reimburse the Insurer, with interest, until the face amount of the Debt Service Reserve Fund Surety Bond is reinstated before any deposit is made to the Sewer Fund. No optional redemption of Obligations may be made until the Insurer's Debt Service Reserve Fund Surety Bond is reinstated. The Debt Service Reserve Fund Surety Bond will be held by the Paying Agent in the Common Reserve Subaccount and is provided as an alternative to the City and County depositing funds equal to the Common Reserve Subaccount Requirement for outstanding Obligations. The Debt Service Reserve Fund Surety Bond will be issued in the face amount equal to Common Reserve Subaccount Requirement for the Obligations and the premium therefor will be fully paid by the City and County at the time of delivery of the Obligations.

REVENUE BOND DEBT SERVICE REQUIREMENTS

Years Ending June 30⁽¹⁾

Year	Debt Service on Outstanding Senior Bonds	Debt Service on Outstanding Junior Bonds	Principal Series 2003 Bonds	Interest Series 2003 Bonds ⁽²⁾	Total Series 2003 Debt Service	Total Junior Debt Service	Total Debt Service
2003	\$10,638,831	\$11,460,673	\$ -	\$ -	\$ -	\$11,460,673	\$22,099,504
2004	10,640,931	11,460,673	-	7,277,088	7,277,088	18,737,761	29,378,692
2005	10,641,231	11,460,673	-	11,160,240	11,160,240	22,620,913	33,262,144
2006	12,945,606	11,460,673	-	11,160,240	11,160,240	22,620,913	35,566,519
2007	12,948,581	11,460,673	-	11,160,240	11,160,240	22,620,913	35,569,494
2008	12,948,931	11,460,673	4,900,000	11,034,016	15,934,016	27,394,689	40,343,620
2009	12,947,822	12,341,773	5,100,000	10,778,833	15,878,833	28,220,605	41,168,427
2010	12,945,663	14,148,691	5,300,000	10,512,712	15,812,712	29,961,403	42,907,066
2011	12,947,163	16,868,704	5,500,000	10,236,730	15,736,730	32,635,434	45,582,596
2012	12,944,363	21,331,768	5,700,000	9,950,528	15,650,528	36,982,296	49,926,658
2013	12,945,813	22,905,356	6,000,000	9,651,952	15,651,952	38,557,309	51,503,121
2014	12,945,219	22,906,656	6,200,000	9,339,778	15,539,778	38,446,434	51,391,653
2015	12,947,013	22,911,156	6,500,000	9,015,230	15,515,230	38,426,386	51,373,399
2016	12,943,494	22,912,938	6,700,000	8,677,928	15,377,928	38,290,866	51,234,359
2017	12,943,856	22,916,081	7,000,000	8,328,323	15,328,323	38,244,404	51,188,260
2018	12,947,056	22,919,538	7,300,000	7,962,402	15,262,402	38,181,940	51,128,996
2019	12,947,169	22,922,256	7,600,000	7,581,644	15,181,644	38,103,900	51,051,069
2020	12,949,538	22,918,925	7,900,000	7,185,556	15,085,556	38,004,481	50,954,019
2021	12,948,844	22,922,800	8,200,000	6,774,715	14,974,715	37,897,515	50,846,359
2022	12,948,500	22,919,675	8,500,000	6,347,390	14,847,390	37,767,065	50,715,565
2023	12,947,481	22,921,175	8,900,000	5,902,736	14,802,736	37,723,911	50,671,392
2024	12,949,644	22,920,175	9,200,000	5,440,218	14,640,218	37,560,393	50,510,037
2025	12,943,088	22,922,488	9,600,000	4,960,470	14,560,470	37,482,957	50,426,045
2026	12,942,128	22,920,513	10,000,000	4,458,930	14,458,930	37,379,443	50,321,571
2027	12,946,600	22,918,938	10,400,000	3,937,626	14,337,626	37,256,564	50,203,164
2028	12,950,122	22,920,850	10,800,000	3,395,882	14,195,882	37,116,732	50,066,854
2029	12,946,559	22,919,338	11,300,000	2,831,917	14,131,917	37,051,255	49,997,814
2030	9,386,219	-	11,700,000	2,243,388	13,943,388	13,943,388	23,329,607
2031	9,386,747	-	12,200,000	1,632,638	13,832,638	13,832,638	23,219,385
2032	9,384,469	-	12,700,000	996,338	13,696,338	13,696,338	23,080,807
2033	-	-	13,200,000	335,417	13,535,417	13,535,417	13,535,417

(1) Based on payments, not on accruals.

(2) Assumes interest at an average rate of 4% per annum.

THE CITY AND COUNTY AND THE DEPARTMENT

Purpose and Powers

The City and County. The City and County of Honolulu includes the entire island of Oahu and a number of outlying islands. Of the eight major islands that constitute the State of Hawaii, Oahu, with an area of 593 square miles, is smaller than the Islands of Hawaii and Maui but larger than the Islands of Kauai, Molokai, Lanai, Niihau and Kahoolawe. With slightly less than a tenth of the land area in the entire State, Oahu contains nearly three-fourths of the State's resident population. Based on the 2000 U.S. Census, the resident population of the State was 1,121,537, and that of Oahu was 845,157, approximately 72% of the total State population. Honolulu is the seat of the State Government and is the State's trade, finance, communication, and transportation center. Most Federal establishments and personnel (both civilian and military), manufacturing, major educational and scientific, and significant agricultural activities are located on Oahu.

City Council and Mayor. The City Council (the "City Council") is the governing body of the City and County and it consists of nine members. All members are elected from nine districts to serve four year terms with a limitation of two consecutive full terms. Pursuant to the City Charter of the City and County, the City Council has the power, among other things: (i) to exercise the legislative power of the City, (ii) to enact operating and capital budget ordinances, (iii) with certain exceptions, to fix fees and charges for services rendered by the City, and (iv) to authorize the issuance of revenue bonds for the purpose of initiating, constructing, acquiring, extending, replacing or otherwise improving any revenue-producing facility. The Mayor is the Chief Executive Officer of the City. The Mayor is elected to serve a four year term with a limitation of two consecutive full terms. The Mayor exercises direct supervision over all agencies specifically identified in the City Charter and, through the Managing Director, exercises supervision over all other executive agencies of the City.

Department of Environmental Services. The Department of Environmental Services was established on July 1, 1998, pursuant to a plan of reorganization which combined certain components of the Department of Wastewater Management, the department which previously administered the Wastewater System, with other administrative departments having compatible functions. The Department of Environmental Services, among other things, is charged with the responsibility to administer the planning, design and construction of wastewater facilities, oversee the operation and maintenance of sewer lines, treatment plants and pumping stations, monitor the collection, treatment and disposal of wastewater, provide chemical treatment and pumping of defective cesspools, provide solid waste processing, collection and disposal, promulgate rules and regulations as necessary to administer and enforce requirements established by law, and perform such other duties as may be required by law. The Department consists of four divisions: Environmental Quality, Treatment and Disposal, Collection System Maintenance and Refuse Collection and Disposal, plus an Office of Administrative Support.

Power to Fix and Collect Rates and Charges. By ordinance and resolution, the City Council requires that revenues of the Wastewater System be kept in the Sewer Fund and that the wastewater program shall be self-supporting. Consistent with such requirements, the Department is budgeted as a self-sustaining enterprise for the purpose of determining costs associated with providing wastewater services. Through the adoption of the annual operating and capital budgets, the revenue requirements and wastewater rates are reviewed to determine the adequacy of revenues to meet needs. Pursuant to the Act and the City Charter, the City Council has the power to impose, prescribe and collect rates, rentals, fees or charges for the use and services of, and the facilities furnished by, the Wastewater System so that the Wastewater System will be and remain self-sustaining. The rates, rentals, fees or charges imposed and prescribed are required to produce revenues which will be at least sufficient to pay debt service on all revenue bonds issued for the purposes of the Wastewater System, including the Bonds, and including reserves therefor, to pay the costs of operation, maintenance and repair of the Wastewater System, and to carry out the covenants of all resolutions authorizing the issuance of revenue bonds for the purposes of the Wastewater System, including the Bond Resolution and the First Bond Resolution. The rates and charges fixed and imposed by the City Council are not subject to approval by any federal or state regulatory bodies. Rates and charges are determined on the basis of a recommendation by the Director of Environmental Services and the Mayor, subject to approval by ordinance of the City Council. An ordinance requires three readings and a public hearing for enactment by the City Council.

Department Work Force

The Department employs approximately 705 persons in various managerial, clerical, engineering and operational positions in support of wastewater activities. This work force, with the exception of 9 excluded employees, is represented by one blue-collar, non-supervisory bargaining unit, one blue collar, supervisory bargaining unit, one white-collar, non-supervisory bargaining unit, one white-collar, supervisory bargaining unit, and one professional and scientific bargaining unit. All bargaining unit contracts are state-wide and apply to all State government and county government activities, and all are effective until June 30, 2003. All employees are covered by the Hawaii State Employees Retirement System.

Department Principal Officers

The principal officers of the Department of Environmental Services include the Director, Deputy Director and Executive Assistant.

The following are brief biographies of the Department's principal officers:

Frank J. Doyle, Deputy Director and Acting Director. Mr. Doyle was appointed to the position of Acting Director on February 14, 2003. He has served as Deputy Director of the Department of Environmental Services since 2001 and as Chief of the Division of Refuse Collection and Disposal from 1977 to 2001, during which time he held the position of Manager and Chief Engineer for the Office of Rapid Transit from 1990 to 1993. Prior to this, he was employed in the chemical industry for approximately 10 years, designing and constructing chemical complexes throughout the United States and Mexico. He is a graduate of Pennsylvania Military College and the University of Hawaii-Manoa with a Master of Science degree in Civil Engineering and was in private practice before coming to the City and County.

Timothy A. Houghton, Executive Assistant. Mr. Houghton served as Executive Assistant for the Department of Wastewater Management from its creation on July 1, 1993, and continues in that role with the Department of Environmental Services. As Executive Assistant, among other things, Mr. Houghton is responsible for Department financial and personnel activities. Prior to that he worked on the Honolulu Rapid Transit Project and with the Department of Auditoriums. Mr. Houghton has a Bachelor of Arts degree from San Francisco State University and a Master of Science in Systems Management degree from the University of Southern California.

THE WASTEWATER SYSTEM

Introduction

The Wastewater System services approximately 136,000 separate accounts and a population of approximately 600,000, which is approximately 68% of the total population of the City and County. The service area covers nearly 500 square miles. The customer base includes the residential population, business and industries, and other users located in the service area. Of the 136,000 accounts, 129,000 are residential and provide 70% of the total revenue from sewer service charges. See "CERTAIN OPERATING AND OTHER STATISTICS." The average total volume of wastewater processed by the City and County's Wastewater System is 111 million gallons per day. A number of small private wastewater systems also serve some areas in the City and County. The average total volume of wastewater processed by all such private systems is 4.1 million gallons per day, or 4% of the total wastewater processed in the City and County.

General Description of Existing Facilities

The Wastewater System serving the island of Oahu is divided into eight wastewater basins for planning purposes: Central Oahu, East Mamala Bay, Kailua/Kaneohe/Kahaluu, North Oahu East/West, Waianae, Waimanalo, and West Mamala Bay. Each basin is served by a wastewater treatment plant ("WWTP"). The function of each WWTP is to treat the wastewater by removing or reducing the levels of organic and inorganic materials contained in the wastewater to levels that satisfy federal and state permit requirements for the discharge of such wastewater into the ocean, streams, reservoirs or injection wells. In addition to treatment facilities, the Wastewater System includes collection, pumping and other related facilities.

A description of the wastewater basins and major facilities is as follows:

East Mamala Bay. The largest and the most densely populated basin is East Mamala Bay. Approximately 374,400 people reside in East Mamala Bay, representing approximately 44% of the resident population of the entire island. The basin is served by the Sand Island WWTP, a primary plant, and the largest treatment facility in terms of wastewater flow. The treatment plant has the capacity to process 82 million gallons per day (“MGD”) of wastewater flow, and currently treats 70.1 MGD.

West Mamala Bay. West Mamala Bay is the second largest basin and includes Ewa, Central Oahu as far north as Mililani, and the Halawa to Pearl City area of the Primary Urban Center. The population of the basin area is approximately 240,000, or more than 28 percent of the estimated population of Oahu. The basin is served by the Honouliuli WWTP, which is the second largest treatment plant in the Wastewater System, with a primary treatment design capacity of 38 MGD and a secondary treatment design capacity of 13 MGD. It currently processes 26.0 MGD of wastewater flow. The secondary treated effluent is provided to a recycled water facility.

Kailua/Kaneohe/Kahaluu. The third largest basin includes the communities of Kailua, Kaneohe, and Kahaluu and surrounding areas in the eastern part of the island. The eastern portion of Oahu is also referred to as the Windward basin area. The basin area population is nearly 106,000, or approximately 13 percent of the island’s population. The basin is served by the Kailua Regional WWTP, the third largest treatment plant in the Wastewater System. The Kailua WWTP has a design capacity of 15.25 MGD and currently treats about 13.24 MGD of wastewater flow.

North Oahu (East and West). The North Oahu area is largely unsewered. Small facilities existing are the Kahuku WWTP (0.4 MGD capacity, secondary) in the east basin, and the Pa’alaa Kai WWTP (0.14 MGD capacity, secondary) in the west basin.

Waianae. The Waianae basin serves the west coast of the island, which has a population of approximately 39,300. The Waianae WWTP has the capacity to process 5.2 MGD at a secondary level.

Central Oahu. Central Oahu, including military bases and the communities of Wahiawa and Whitmore Village, is served by the Wahiawa WWTP (2.5 MGD capacity, secondary).

Waimanalo. The Waimanalo basin is served by the Waimanalo WWTP with a capacity of 0.7 MGD. It is a secondary plant and serves the Waimanalo community, with a population of 9,200.

The Sand Island WWTP, the Honouliuli WWTP and the Kailua Regional WWTP are the three largest WWTPs. The remaining WWTPs provide treatment of wastewater to the rest of the island. Though the four basin areas including Central Oahu, North Oahu, Waianae, and Waimanalo comprise the majority of the geographical area of the island, the population density is much lower in comparison to the East and West Mamala Bay and the Kailua/Kaneohe/Kahaluu basin areas. The combined population of the four basin areas is less than 12 percent of the total population of Oahu. The total design capacity of the WWTPs in the 4 basin areas is nearly 9 MGD and the current wastewater flow is approximately 5.9 MGD. Two private wastewater systems provide collection and treatment for the communities of Hawaii Kai and Laie. The Hawaii Kai system has an average flow of 3.8 MGD, including flows from the City and County’s Kuliouou WWPS, and the Laie system has an average flow of 0.3 MGD. The two systems combined process less than 4% of the average flow of the City and County’s Wastewater System. The City and County has entered into an agreement to acquire the Laie wastewater system by the end of 2003.

Environmental Compliance

The WWTPs and other facilities operated by the Department are governed by either National Pollutant Discharge Elimination System (NPDES) permits or State of Hawaii Department of Health Underground Injection Control permits. Since 1991, the United States Environmental Protection Agency (“EPA”), the State of Hawaii and several environmental groups have filed various legal and regulatory actions against the City and County alleging violations of the federal Clean Water Act and the several NPDES and State of Hawaii permits held by the Department. The City and County has entered into settlements with respect to several of such actions. The consent decrees entered into by the City and County in connection with such settlements require the City and County, among

other things, to rehabilitate and expand certain existing facilities, to implement pretreatment programs; efficient reuse and biosolids reuse, and to construct new facilities. The Department has undertaken the rehabilitation and expansion of existing facilities, the implementation of pretreatment programs, efficient reuse and biosolids reuse, and the construction of new facilities in the last several years for the purpose of complying with the existing consent decrees. The Department has developed the 2003-2007 Capital Improvement Program, the 2003-2012 Capital Improvement Program and the 1998-2017 Capital Improvement Program, in part, to comply with existing consent decrees and administrative orders.

Facilities of the Wastewater System, except for the Waimanalo WWTP, which is operated by the Department but is owned by the State of Hawaii, are meeting current regulatory requirements and are operated and maintained in accordance with standard utility practices. However, the collection and pumping facilities of the Wastewater System do not meet all of the current and anticipated federal and state regulatory requirements and will require additional capacity to serve projected growth in the service area. The Department has developed plans which will provide for anticipated requirements.

Projected Customer Growth

The resident population in Oahu, the area served by the Wastewater System, is projected to grow modestly through 2020. The actual and projected resident population, by basin area, for the years 1990 through 2020 is shown in the following tables. The majority of growth between the years 1990 and 2020 is expected to occur in East and West Mamala Bay. Of the total population growth projected to occur between 1990 and 2020, 94,000 or 59% is expected to take place in West Mamala Bay and over 54,000, or 34% , is expected to occur in East Mamala Bay. The tables show an estimated average annual population increase of 5,308 between 1990 and 2020, or roughly 0.5% annually.

Table 1

**Actual and Projected Resident Population
By Basin⁽¹⁾, Oahu, 1990-2020**

Basin	1990	2000	2005	2010	2015	2020
East Mamala Bay	380,157	374,366	385,303	402,731	421,828	434,250
West Mamala Bay	199,005	239,713	251,239	267,301	273,752	293,036
North Oahu (East/West) ⁽²⁾	29,992	31,094	31,331	31,372	34,325	34,924
Waianae	37,411	39,271	40,635	41,094	41,336	42,183
Central Oahu	44,540	45,252	44,996	44,716	44,546	44,231
Kailua/Kaneohe/Kahaluu	108,639	106,300	105,502	104,738	108,812	109,214
Waimanalo	9,055	9,161	9,099	9,043	9,631	9,749
Total	808,799	845,157	868,105	900,955	934,230	967,587

Notes:

- 1 Population from Planning Department. Military bases are included (City and County of Honolulu Planning Department, 2000; City and County of Honolulu)
- 2 Includes population of Laie, which is currently served by a private sewer system operator, but which will be served by the City and County of Honolulu beginning in 2003.

Source: *City and County of Honolulu, Department of Environmental Services, City & County of Honolulu, Department of Planning and Permitting, 2001.*

Table 2

**Actual and Projected Percentage Growth in Resident Population
By Basin, Oahu, 1990-2020**

Basin	1990-2000	Percent of Total Growth	1990-2020	Percent of Total Growth
	Average Annual Change		Average Annual Change	
North Oahu (East)	(45)	-1.2%	49	0.9%
Kailua- Kaneohe/Kahaluu	(234)	-6.4%	19	0.4%
Waimanalo	11	0.3%	23	0.4%
East Mamala Bay	(579)	-15.9%	1,803	34.0%
West Mamala Bay	4,071	112.0%	3,134	59.1%
Waianae	186	5.1%	159	3.0%
Wahiawa	71	2.0%	(10)	-0.2%
North Oahu (West)	155	4.3%	131	2.5%
Total	3,636	100.0%	5,308	100.0%

Source: City & County of Honolulu, Department of Environmental Services, City & County of Honolulu, Department of Planning and Permitting, 2001.

The Department has developed the 2003-2007 Capital Improvement Program, the 2003-2012 Capital Improvement Program and the 1998-2017 Capital Improvement Program, in part to provide new facilities which will be required to reliably serve projected growth in the number of customers served by the Wastewater System.

CAPITAL IMPROVEMENT PROGRAM

The Department staff manages and updates at least annually a long-range Capital Improvement Program (the “CIP”) to achieve several goals. The CIP is a long-range planning tool used to estimate project costs and timing of expenditures over a 20-year period, currently through 2017. The 2003-2007 Capital Improvement Program and the 2003-2012 Capital Improvement Program are part of this 20-year plan. The Department develops the CIP with the objective of providing safe and reliable facilities to process the wastewater discharge of all sewer customers throughout Oahu. CIP projects provide for the rehabilitation of existing facilities, the expansion of capacity to accommodate growth, and the improvement of facilities and processes.

EPA Consent Decree

The City and County and the EPA have entered into a consent decree, approved October 17, 1995, that has established significant portions of the City’s direction on future wastewater issues. The overall goal established by the consent decree is to develop a proactive plan to reduce and prevent wastewater spills and bypasses from the collection system, pump stations, and treatment plants.

Consent decree projects are developed to meet three major program objectives:

1. *Pretreatment*: Source control program to control introduction of inappropriate materials into the collection and treatment system. This program does not require funding of any CIP project.
2. *Collection system compliance*: Spill reduction program for both dry weather spills, and wet weather spills. This is reflected in many of the CIP projects.
3. *Avoided cost*: Additional measures taken by the Department to avoid fines for violations or noncompliance.

Criteria for Ranking CIP Projects by Priority

The CIP is a flexible tool which allows the Department staff to determine the impact of adjusting the phasing and priority of projects. As of Spring 2003, the 1998-2017 long-range CIP included a list of projects with estimated appropriations totaling approximately \$2.3 billion (actual dollars through 2004, inflated dollars thereafter). Many of the projects shown in the CIP may not begin in the year specified or at all if needs change. CIP projects are ranked by priority to determine order and timing of projects. The policy is shown in the following table, with the highest priority criteria listed first:

Table 3
Priority for CIP Projects

Priority Class	Description
I	Safety and public health – immediate
II	Protection of the environment – immediate
III	Permit and regulatory compliance – immediate
IV	Completion of ongoing projects
V	Preventive
VI	Funding requirements
VII	System expansion
VIII	Other

The rankings are intended as guidelines for CIP project planning, not as hard and fast rules. A project considered in a low priority class may be upgraded to a high priority position in the CIP due to any number of factors. For example, if a service area is very close to reaching and surpassing the capacity of its wastewater facilities, the expansion of the system in that area rises in priority. System expansion can entail projects which affect permit and regulatory compliance, protection of the environment, or safety and public health. Through the use of these guidelines combined with analyses of funding and other resource constraints, staff can develop a CIP which best satisfies the needs of the Department customer base. The 1998-2017 Capital Improvement Program was developed using these CIP guidelines and constitutes the current 20-year CIP.

Classification of CIP Projects

The City and County expects to use various funding sources to finance CIP projects: (i) the proceeds of the Series 2003 Bonds and Bonds previously issued, (ii) proceeds of additional Bonds to be hereafter issued, (iii) proceeds of Outstanding Senior Bonds and additional First Resolution Obligations to be hereafter issued, (iv) proceeds of Reimbursable Obligations previously issued and currently available, (v) the Net Revenues of the Wastewater System, and (vi) Wastewater System Facility Charges. Revenues from Wastewater System Facility Charges are intended to cover a portion of the project expenditures relating to expansion of the Wastewater System to serve future growth in the number of customers. The classes of CIP projects include:

System expansion: Improvements which increase the design capacity of treatment, transmission, or support facilities and equipment to accommodate new or future growth. Future users would finance system expansion project costs partially through revenues from Wastewater System Facility Charges.

System upgrade: Improvements which upgrade the service level standard. For example, an upgrade to secondary treatment processes where only primary treatment processes were used.

Replacement/rehabilitation: Improvements which replace or rehabilitate facilities serving existing development.

2003-2007 Capital Improvement Program

To meet certain consent decrees entered into by the Department with Federal and State regulatory bodies and to reliably serve projected growth in the number of customers served by the Wastewater System, the Department has developed and adopted the 2003-2007 Capital Improvement Program. The additions and

improvements to the Wastewater System, the costs of which are to be financed in part from the proceeds of the Series 2003 Bonds, are part of the 2003-2007 Capital Improvement Program. The City and County expects to appropriate approximately \$744 million (actual dollars through 2004, inflated dollars thereafter) for the 2003-2007 Capital Improvement Program. A portion of these appropriations will actually be expended after the 2003-2007 period. The projected appropriations for the various CIP projects of and the expected sources of funding for the 2003-2007 Capital Improvement Program are set forth in the following tables.

Table 4

**Projected Appropriations for
2003-2007 Capital Improvement Program**

Project	Projected Cost
CIP Projects	\$694,490,000
Project Management	29,150,000
<u>Capital Equipment</u>	<u>20,360,000</u>
Total	\$744,000,000

Table 5

**Expected Sources of Funding for
2003-2007 Capital Improvement Program**

Funding Source	Projected Amount
Subordinate Obligations ⁽¹⁾	\$ 88,250,000
Facility Charges ⁽²⁾	26,910,000
Net Revenues ⁽³⁾	36,335,000
Series 2003 Bonds	180,000,000
<u>Future Obligations⁽⁴⁾</u>	<u>412,505,000</u>
Total	\$744,000,000

(1) State revolving fund loan proceeds.

(2) Fees collected for new Wastewater System connections.

(3) Cash funded CIP.

(4) Currently expected to be primarily First Resolution Obligations.

2003-2012 Capital Improvement Program

The 2003-2012 Capital Improvement Program is part of the 1998-2017 Capital Improvement Program. The City and County expects to appropriate approximately \$1.38 billion (actual dollars through 2004, inflated dollars thereafter) for the 2003-2012 Capital Improvement Program. A portion of these appropriations will actually be expended after the 2003-2012 period. The projected appropriations for the various CIP projects of and the expected sources of funding for the 2003-2012 Capital Improvement Program are set forth in the following tables.

Table 6

**Projected Appropriations for
2003-2012 Capital Improvement Program**

Project	Projected Cost
CIP Projects	\$1,273,580,000
Project Management	61,550,000
<u>Capital Equipment</u>	<u>43,570,000</u>
Total	\$1,378,700,000

Table 7

**Expected Sources of Funding for
2003-2012 Capital Improvement Program**

<u>Funding Source</u>	<u>Projected Amount</u>
Subordinate Obligations ⁽¹⁾	\$138,250,000
Facility Charges ⁽²⁾	63,200,000
Net Revenues ⁽³⁾	148,859,000
Series 2003 Bonds	180,000,000
<u>Future Obligations</u> ⁽⁴⁾	<u>848,391,000</u>
Total	\$1,378,700,000

(1) State revolving fund loan proceeds.

(2) Fees collected for new Wastewater System connections.

(3) Cash funded CIP.

(4) Currently expected to be primarily First Resolution Obligations.

1998-2017 Capital Improvement Program

The 1998-2017 Capital Improvement Program (“CIP”) is the current twenty-year CIP the Department has undertaken. The City and County expects to appropriate approximately \$2.3 billion (actual dollars through 2004, inflated dollars thereafter) for the 1998-2017 Capital Improvement Program. A portion of these appropriations will actually be expended after the 1998-2017 period. The projected appropriations for the various CIP projects of and the expected sources of funding for the 1998-2017 Capital Improvement Program are set forth in the following tables.

Table 8

**Projected Appropriations for
1998-2017 Capital Improvement Program**

<u>Project</u>	<u>Projected Cost</u>
CIP Projects	\$2,017,120,000
Project Management	107,460,000
Capital Equipment	81,280,000
<u>Ongoing Projects</u>	<u>84,420,000</u>
Total	\$2,290,280,000

Table 9

**Expected Sources of Funding for
1998-2017 Capital Improvement Program**

<u>Funding Source</u>	<u>Projected Amount</u>
Reimbursable Obligations ⁽¹⁾	\$ 83,985,000
Subordinate Obligations ⁽²⁾	257,024,000
Facility Charges ⁽³⁾	113,264,000
Net Revenues ⁽⁴⁾	411,667,000
Series 1998 Bonds	50,000,000
Series 2001 Bonds	125,000,000
Series 2003 Bonds	180,000,000
<u>Future Obligations⁽⁵⁾</u>	<u>1,069,340,000</u>
Total	\$2,290,280,000

(1) Previously issued general obligation bonds.

(2) State revolving fund loan proceeds.

(3) Fees collected for new Wastewater System connections.

(4) Cash funded CIP.

(5) Currently expected to be primarily First Resolution Obligations.

An estimated \$1.91 billion of non-discretionary CIP project expenditures for various treatment, collection and other facilities are required to be constructed during the 20-year CIP program. This is to eliminate the current and projected critical deficiencies, to meet consent decree milestones, and to provide a wastewater system in a satisfactory operating condition based on projected wastewater usage and environmental and other regulatory requirements. The remaining approximately \$0.38 billion of CIP projects are discretionary, and have been identified primarily to improve wastewater treatment and collection systems efficiency. These CIP project expenditures are to be funded from proceeds of bonds, including the Series 2003 Bonds, and from net revenues and other charges.

The projects to be financed by proceeds of the Series 2003 Bonds are the highest priority projects required to meet consent decree requirements and protect public health. They are included in recently completed facility plans, which identify the need for projects through the year 2017, and provide the most cost effective facilities evaluated in those plans.

In the opinion of the Department: (1) the estimated project costs and construction schedules that have been developed for the projects to be financed, including the projects to be financed from the proceeds of the Series 2003 Bonds, are reasonable and achievable; (2) the 1998-2017 Capital Improvement Program is technically sound and conforms with good engineering practice and the estimated total costs of the program are realistic; (3) the cost-effectiveness of the Wastewater System operations and maintenance activities is anticipated to improve as proposed projects in the 1998-2017 Capital Improvement Program are accomplished; and (4) completion of the proposed projects will permit the City and County to attain and to remain in compliance with all federal, state, and local regulations regarding the treatment and discharge as expressed in the current NPDES permit, consent decrees and administrative orders.

Projected revenues, expenses and coverages for the Wastewater System for the Fiscal Years 2003 to 2012, inclusive, are based on inflated dollars (*i.e.*, adjusted from 2003 dollars). The projections for Fiscal Years 2003 to 2012, inclusive, support (i) issuance the Series 2003 Bonds to finance \$180 million of necessary additions and improvements to the Wastewater System, to fund the Common Reserve Subaccount in an amount sufficient to satisfy its requirement, and to pay the costs of issuing the Series 2003 Bonds; (ii) financing an additional \$1.38 billion of improvements to the Wastewater System from proceeds of additional Bonds and First Resolution Obligations to be hereafter issued, proceeds of Reimbursable Obligations previously issued and currently available, the Net Revenues and Wastewater System Facility Charges over the nine year period; and (iii) all reserve funding and coverage requirements under the Bond Resolution and the First Bond Resolution by raising sewer rates and charges by 12% in Fiscal Year 2004-2005 and another 9% to 13% in each of the Fiscal Years thereafter, and by raising Wastewater System Facility Charges by 305.0% in Fiscal Year 2003-2004 and another 3.0% in each of the

Fiscal Years thereafter. Rate changes are subject to City Council approval. The Department has concluded these rates will provide revenue sufficient to:

- Meet all projected costs of operation, maintenance and routine replacement of sewer system facilities.
- Meet the existing debt service obligations and the projected requirements for the Series 2003 Bonds and future bond issues.
- Provide sufficient revenue to pay the costs of the City and County of Honolulu's CIP through the end of the forecast period.
- Meet reserve requirements of bond resolution.

The average monthly residential wastewater charge is expected to increase from \$33.05 to \$60.67 (in inflated dollars) by 2010. The Wastewater System Facility Charge is expected to increase from \$1,146 to \$5,541 (in inflated dollars) by 2010. The revenues from the Wastewater System Facility Charge were 1.4% of total revenues of the Wastewater System in fiscal year 2001-2002 and is projected to grow to approximately 2.9% through fiscal year 2011-2012. The rate at which growth occurs will not affect the ability of the City and County to meet its debt obligations because the growth is a small component of the overall costs and revenues associated with the Department's financial projections.

CERTAIN FINANCIAL, OPERATING AND OTHER INFORMATION AND STATISTICS

Financial Performance

In the period since the wastewater program became fully self-supporting in 1993, the program's financial position has been consistently strong. The change to enterprise fund status in 1998 further strengthened the position of the utility through clearer definition of enterprise assets, understanding of their current value, and clarity in responsibilities. The issue of the initial Wastewater Revenue bonds in 1998 accompanied by a strong debt and financial policy adopted by the City Council served to insure a continuing commitment to a strong financial posture for the wastewater enterprise.

HISTORICAL AND PROJECTED REVENUES, EXPENSES AND COVERAGES

General

Since its initial revenue bond issue in 1998, the Department has exceeded coverage requirements. Table 10 sets forth the Department's determination of historical and projected revenues, expenses and debt service coverage of the Wastewater System.

The prospective financial information included in this Official Statement has been prepared by, and is the responsibility of, the Department's management. PricewaterhouseCoopers LLP has neither examined nor compiled the prospective financial information, and accordingly, PricewaterhouseCoopers LLP does not express an opinion or any other form of assurance with respect thereto. The PricewaterhouseCoopers LLP report included in the offering document relates to the Department's historical financial information. It does not extend to the prospective financial information and should not be read to do so.

The prospective financial information was not prepared with a view toward compliance with published guidelines of the Securities and Exchange Commission or the guidelines established by the American Institute of Certified Public Accounts for preparation and presentation of prospective financial information.

Table 10**Summarized Historical and Projected Revenues, Expenses and Debt Service Coverages
Fiscal Year Ending June 30 (\$ in thousands)**

	Historical		Projected				
	2001 ⁽¹⁾	2002 ⁽¹⁾	2003	2004	2005	2006	2007
Revenues ⁽²⁾							
Sewer Service Charges ⁽³⁾	\$111,555	\$112,148	\$112,000	\$112,000	\$127,200	\$144,470	\$162,630
Interest Earnings	7,322	4,779	3,300	4,100	5,300	5,200	6,700
Other Revenues	90	55	233	233	233	233	233
Total Revenues	\$118,967	\$116,982	\$115,533	\$116,333	\$132,733	\$149,903	\$169,563
Operating Expenses ⁽⁴⁾	60,710	62,755	74,907	71,362	74,580	74,980	77,030
Net Revenues	\$58,257	\$54,227	\$40,626	\$44,971	\$58,153	\$74,923	\$92,533
Annual Debt Service							
Senior Lien Bonds ⁽⁵⁾	2,574	6,826	12,764	10,641	16,563	24,941	32,454
D/S Coverage ⁽⁶⁾	22.63x	7.94x	3.18x	4.23x	3.51x	3.00x	2.85x
Senior and Junior Lien Bonds ⁽⁷⁾	14,034	18,287	24,225	22,728	32,080	47,493	54,099
D/S Coverage ⁽⁶⁾	4.15x	2.97x	1.68x	1.98x	1.81x	1.58x	1.71x
Total Obligations ⁽⁸⁾	34,767	29,805	35,566	35,887	47,017	64,278	72,886
D/S Coverage ⁽⁶⁾	1.72x	1.87x	1.18x	1.42x	1.37x	1.27x	1.36x

(1) Audited.

(2) Does not include System Facility Charges, which are pledged under the Resolution but are not defined in Revenues.

(3) Sewer service charges are anticipated to be increased by 12% in 2005, 13% in 2006, and 12% in 2007.

(4) Operating expense projections reflect both anticipated operational changes and beyond 2005 are inflated at 3% per year for expenses and 3% per year for personnel costs. In year 2005, additional electrical costs are included for required one year test of full operation of newly installed ultraviolet disinfection facility at the Sand Island WWTP. It is anticipated that this facility will only be operated on a limited, as needed, basis beyond that one year period. Operating expenses do not include debt service, depreciation, or cash expenditures on capital improvements.

(5) Includes actual debt service for Senior Series 1998 and 2001 Bonds and assumes 6% interest rate for all future Senior Bond issues.

(6) Minimum debt service coverage requirements are: Senior Lien Bonds – 1.2x; Senior and Junior Lien Bonds – 1.1x; Total Obligations – 1.0x. Debt service coverage for Total Obligations includes revenue from System Facility Charges.

(7) Includes actual debt service for Senior and Junior Series 1998 and Senior Series 2001 Bonds and assumes a 4% interest rate for Junior Series 2003 Bonds and a 6% interest rate for all future Senior Bond issues.

(8) Includes actual debt service for existing obligations including Senior and Junior Series Revenue Bonds; reimburseable General Obligation Bonds; State Revolving Funds Loans; and any other debt obligations and assumes future interest rates for Revenue Bonds as indicated above.

Sewer service charge revenue grew with the rate increase effective July 1, 1993, and has continued to hold steady since that time. Revenues have been sufficient throughout the period to meet all operation and maintenance and debt service requirements, including coverage since 1998, without a need for rate increases. During the past ten years, existing rates generated revenue beyond immediate needs and policy requires minimizing rate impacts on customers. Water conservation efforts have held water use at the same level for several years; however, the significant base component of the rate structure and growth in customers has precluded these efforts from having a major impact on revenues. The sewer service charge program will remain strong reflecting the high residential component of wastewater customers and the lack of any single large commercial customer.

Receipts from the Wastewater System Facility Charge have averaged approximately 1.77 million for the past three years reflecting development; however, the Wastewater System Facility Charge accounts for less than 2% of revenues, is solely dedicated to expansion, and is not considered when calculating debt service coverage.

Equally important are continuing efforts to control increases in expenses. While operational expenditures and budgets have increased slightly due to negotiated salary increases, continuing analysis of staffing levels, operational procedures, and new facilities, and automation opportunities continue to mitigate the rate of increase. The Department has initiated bottom-up re-engineering program aimed at identifying changes that need to occur to insure an even more efficient enterprise.

Net revenues have decreased over the period, including fiscal years 2000, 2001, and 2002, reflecting additional borrowing and maintenance of a stable rate structure. Continuing cost controls and improved structuring of capital debt help maintain relatively high net revenues. Net revenues were artificially high in 2000 reflecting the change to full enterprise accounting and full versus modified accrual of sewer service charge revenues. Over the past three-year period, net income (net revenues minus total obligations) was \$66 million (18% of total revenues) without any increase in fees and charges. The enterprise has continued to maintain a surplus throughout the period. A portion of this surplus has been used in FY 2002 and FY 2003 to repay the City General Fund for assets contributed to the Wastewater Enterprise.

The financial position of the Wastewater Enterprise is strong, with reserves which provide reasonable protection against unforeseen events and financial flexibility for the future. Financial planning continues to identify the best way to maintain a strong financial position while providing quality service to the customer and the community at a reasonable price. City Council and Administration policies support the continuing revenue levels necessary to provide for current and future requirements.

For a further description of the analysis by the Department of the Wastewater Enterprise, see "Management's Discussion and Analysis" in Appendix A hereto.

Billing and Collection

Over 90% of Wastewater System sewer service charge billing is handled by the Board of Water Supply through inclusion on water bills. This billing program consistently has a delinquency (bills over 90 days old) of 1.53% and an uncollectable rate of 1.22%.

Should bills not be paid, the authority exists, and has been exercised, to terminate water service for non-payment of water and sewer service charges.

Ten Largest Customers

The ten largest customers, listed below, of the Wastewater System account for less than 5% of the annual revenues of the system.

Table 11

Ten Largest Customers

<u>Customer</u>	<u>Sewer Service Charges (FY02)</u>	<u>Percentage of Revenues</u>
State of Hawaii, Dept. of Education	\$1,178,731	1.01%
Honolulu International Airport	1,163,168	0.99
University of Hawaii	519,135	0.44
Hilton Hawaiian Village	409,982	0.35
Sheraton Waikiki Hotel	324,029	0.28
Halawa Correctional Facility	296,118	0.25
Hyatt Regency Waikiki	228,473	0.20
United Laundry Services	212,236	0.18
Azabu USA	196,926	0.17
Marriott Ihilani Hotel	192,181	0.16

Debt and Financial Policies

The City Council, by resolution adopted on November 10, 1998, established the Debt and Financial Policies for the Wastewater System to provide a general framework for the conduct of financial activities and has been in compliance with such policies since their adoption. Such Debt and Financial Policies specify, among other things, that the City and County will target to maintain revenues (excluding Wastewater System Facility Charges) of 1.60 times senior revenue bond debt service and 1.25 times debt service for all revenue bonds, regardless of the priority of lien. It is expected that the City and County will adopt increases in the sewer service charges necessary to meet the debt service coverage requirements prescribed in its debt and financial policies. The debt and financial policies do not constitute an agreement with holders of Bonds, and the City and County has not undertaken any obligation to such holders or any other person to comply with such policies or to meet such targets.

Since establishment of these policies in November 1998, the Wastewater Enterprise has consistently met or exceeded all policy requirements.

Certain operating and financial statistics of the Department are summarized in the following tables. Unless otherwise noted, tables provided herein contain data furnished by the City and County.

Table 12**Water and Sewer Customer Accounts as of September 2002**

Customer Class	Sewer Regular Monthly Charges	Cesspool Monthly Charge (Contract)	Cesspool Per Call	Separate BWS Water Meter (domestic use)	Cesspool Chemical Treat	Agreed to Monthly Charge	Sewer No Charge	Non-residential SS surcharge	Private Well	Water Private water Meter	Waste Private Water Meter	Minimum Monthly Charge Only	Septic System	Total	Percent Accounts
1 - Public Sewer															
10 - Single family/duplex	121,738	625	10,472	0	137	45	8,479	0	0	0	20	0	536	142,052	88.61%
15 - Mixed residential	0	0	3	0	0	0	189	0	0	0	7	0	1	200	0.12%
20 - Multi-family	5,900	4	115	0	0	0	404	0	0	0	28	0	3	6,454	4.03%
25 - Mixed users	284	0	3	0	0	2	0	0	0	0	24	0	0	313	0.20%
Total residential	127,922	629	10,593	0	137	47	9,072	0	0	0	79	0	540	149,019	92.95%
Residential Sewer Accounts	127,922	629	0	0	137	47	0	0	0	0	79	0	0	128,814	94.92%
30 - Commercial	4,642	0	609	1	0	14	2,067	0	1	0	107	54	25	7,520	4.69%
40 - Hotels	259	0	6	0	0	0	5	0	1	0	0	0	0	271	0.17%
50 - Industrial	501	0	94	0	0	1	19	0	0	1	0	0	2	618	0.39%
61 - US Military Installation	9	0	13	0	0	0	12	0	0	0	2	0	1	37	0.02%
62 - US Non-military	25	0	7	0	0	0	5	0	0	0	1	0	0	38	0.02%
63 - State	203	0	111	0	0	162	325	0	1	0	12	0	2	816	0.51%
65 - City	123	0	152	0	0	206	460	0	0	0	4	43	4	992	0.62%
70 - Agriculture	2	0	427	0	0	0	33	0	0	0	0	0	0	462	0.29%
80 - Religious	455	0	54	0	0	1	12	0	0	0	22	0	3	547	0.34%
Total Non-residential	6,129	0	1,473	1	0	384	2,938	0	43	1	148	97	37	11,301	7.05%
Non-residential Sewer Accounts	6,129	0	0	1	0	384	0	0	43	1	148	97	37	6,890	4.30%
Total Accounts	134,141	629	12,066	1	137	431	12,010	0	43	1	227	97	577	160,320	100%
Total Sewer Accounts	134,141	0	0	1	137	431	0	0	43	1	227	97	37	135,704	100%
Percent Total Accounts	83.67%	0.39%	7.53%	0.00%	0.09%	0.27%	7.49%	0.00%	0.00%	0.00%	0.14%	0.06%	0.36%	100.00%	
Percent Sewer Accounts	98.95%	0.46%	0.00%	0.00%	0.10%	0.32%	0.00%	0.00%	0.00%	0.00%	0.17%	0.07%	0.03%	100.00%	

Table 13

History of New Sewer Connections by Type

Fiscal Year Ending	Single Family New Units	Multi Family		Nonresidential ESDUs	Total ESDUs
		New Units	ESDUs		
1998	998	226	158	118	1,274
1999	1,387	122	85	25	1,497
2000	1,527	69	48	36	1,611
2001	1,236	422	295	46	1,577
2002	974	541	379	36	1,389
5 year average	1,220	280	190	50	1,470
Projected annual growth	1,250	340	240	40	1,530

Table 14

**Existing Sewer Users
Fiscal Year Ended June 30, 2002**

Customer Classification	Number of Living Units	Number of Equivalent Single- Family Dwelling Units (ESDUs)	Estimated Wastewater Flow (MGD)
Residential			
Single family/duplex	128,109	128,109	38.889
Multi-family residences	110,521	76,788	23.310
Less: Hawaii Kai	994	994	0.302
Total residential	238,630	204,897	62.199
Nonresidential	N/A	77,832	23.627
Infiltration/Inflow	N/A	N/A	28.834
Total	477,260	281,735	114.660

Table 15

**Historic Population Growth
Oahu, 1970 - 2001**

Calendar Year	Resident Population	Defacto Population*
1970	630,528	650,700
1980	764,600	822,408
1990	838,534	913,268
1991	850,510	901,717
1992	863,959	912,514
1993	870,348	909,506
1994	878,591	919,818
1995	881,399	921,620
1996	883,443	921,609
1997	886,711	932,931
1998	886,909	931,439
1999	878,906	927,689
2000	875,670	925,233
2001	881,295	925,250

Source: *State of Hawaii Department of Business, Economic Development & Tourism, Data Book, 2001. U.S. Census 2000.*
*Includes visitor population.

Table 16

Number of Equivalent Single Family Dwelling Units (ESDUs)

Fiscal Year Beginning 7/1	Single-Family Units	Multifamily Units	ESDUs	Commercial ESDUs	Total ESDUs
1993	114,407	103,516	72,462	76,704	263,573
1994	116,446	105,058	73,541	76,941	266,928
1995	118,247	106,758	74,731	77,130	270,166
1996	119,451	107,039	74,928	77,280	271,659
1997	120,810	108,437	75,907	77,359	274,076
1998	121,725	109,514	76,405	77,561	275,691
1999	122,723	109,740	76,563	77,679	276,965
2000	124,110	109,862	76,648	77,704	278,462
2001	125,637	109,931	76,696	77,740	280,073
2002	126,873	110,226	76,742	77,786	281,401
2003	128,109	110,521	76,788	77,832	282,729

Table 17

Wastewater Flows by Treatment Facility (MGD)

<u>Treatment Facility</u>	<u>Design Capacity</u>	<u>2002 Flow</u>	<u>Projected Flow (2020)</u>
Sand Island	82.00	70.100	92.60
Kahuku WWTP	0.40	0.183	0.15
Honouliuli WWTP	38.00	25.400	32.80
Waimanalo WWTP	0.70	0.520	0.62
Kuliouou WWPS* (Hawaii Kai WWTP)	N/A	0.358	0.38
Wahiawa WWTP	2.50	1.840	1.89
Kailua WWTP	15.25	13.240	13.40
Waianae WWTP	5.20	3.260	3.50
Paalaa Kai WWTP	0.14	0.115	0.14

* The Kuliouou WWPS does not provide treatment, but pumps wastewater from a Department Collection System to a private treatment plant (Hawaii Kai WWTP). Inclusion here is to show total volume of wastewater handled by the Department.

Table 18

History of Major Wastewater Revenue Sources

<u>Fiscal Year Ending June 30</u>	<u>Sewer Service Charges*</u>	<u>Wastewater Facilities Charge</u>
1993	77,492,000	5,206,000
1994	105,303,000	3,895,000
1995	109,541,000	3,543,000
1996	111,259,000	1,769,950
1997	110,891,000	1,166,000
1998	111,841,000	1,027,000
1999	111,378,000	1,666,000
2000**	122,451,000	2,279,000
2001	111,555,000	1,413,000
2002	112,148,000	1,608,000

* Sewer Service Charge Only - Does Not Include Connection Or Lateral Installation Charges.

** Sewer Service Charge revenue converted to full accrual accounting in Fiscal Year 2000.

Table 19

Summary of Current Sewer Rate Ordinance*

	<u>Effective 7/1/93 Standard</u>
Residential sewer service charges	
Single family and duplex dwellings served by city water system per dwelling unit per month:	
Monthly base charge:	\$24.85
Month usage charge:	
First 2,000 gallons of metered water consumed:	no charge
Charge per 1,000 gallons of metered water consumed over 2,000 gallons, the water consumed reduced by the irrigation factor of 18%:	1.05
Single family and duplex dwellings not served by city water system per dwelling unit per month:	33.65
Multiple-unit dwellings served by city water system per dwelling unit per month:	
Monthly base charge:	17.40
Monthly usage charge:	
First 2,000 gallons of metered water consumed:	no charge
Charge per 1,000 gallons of metered water consumed over 2,000 gallons, the water consumed reduced by the irrigation factor of 18%:	1.05
Multiple-unit dwellings not served by city water system per dwelling unit per month:	23.55
Nonresidential sewer service charges	
Domestic strength wastewater:	
1. Metered water usage:	
a. If 9,000 gallons or less per month,	
(1) Monthly base charge:	22.35
(2) Charge per 1,000 gallons:	0.13
b. If more than 9,000 gallons per month,	
(1) Charge per 1,000 gallons:	2.49
2. Metered wastewater discharge:	
a. If 7,000 gallons or less per month,	
(1) Monthly base charge:	22.35
(2) Charge per 1,000 gallons:	0.16
b. If more than 7,000 gallons per month,	
(1) Charge per 1,000 gallons:	3.12
Extra strength wastewater:	
1. Charge per 1,000 gallons of water usage: 0.857 + 0.143, (S.M./200):	2.49
2. Charge per 1,000 gallons of wastewater discharge: 0.857 + 0.143 (S.M./200):	3.12
<hr/>	
* <i>A separate and modified rate schedule exists for those customers, such as the U.S. Government agencies, who prepay a capital contribution to account for additional capacity requirements.</i>	
Wastewater system facility charge	<u>Effective 1991/92</u>
Wastewater system facility charge per ESDU	1,146
Terms in strength surcharge formula (A+(SSI/200xB)):	
A. Flow component of wastewater system facility charge	985
B. Strength component of wastewater system facility charge	161

FINANCIAL STATEMENTS

The operations of the Department are accounted for in the Sewer Fund and the Wastewater System Facility Charge Account. The Sewer Fund is classified as an enterprise fund of the City and County and is currently audited as a part of the City and County's general purpose financial statements that are prepared annually.

The following tables have been extracted from both unaudited and audited financial statements of the City and County relating to the Department. It should be noted that "Revenues" as defined in the First Bond Resolution does not include Wastewater System Facility Charges.

The Sewer Fund was converted to enterprise accounting effective July 1, 1999. This change in accounting results in different presentations of financial data beginning with Fiscal Year 1999/2000, including accounting for infrastructure, property, plant and equipment costs and related depreciation expenses. Tables 20 and 21 summarize revenues and expenses and Tables 22 and 23 provide fund balances. Future presentations will be in accordance with those shown in Tables 21 and 23 reflecting enterprise accounting and consistency with GASB 34 reporting requirements.

The financial statements of the Department as of June 30, 2002, and for the year then ended, included in this Official Statement, have been audited by PricewaterhouseCoopers LLP, independent accountants, as stated in their report included herein as Appendix A.

The financial statements of the Department as of June 30, 2001 and for the year then ended, as restated, included in this Official Statement, have been audited by PricewaterhouseCoopers LLP, independent accountants. The Department restated its 2001 financial statements to properly include certain previously excluded capital assets owned by the Department, together with related depreciation expense. The Department also restated its 2001 financial statements to correct the carrying value of the inventories of materials and supplies and related expense.

Table 20

**Department of Environmental Services
Summary of Wastewater Revenues and Expenses – FY 98-99**

Amounts in Thousands

	1997/98	1998/99
<u>Revenues</u>		
Sewer service charges	\$111,841	\$111,378
System facility charge	1,027	1,666
Other	280	188
Investments	0	2,864
Total revenues	113,148	116,096
<u>Expenses</u>		
Direct operating expenses		
Administration	2,750	3,362
Service control	1,850	0*
Planning	1,076	0*
Engineering	1,904	0*
Construction	1,622	0*
Environmental (Water) quality	4,188	3,997
Sewer maintenance	7,384	5,982
Cesspool pumping	931	905
Chemical treatment	98	91
Treatment and disposal		
Administration / maintenance	10,397	9,417
East Oahu	5,532	5,150
Windward	4,274	3,897
West Oahu	6,112	5,879
Total treatment and disposal	26,315	24,343
Subtotal direct operating expenses	48,118	38,680
Central administrative support	5,795	4,894
Non-salary personnel costs	9,862	8,054
Other City agencies	3,491	7,694
Building Rental	675	675
Radio support	175	35
Judgment and losses	0	0
General fund reimbursement	3,772	0
Subtotal indirect operating expenses	23,770	21,352
Existing general obligation bond debt service & state revolving fund loans	39,104	24,506
Facilities replacement reserve	0	0
Total expenses	110,992	84,538
Net income	\$2,156	\$31,558

* A city-wide reorganization effective July 1, 1998, resulted in direct operating expenses for the categories Service Control, Planning, Engineering, and Construction to be distributed into other direct operating expense categories (Administration) and into indirect operating categories (Other City Agencies).

Table 21

**Department of Environmental Services
Sewer Fund
Enterprise Fund Statement of Revenues, Expenses and Changes in Retained Earnings
(AMOUNTS IN THOUSANDS)**

	1999/2000	2000/2001	2001/2002
Operating Revenues:			
Sewer Service Charges	\$122,451	\$111,555	112,148
Other Revenue	2,410	1,486	1,662
Total Operating Revenues	<u>124,861</u>	<u>113,041</u>	<u>113,810</u>
Operating Expenses:			
Administrative and general	31,323	30,514	32,943
Maintenance	532	389	204
Depreciation	23,295	25,418	29,983
Contractual services	7,105	6,806	6,665
Fringe benefits	10,157	7,614	10,677
Materials and supplies	58	6,393	3,850
Fuel and lubricants	535	1,893	1,641
Utilities	7,125	7,087	6,754
Other	--	14	22
Total Operating Expenses	<u>80,130</u>	<u>86,128</u>	<u>92,738</u>
Operating Income	<u>44,731</u>	<u>26,913</u>	<u>21,072</u>
Nonoperating Revenues (Expenses):			
Interest revenue	7,873	7,322	4,779
Interest expense	(27,910)	(17,677)	(18,208)
Loss from disposal of property	(6)	17	1
Other	(262)	(223)	(1,754)
Total Nonoperating Revenues (Expenses)	<u>(20,305)</u>	<u>(10,562)</u>	<u>(15,182)</u>
Income before operating transfers and capital contributions	24,426	16,350	5,890
Contributed Capital	555,688	9,328	2,066
Operating Transfers In	25,976	--	--
Operating Transfers Out	(5,733)	(6,120)	(46,995)
Net Income (Loss)	<u>600,357</u>	<u>19,559</u>	<u>(39,039)</u>
Retained Earnings – July 1 as previously reported	--	600,357	818,419
Prior period adjustment	--	198,503	--
Retained Earnings – July 1 as restated	--	798,860	818,419
Retained Earnings – June 30	\$600,357	\$818,419	\$779,381

Table 22

**Department of Environmental Services
Summary of Wastewater Fund Balances FY 97-99**

Amounts in Thousands

	1997/98	1998/99
	(\$ in thousands)	
Sewer Fund (#170)		
Excess of revenues over (under) expenditures and other uses	\$ 1,256	\$56,511
Unreserved – undesignated fund balance, July 1	42,983	42,885
Unreserved – undesignated fund balance, June 30 (budgetary basis)	44,239	99,396
Adjustments to conform with GAAP:		
Encumbrances included above	5,522	3,573
Expenditures – prior year encumbrances	(10,366)	(4,990)
Accrued Retroactive payroll	45	(4,024)
Decrease (increase) in reserved for encumbrances	5,208	1,874
Residual equity transfer to WW System Facility Charge Fund	(1,763)	
Increase in reserved fund balance, June 30	--	(36,477)
Unreserved – undesignated fund balance, June 30 (GAAP basis)	42,885	59,352
Reserved for encumbrances, June 30	10,889	9,015
Increase in reserved for debt service	0	36,477
Fund balance (GAAP basis), June 30	<u>\$53,774</u>	<u>\$104,844</u>
Wastewater System Facility Charge Fund (#175)*		
Excess of revenues over (under) expenditures and other uses	\$900	
Unreserved-undesignated fund balance, July 1	<u>(2,663)</u>	
Unreserved-undesignated fund balance, June 30 (budgetary basis)	(1,763)	
Adjustments to conform with GAAP: Residual equity transfer from Sewer Fund	1,763	
Unreserved-undesignated fund balance, June 30 (GAAP basis)	0	
Reserved for encumbrances, June 30	0	
Fund balance (GAAP basis), June 30	0	

* *The Wastewater System Facility Charge Fund was abolished in May 1998. Wastewater System Facility Charges are accounted for in the Wastewater System Facility Charge Account.*
Source: Comprehensive Annual Financial Reports, June 30, 1997, 1998, and 1999.

Table 23

**Department of Environmental Services
Sewer Fund
Enterprise Fund Balance Sheet
(AMOUNTS IN THOUSANDS)**

	1999/2000	2000/2001	2001/2002
ASSETS			
Current Assets:			
Cash and cash equivalents	\$57,462	\$33,973	\$25,643
Investments	84,016	65,276	142,946
Receivables			
Accounts	16,227	16,406	16,772
Interest	393	682	985
Due from other funds	7,583	5,198	6,859
Inventories of parts, materials and supplies at cost	17,872	4,281	4,710
Total Current Assets	<u>183,553</u>	<u>125,816</u>	<u>197,916</u>
Fixed Assets:			
Land	63,713	5,368	5,630
Buildings and Improvements	331,031	394,973	394,423
Land Improvements	0	2,387	2,552
Transmission and distribution system	469,538	754,021	787,519
Equipment and machinery	19,674	22,418	19,963
Construction work in progress	62,238	70,490	109,690
Accumulated depreciation	(23,295)	(56,727)	(84,656)
Total Fixed Assets	<u>922,899</u>	<u>1,192,931</u>	<u>1,235,120</u>
Total Assets	<u>\$1,106,452</u>	<u>\$1,318,747</u>	<u>\$1,433,036</u>
LIABILITIES AND NET ASSETS			
Current Liabilities:			
Accounts payable	7,853	10,945	6,554
Interest payable-current	8,333	8,227	8,127
Notes payable-current	3,868	4,171	5,408
Tax-exempt commercial paper	0	3,199	10,183
Bonds payable-current	9,417	10,945	10,906
Other current liabilities	0	357	488
Total Current Liabilities	<u>29,471</u>	<u>34,208</u>	<u>41,666</u>
Notes payable	64,131	64,659	85,003
General obligation bonds payable	87,270	77,418	67,645
Revenue bonds payable	319,453	318,443	453,413
Deferred credits and other liabilities	5,770	5,600	5,929
Total Liabilities	<u>506,095</u>	<u>500,328</u>	<u>653,655</u>
Net Assets			
Invested in capital assets, net of related debt	463,480	726,116	650,381
Restricted for Debt Service	38,039	39,562	54,489
Unrestricted	98,838	52,741	74,510
Total Retained Earnings	<u>600,357</u>	<u>818,419</u>	<u>779,381</u>
Total Liabilities and Retained Earnings	<u>\$1,106,452</u>	<u>\$1,318,747</u>	<u>\$1,433,036</u>

The Bond Resolution requires the Department to maintain and keep proper books of account relating to the Wastewater System and in accordance with generally accepted accounting principles. The Bond Resolution also requires that within one hundred eighty (180) days after the end of each Fiscal Year the Department will cause such

books of account to be audited by an independent certified public accountant. Such audit may be part of a comprehensive audit of the City and County if the Wastewater System in such audit is treated as an “enterprise fund” and the revenues and expenses of the Wastewater System are stated in a manner which permits identification by category of the sources and uses of the Revenues.

PENDING LITIGATION

In the normal course of business, claims and lawsuits are filed against the City and County and the Department and their respective officers and employees. The City and County and the Department generally are self-insured with respect to general liability claims. In the Fiscal Years ended June 30, 2001 and June 30, 2002, the Department has reached lawsuit settlements with claimants totaling \$113,562.58. There were no judgments chargeable against the Department during such period. The City and County’s Corporation Counsel is of the opinion that no pending litigation will be determined so as to result individually or in the aggregate in a final judgment against the Department which would constitute a material impairment of the Department’s financial position.

The Corporation Counsel reports that there is no controversy or litigation now pending or, to the best of the City and County’s and the Department’s knowledge, threatened, which seeks to restrain or enjoin the execution, issuance, sale or delivery of the Series 2003 Bonds or that in any way contests the validity of the Series 2003 Bonds; or any proceedings of the City and County taken with respect to the authorization, sale, or issuance of the Series 2003 Bonds, the pledge or application of any moneys provided for the payment of or security for the Series 2003 Bonds.

RATINGS

Moody’s Investors Service and Fitch Ratings have assigned ratings of “Aaa” and “AAA”, respectively, to the Series 2003 Bonds with the understanding that upon delivery of the Series 2003 Bonds, the Policy insuring the payment of the principal of and interest on the Series 2003 Bonds will be issued by the Bond Insurer. Such ratings reflect only the respective views of such organizations, and an explanation of the significance of such ratings may be obtained from the rating agency furnishing the same, at the following addresses: Moody’s Investors Service, 99 Church Street, New York, New York 10007, and Fitch Ratings, One State Street Plaza, New York, New York 10004. There is no assurance that such ratings will continue for any given period of time or that they will not be revised or withdrawn entirely by such rating agencies, if in the judgment of such rating agencies, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an effect on the market price of the Series 2003 Bonds.

UNDERWRITING

The Series 2003 Bonds are being purchased for reoffering by the Underwriters. The Underwriters have agreed to purchase the Series 2003 Bonds at an aggregate purchase price of \$217,021,042.74, being the principal amount of the Bonds less an underwriting discount of \$1,378,957.26. Each contract of purchase with respect to a series of the Series 2003 Bonds provides that the applicable Underwriter will purchase all the Series 2003 Bonds of such series if any are purchased. The initial public offering price of the Series 2003 Bonds is 100% of the principal amount thereof. The Underwriters may offer and sell the Series 2003 Bonds to certain dealers (including depositing the Series 2003 Bonds into investment trusts) and others at prices lower than the initial public offering prices stated on the cover page hereof. The public offering prices may be changed from time to time by the Underwriters.

TAX MATTERS

In the opinion of Orrick, Herrington & Sutcliffe LLP, Bond Counsel, based upon an analysis of existing laws, regulations, rulings, and court decisions, and assuming, among other matters, compliance with certain covenants, interest on the Series 2003 Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986 (the “Code”), and the Series 2003 Bonds and the income therefrom are exempt from all taxation by the State or any county or other political subdivision thereof, except inheritance, transfer, estate and certain franchise taxes. Bond Counsel is of the further opinion that interest on the Series 2003 Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although Bond Counsel observes that such interest is included in adjusted current earnings when

calculating corporate alternative minimum taxable income. A complete copy of the proposed form of the opinion of Bond Counsel for the Series 2003 Bonds is set forth in Appendix D hereto.

The amount (if any) by which the amount (excluding amounts stated to be interest and payable at least annually over the term of such Series 2003 Bonds) to be paid at maturity of any maturity of the Series 2003 Bonds exceeds the issue price of such Series 2003 Bonds constitutes “original issue discount,” the accrual of which, to the extent properly allocable to each owner thereof, is treated as interest on the Series 2003 Bonds which is excluded from gross income for federal income and State of Hawaii tax purposes. For this purpose, the issue price of a particular maturity of the Series 2003 Bonds is the first price at which a substantial amount of such maturity of the Series 2003 Bonds is sold to the public (excluding bond houses, brokers, or similar persons or organizations acting in the capacity of underwriters, placement agents or wholesalers). The original issue discount with respect to any maturity of the Series 2003 Bonds accrues daily over the term to maturity of such Series 2003 Bonds on the basis of a constant interest rate compounded semiannually (with straight-line interpolations between compounding dates). The accruing original issue discount is added to the adjusted basis of such Series 2003 Bonds to determine taxable gain or loss upon disposition (including sale, redemption, or payment on maturity) of such Series 2003 Bonds. Owners of the Series 2003 Bonds should consult their own tax advisors with respect to the tax consequences of ownership of Series 2003 Bonds with original issue discount, including the treatment of purchasers who do not purchase such Series 2003 Bonds in the original offering to the public at the first price at which a substantial amount of such Series 2003 Bonds is sold to the public.

Series 2003 Bonds purchased, whether at original issuance or otherwise, for an amount greater than their principal amount payable at maturity (or, in some cases, at their earlier call date) (“Premium Bonds”) will be treated as having amortizable bond premium. No deduction is allowable for the amortizable bond premium in the case of bonds, like the Premium Bonds, the interest on which is excluded from gross income for federal income tax purposes. However, the amount of tax exempt interest received, and a purchaser’s basis in a Premium Bond, will be reduced by the amount of amortizable bond premium allocable to such purchaser. Owners of Premium Bonds should consult their own tax advisors with respect to the proper treatment of amortizable bond premium in their particular circumstances.

The Code imposes various restrictions, conditions and requirements relating to the exclusion from gross income for federal income tax purposes of interest on obligations such as the Series 2003 Bonds. The County has covenanted to comply with certain restrictions designed to insure that interest on the Series 2003 Bonds will not be included in federal gross income. Failure to comply with these covenants may result in interest on the Series 2003 Bonds being included in gross income for federal income tax purposes, possibly from the date of original issuance of the Series 2003 Bonds. The opinion of Bond Counsel assumes compliance with these covenants. Bond Counsel has not undertaken to determine (or to inform any person) whether any actions taken (or not taken) or events occurring (or not occurring) after the date of issuance of the Series 2003 Bonds may adversely affect the value of, or the tax status of interest on, the Series 2003 Bonds. Further, no assurance can be given that pending or future legislation or amendments to the Code, if enacted into law, or any proposed legislation or amendments to the Code, will not adversely affect the value of, or the tax status of interest on, the Series 2003 Bonds. Prospective Bondholders are urged to consult their own tax advisors with respect to proposals to restructure the federal income tax.

Certain requirements and procedures contained or referred to in the Resolution, the Series 2003 Certificate providing for issuance of the Series 2003 Bonds, the Tax Certificate relating to the Series 2003 Bonds, and other relevant documents may be changed and certain actions may be taken or omitted under the circumstances and subject to the terms and conditions set forth in such documents. Bond Counsel expresses no opinion as to any Series 2003 Bonds or the interest thereon if any such change occurs or action is taken or omitted upon the advice or approval of counsel other than Orrick, Herrington & Sutcliffe LLP.

Although Bond Counsel is of the opinion that interest on the Series 2003 Bonds is excluded from gross income for federal income tax purposes and that the Series 2003 Bonds and the income therefrom are exempt from taxation by the State or any political subdivision thereof, except inheritance, transfer, estate and certain franchise taxes, the ownership or disposition of, or the accrual or receipt of interest on, the Series 2003 Bonds may otherwise affect a Bondholder’s federal or state tax liability. The nature and extent of these other tax consequences will depend upon the particular tax status of the Bondholder or the Bondholder’s other items of income or deduction. Bond Counsel expresses no opinion regarding any such other tax consequences.

APPROVAL OF LEGAL PROCEEDINGS

All legal matters incident to the authorization, issuance and sale of the Series 2003 Bonds are subject to the approval of Orrick, Herrington & Sutcliffe LLP, San Francisco, California, Bond Counsel to the City and County. The form of the opinion Bond Counsel proposes to render is set forth in Appendix E hereto. Copies of the approving opinion of Bond Counsel will be available at the time of delivery of the Series 2003 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 Underwriters by their counsel, McCorriston Miller Mukai MacKinnon LLP, Honolulu, Hawaii.

CONTINUING DISCLOSURE

In order to assist the Underwriters in complying with Rule 15c2-12 promulgated by the Securities and Exchange Commission ("Rule 15c2-12"), the City and County will undertake in a Master Continuing Disclosure Certificate of the City and County, as supplemented, constituting a written agreement for the benefit of the holders of the Series 2003 Bonds (the "Continuing Disclosure Certificate"), to provide to each Nationally Recognized Municipal Securities Information Repository (as referred to in Rule 15c2-12) and others, on an annual basis, certain financial and operating data concerning the Department, financial statements, notice of certain events if material, and certain other notices, all as described in the Continuing Disclosure Certificate. The undertaking is an obligation of the Department that is enforceable as described in the Continuing Disclosure Certificate. Beneficial Owners of the Series 2003 Bonds are third party beneficiaries of the Continuing Disclosure Certificate. The execution of the Continuing Disclosure Certificate is a condition precedent to the obligation of the Underwriters to purchase the Series 2003 Bonds. The form of the Master Continuing Disclosure Certificate and the proposed form of the Series 2003 Certificate are contained in Appendix D. The City and County has never failed to comply with any previous undertaking under Rule 15c2-12.

MISCELLANEOUS

Additional information may be obtained, upon request, from either the Department of Budget and Fiscal Services or the Department of Environmental Services of the City and County.

Reference in this Official Statement to the Act, the City Charter, the Bond Resolution and the Series 2003 Resolution do not purport to be complete. Refer to the Act, the City Charter, the Bond Resolution and the Series 2003 Resolutions for full and complete details of their provisions. Copies of the City Charter, the Bond Resolution and the Series 2003 Resolution are on file with the City Clerk of the City and County.

The agreements of the City and County with holders of the Series 2003 Bonds are fully set forth in the Bond Resolution and the Series 2003 Resolution. Neither any advertisement of the Series 2003 Bonds nor this Official Statement is to be construed as a contract with purchasers of the Series 2003 Bonds.

Any statements in this Official Statement involving matters of opinion or of estimates, whether or not expressly stated, are intended merely as expressions of opinion or estimates, and not as representations of fact, and no representation is made that any of the estimates will be realized.

The City and County's use of certain information included in this Official Statement has been furnished or reviewed and authorized by the sources described below. While the City and County believes that these sources are reliable, the City and County has not independently verified this information and does not guarantee the accuracy or completeness of the information furnished by the respective sources. The City and County is relying on certificates from certain sources, to be delivered at or prior to the time of delivery of the Series 2003 Bonds, as to the accuracy of such information provided or authorized by such sources.

The information regarding DTC and DTC's book-entry system has been furnished by DTC.

Appendix A contains extracts of the financial statements of the City and County as of June 30, 2002, relating to the Sewer Fund, together with the auditor's report thereon.

The execution and delivery of this Official Statement by the Director of Budget and Fiscal Services and the Acting Director of Environmental Services have been duly authorized by the City and County.

Director of Budget
and Fiscal Services
City and County of Honolulu

Acting Director of Environmental Services
City and County of Honolulu

Appendix A

Extracts from Audited Financial Statements of City and County

Appendix B

Multi-Mode Provisions

The Series Certificate contains provisions relating to the determination of interest on the Series 2003 Bonds and related matters, certain of which are summarized below. This summary does not purport to be comprehensive or definitive and is subject to all of the provisions of the Series 2003 Certificate, to which reference is hereby made. Copies of the Series 2003 Certificate are available from the City and County.

Definitions

In addition to the terms defined elsewhere in this Official Statement, the following terms shall have the following meanings with respect to each separate series of the Series 2003 Bonds, unless the context otherwise requires:

“AA’ *Financial Commercial Paper Rate*,” on any date of determination, means (a) for Auction Periods of 35 days or less, the interest equivalent of commercial paper having a maturity of 30 days, (b) for Auction Periods greater than 35 days and less than 75 days, the interest equivalent of commercial paper having a maturity of 60 days, (c) for Auction Periods greater than 75 days and less than 105 days, the interest equivalent of commercial paper having a maturity of 90 days; as each such rate is published on the Business Day prior to such date by the Board of Governors of the Federal Reserve System on its Website at <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 Commercial Paper 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 any Broker-Dealer) 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 for the immediately preceding Interest Payment 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.

“*Adjustable Rate*” means a daily, weekly, monthly or longer rate borne by any Series 2003 Bond following conversion of such Bond from an Auction Rate Bond.

“*Adjustable Rate Conversion Date*” means a date on which any Series 2003 Bonds begin to bear interest at an Adjustable Rate.

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

- (a) the “AA” Financial Commercial Paper Rate on such date; and
- (b) 1.00 minus the Statutory Corporate Tax Rate on such date.

“*All Hold Rate*,” on any date of determination, means the interest rate per annum equal to 90% (as such percentage may be adjusted as described herein) of the lesser on such date of:

- (a) the After-Tax Equivalent Rate on such date; and
- (b) the Applicable 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 Auction Rate Bonds Rate*” means the rate per annum at which interest is payable on the Auction Rate Bonds for any Auction Period, but not exceeding the maximum rate permitted by the laws of the State.

“*Applicable Index*” means the Kenny Index in the case of the Series 2003A Bonds or the BMA Index in the case of the Series 2003B Bonds.

“*Applicable Number of Business Days*” means the greater of (i) two Business Days or (ii) 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 Number of Days*” means (i) in the case of the Series 2003A Bonds, 365 or 366 days, as appropriate, and (ii) in the case of the Series 2003B Bonds, 360 days.

“*Applicable Percentage*,” on any date of determination, means the percentage determined (as such percentage may be adjusted as described herein) based on the lower of the prevailing credit ratings on the Auction Rate Bonds in effect at the close of business on the Business Day immediately preceding such date, as set forth below:

Credit Ratings

<u>Moody's</u>	<u>S&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-” to “BBB+”	200%
Below “Baa3”	Below “BBB-”	Below “BBB-”	265%

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

“*Authorized Denominations*” means (i) with respect to the Series 2003 Bonds bearing interest at an Auction Rate, \$50,000 or any integral multiple thereof, (ii) with respect to the Bonds outstanding as Adjustable Rate Bonds other than when bearing interest at a Long Rate in excess of one year, \$50,000 or any integral multiple thereof, and (iii) with respect to the Bonds bearing interest at a Fixed Rate or at a Long Rate in excess of one year, \$5,000 or any integral multiple thereof.

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

“*Auction Agency Agreement*” means each initial Auction Agency Agreement between the Paying Agent 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 the initial Auction Agent appointed pursuant to the Series 2003 Certificate and any successor appointed as such.

“*Auction Agent Fee*” means the fee to be paid to the Auction Agent for the services rendered by it under the Auction Agency Agreement and the Broker-Dealer Agreement.

“*Auction Agent Fee Rate*,” on any Auction Date, means the rate per annum at which the fee to be paid to the Auction Agent for the services rendered by it under the Auction Agency Agreement and the Broker-Dealer Agreement with respect to such Auction Date accrues, as provided in the Auction Agency Agreement.

“*Auction Date*” means each initial Auction Date set forth in the Series 2003 Certificate 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 Auction Rate Bonds is no longer maintained in book-entry form by the Depository;
- (b) each Auction Period commencing after the occurrence and during the continuance of a Payment Default; or
- (c) any Auction Period commencing less than the Applicable Number of Business Days after the cure or waiver of a Payment Default.

Notwithstanding the foregoing, the Auction Date for one or more Auction Periods may be changed as described herein.

“*Auction Period*” means, with respect to any Auction Rate Bonds (i) each successive 35-day period after the Initial Interest Period, commencing on a Friday (or the Business Day following the last day of the prior Interest Period, if the prior Interest Period does not end on a Thursday), and ending on (and including) a Thursday (unless such day 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), and (ii) if, and for so long as, Interest Payment Dates are specified to occur at the end of each Auction Period following a change therein, each period commencing on an Interest Payment Date and ending on but excluding the next succeeding Interest Payment Date.

“*Auction Procedures*” means the procedures set forth herein under “Auction Procedures”.

“*Auction Rate*” means the rate of interest per annum on any Auction Date that results from the implementation of the Auction Procedures.

“*Auction Rate Bonds*” means the Series 2003 Bonds outstanding as Auction Rate Bonds prior to their conversion to bear interest at a Fixed Rate or an Adjustable Rate.

“*Available Auction Rate Bonds*” has the meaning set forth herein under “Auction Procedures.”

“*Bid*” has the meaning set forth herein under “Auction Procedures.”

“*Bidder*” has the meaning set forth herein under “Auction Procedures.”

“*BMA Index*” means, on any date, a rate determined on the basis of the seven-day high grade market index of tax-exempt variable rate demand obligations, as produced by Municipal Market Data and published or made available by the Bond Market Association (“BMA”) or any person acting in cooperation with or under the sponsorship of BMA and acceptable to the Market Agent (if any) for the applicable Series of Bonds, and effective from such date; provided, however, that if such index ceases to be available, “BMA Index” means any index reasonably selected by the City and County and acceptable to the Market Agent, which is widely available to dealers in municipal securities, and which measures the interest rate of municipal securities that bear interest at short-term rates or variable rates.

“*Broker-Dealer*” means UBS PaineWebber Inc. for the Series 2003A Bonds and Citigroup Global Markets Inc. for the Series 2003B Bonds, 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 a capital surplus of at least \$100,000,000, (iii) has been selected by the City and County with the approval of the Market Agent (which approval shall not be unreasonably withheld), and (iv) has entered into a Broker-Dealer Agreement that remains effective.

“Broker-Dealer Agreement” means each initial Broker-Dealer Agreement between the Auction Agent and a Broker-Dealer, and any similar agreement with an additional or successor Broker-Dealer pursuant to which the Broker-Dealer agrees to participate in Auctions as set forth in the Auction Procedures, 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 it under the Broker-Dealer Agreement.

“Broker-Dealer Fee Rate,” on any Auction Date, means the rate per annum at which the service charge to be paid to the Broker-Dealer for the services rendered by it with respect to such Auction Date accrues, as provided in the Broker-Dealer Agreement and the Auction Agency Agreement.

“Business Day” means (a) in the case of the Series 2003A Bonds, any day other than (i) April 14, April 15, December 30, December 31, (ii) any day on which banks located in the City of New York, New York, the New York Stock Exchange, the Paying Agent or the Auction Agent, are authorized or permitted by law or executive order to close; (b) in the case of the Series 2003B Bonds, any day other than a Saturday, Sunday, holiday or day on which banks located in the City of New York, New York, or the New York Stock Exchange, the Paying Agent or the Auction Agent are authorized or permitted by law or executive order to close; and (c) such other days as may be agreed to in writing by the Paying Agent, the Market Agent, the Auction Agent, the Broker-Dealer and the City and County.

“Change of Preference Law” means, with respect to any Owner of Auction Rate Bonds, 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 hereof 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.

“Conversion Date” means either the Fixed Rate Conversion Date or the Adjustable Rate Conversion Date as the context may require.

“Default Rate” on any date of determination means the interest rate per annum equal to the lesser of (1) the Applicable Percentage of the Applicable Index and (2) the Maximum Interest Rate.

“Depository” means Cede & Co., as the nominee of DTC and its successors and assigns or any other securities depository selected or approved by the City and County.

“Existing Owner” means (a) with respect to and for the purpose of dealing with the Auction Agent in connection with an Auction, a Person who is 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 Auction Rate Bonds.

“Favorable Opinion” means an Opinion of Counsel addressed to the City and County to the effect that the action proposed to be taken is authorized or permitted by the Act and the Resolutions and will not adversely affect any exclusion from gross income of interest on the applicable Series 2003 Bonds for federal income tax purposes.

“Fixed Rate” means the fixed rate or rates of interest on any Series 2003 Bonds to the maturity thereof.

“Fixed Rate Conversion Date” means a date on which any Series 2003 Bonds begin to bear interest at a Fixed Rate.

“Hold Order” has the meaning set forth herein under “Auction Procedures.”

“Initial Interest Payment Date” means the respective initial interest payment dates for the Series 2003A Bonds and the Series 2003B Bonds set forth in the Series 2003 Certificate.

“Initial Interest Period” means the period from and including the date of delivery of the Series 2003 Bonds and ending on and including the day before the Initial Interest Payment Date.

“Interest Amount” means the amount of interest distributable in respect of each \$50,000 in principal amount (taken, without rounding, to .0001 of one cent) of Auction Rate Bonds for any Interest Period or part thereof, calculated as described herein under “Computation of Interest.”

“Interest Payment Date” means, (i) with respect to Series 2003 Bonds bearing interest at an Auction Rate, the Initial Interest Payment date and thereafter the day following the end of each Auction Period, as such period may be changed as described herein, (ii) with respect to Series 2003 Bonds bearing interest at an Adjustable Rate, the dates set forth in the Series 2003 Certificate, (iii) the Adjustable Rate Conversion Date and the Fixed Rate Conversion Date, and (iv) after the Fixed Rate Conversion Date, each January 1 and July 1 commencing with the January 1 or July 1 that occurs no sooner than three months after the Fixed Rate Conversion Date; provided that if any such date is not a Business Day, interest shall be paid on the next succeeding Business Day with the same effect as if paid on such date.

“Interest Period” means with respect to Auction Rate Bonds, the Initial Interest Period and each Auction Period thereafter.

“Kenny Index” means the 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.

“Mandatory Tender Date” means a Conversion Date.

“Market Agent” means the market agent or market agents appointed pursuant to the Series 2003 Certificate and its or their successors or assigns.

“Market Agent Agreement” means each initial Market Agent Agreement between the Paying Agent and a 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 12% per annum or any lower rate which is the maximum rate permitted by law.

“Maximum Rate,” on any date of determination, means 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 and (ii) the Applicable Index on such date; and

(b) the Maximum Interest Rate;

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

“Order” shall have the meaning set forth herein under “Auction Procedures.”

“Owner” as used herein means the beneficial owner of any Series 2003 Bonds.

“Participant” means a member of or participant in the Depository.

“Payment Default” means failure by the City and County to make payment of interest on, premium, if any, and principal of the Auction Rate Bonds when due, and the failure of the Bond Insurer to make payments with respect thereto under the Bond Insurance Policy.

“Person” means and includes, unless otherwise specified, an individual, public entity, company, trust, estate, partnership or association.

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

“Prevailing Market Conditions” means, to the extent relevant (in the professional judgment of the Remarketing Agent) at the time of establishment of the Fixed Rate for the Series 2003 Bonds as described herein under “Conversion,” (a) interest rates on comparable securities then being issued and traded; (b) other financial market rates and indices that may have a bearing on rates of interest; (c) general financial market conditions (including then-current forward supply figures) that may have a bearing on rates of interest; and (d) the financial condition, results of operation and credit standing of the City and County to the extent such standing has a bearing on rates of interest.

“Rating Confirmation” means a letter from each Rating Agency then providing a rating for a series of the Series 2003 Bonds confirming that an action proposed to be taken will not, in and of itself, have the effect of reducing the rating then applicable to such Bonds.

“Record Date” means, with respect to Series 2003 Bonds outstanding as Auction Rate Bonds, (a) if, and for so long as, Interest Payment Dates are specified to occur at the end of each Auction Period, as provided in Section 1.22 of this Multi-Mode Annex, the Applicable Number of Business Days immediately preceding each Interest Payment Date and (b) so long as interest is payable with respect thereto semiannually, one Business Day prior to each Interest Payment Date.

“Redemption Date” means, when used with respect to any Auction Rate Bonds to be redeemed, the date fixed for such redemption.

“Registrar” means the Paying Agent or any separate registrar for the Series 2003 Bonds appointed in accordance with the provisions of the Resolution.

“Remarketing Agent” means each initial remarketing agent named in the Series 2003 Certificate or any other remarketing agent appointed by the City and County.

“SEC” means the Securities and Exchange Commission.

“Securities Exchange Act” means the Securities Exchange Act of 1934, as amended.

“Sell Order” has the meaning set forth herein under “Auction Procedures.”

“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, which on the date hereof is 35%.

“Submission Deadline” means 1:00 p.m., New York City time, on any Auction Date or such 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 set forth herein under “Auction Procedures.”

“Submitted Hold Order” has the meaning set forth herein under “Auction Procedures.”

“Submitted Order” has the meaning set forth herein under “Auction Procedures.”

“Submitted Sell Order” has the meaning set forth herein under “Auction Procedures.”

“Sufficient Clearing Bids” has the meaning set forth herein under “Auction Procedures.”

“Undelivered Bonds” means any Series 2003 Bonds described herein under “Undelivered Bonds.”

“Winning Bid Rate” has the meaning set forth herein under “Auction Procedures.”

General Provisions

The Series 2003 Bonds shall be initially issued as Auction Rate Bonds subject to conversion to a Fixed Rate or an Adjustable Rate. The Auction Rate Bonds shall bear interest for the Initial Interest Period at the rate of interest per annum set forth in the Series 2003 Certificate. For each Auction Period thereafter, until the Fixed Rate Conversion Date or the Adjustable Rate Conversion Date, if any, the unpaid principal amount hereof from time to time outstanding shall bear interest determined in accordance with the auction provisions described herein, payable on each Interest Payment Date and on the date of payment or redemption of principal thereof to the extent of interest accrued on the principal then being paid or redeemed, such interest to accrue from the later of the date thereof or the date through which interest has been paid or duly provided for. Interest at the Auction Rate established from time to time shall be computed for the actual number of days elapsed on the basis of a year consisting of the Applicable Number of Days. In no event shall the Auction Rate on the Auction Rate Bonds exceed the Maximum Rate.

Initially, the Auction Rate Bonds shall be registered in the name of Cede & Co., as the nominee of DTC, as Depository. So long as the ownership of the Auction Rate Bonds is maintained in book-entry form by the Depository, an Existing Owner may sell, transfer or otherwise dispose of its beneficial interest in Auction Rate Bonds 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 or mandatory tenders such Existing Owner, its Broker-Dealer or its Participant advises the Auction Agent of such transfer.

Interest on Auction Rate Bonds

(a) Interest on the Auction Rate Bonds shall accrue for each Auction Period and shall be payable in arrears on each Interest Payment Date.

(b) The rate of interest on the Auction Rate Bonds for the Initial Interest Period shall be such rate of interest per annum as shall be set forth in the Series 2003 Certificate. The rate of interest on the Auction Rate Bonds for each subsequent Auction Period, to but not including the Fixed Rate Conversion Date or Adjustable Rate Conversion Date, shall be the Auction Rate unless the Auction Rate exceeds the Maximum Rate, in which case the rate of interest on the Auction Rate Bonds 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 Auction Rate Bonds for such Auction Period shall be the Maximum Rate; provided that if, on any Auction Date, an Auction is not held for any reason (except as described in clause (iv) of this paragraph), then the rate of interest for the next succeeding Auction Period shall equal the Maximum Rate on such Auction Date. Notwithstanding the foregoing:

(i) if the ownership of the Auction Rate Bonds is no longer maintained in book-entry form by the Depository, the rate of interest on the Auction Rate Bonds for any Auction Period commencing after the delivery of certificates representing Auction Rate Bonds shall equal the Maximum Rate on the Business Day immediately preceding the first day of such Auction Period;

(ii) if a Payment Default occurs, Auctions will be suspended and the Applicable Auction Rate Bonds 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 two Business Days after, such Payment Default is cured will equal the Default Rate;

(iii) if a proposed conversion to a Fixed Rate or Adjustable Rate shall have failed, and the next succeeding Auction Date shall be two or fewer Business Days after (or on) any such failed Fixed Rate Conversion Date or Adjustable Rate Conversion Date, then an Auction shall not be held on such Auction Date and the rate of interest on the Auction Rate Bonds subject to the failed conversion for the next succeeding Auction Period shall be equal to the Maximum Rate calculated as of the first Business Day of such Auction Period; or

(iv) if an Auction is scheduled to occur for the next Auction Period on a date that was reasonably expected to be a Business Day, but such Auction does not occur because such date is later not considered to be a Business Day, the Auction shall nevertheless be deemed to have occurred, and the applicable Auction Rate in effect for the next Auction Period will be the Auction Rate in effect for the preceding Interest Period and such Auction Period will generally be 35 days in duration, beginning on the Business Day following the date of the deemed Auction and ending on (and including) the next applicable Auction Date (unless that Auction Date is not followed by a Business Day, in which case on the next succeeding day that is followed by a Business Day). If the preceding Interest Period was other than approximately 35 days in duration, the Auction Rate for the deemed Auction will instead be the rate of interest determined by the Market Agent on equivalently rated auction securities with a comparable length of auction period.

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

Payments

So long as the Auction Rate Bonds are registered in the name of the Depository or the nominee thereof, payment of interest (other than at maturity) and premium, if any, on, and of principal at redemption of, the Auction Rate Bonds shall be made to the Depository by wire transfer provided proper wire instructions are received. Each Owner of Auction Rate Bonds, by such Owner's purchase of Auction Rate Bonds, appoints the Paying Agent as its agent in connection with the payment by such Owner of its share, if any, of the amounts payable as fees to the Auction Agent and the Broker-Dealers.

Auction Procedures

Prior to a Fixed Rate Conversion Date or an Adjustable Rate Conversion Date, Auctions shall be conducted on each Auction Date (other than the Auction Date immediately preceding (i) each Auction Period commencing after the ownership of the Auction Rate Bonds is no longer maintained in book-entry form by the Depository; (ii) each Auction Period commencing after the occurrence and during the continuance of a Payment Default; or (iii) any Auction Period commencing less than two 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) Bids

(i) Prior to the Submission Deadline on each Auction Date:

(A) each Existing Owner of Auction Rate Bonds may submit to a Broker-Dealer information as to:

(1) the principal amount of Outstanding Auction Rate Bonds, 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;

(2) the principal amount of Outstanding Auction Rate Bonds, 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

(3) the principal amount of Outstanding Auction Rate Bonds, 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) one or more Broker-Dealers may contact Potential Owners to determine the principal amount of Auction Rate Bonds 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.

For the purposes hereof, the communication to a Broker-Dealer of information referred to in clause (A)(1), (A)(2), (A)(3) 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)(1) of this paragraph (i) is hereinafter referred to as a "Hold Order" and collectively as "Hold Orders;" (y) clause (A)(2) or (B) of this paragraph (i) is hereinafter referred to as a "Bid" and collectively as "Bids" and (z) clause (A)(3) of this paragraph (i) is hereinafter referred to as a "Sell Order" and collectively as "Sell Orders."

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

(1) the principal amount of Outstanding Auction Rate Bonds specified in such Bid if the Auction Rate determined as provided herein shall be less than the rate specified in such Bid; or

(2) such principal amount or a lesser principal amount of Outstanding Auction Rate Bonds to be determined as set forth in (d)(i)(D) below, if the Auction Rate determined as provided herein shall be equal to the rate specified in such Bid; or

(3) such principal amount or a lesser principal amount of Outstanding Auction Rate Bonds to be determined as set forth in (d)(ii)(C) below if the rate specified shall be higher than the Maximum Rate and Sufficient Clearing Bids have not been made.

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

(1) the principal amount of Outstanding Auction Rate Bonds specified in such Sell Order; or

(2) such principal amount or a lesser principal amount of Outstanding Auction Rate Bonds as set forth in (d)(ii)(C) below if Sufficient Clearing Bids have not been made.

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

(1) the principal amount of Outstanding Auction Rate Bonds specified in such Bid if the Auction Rate determined as provided herein shall be higher than the rate specified in such Bid; or

(2) such principal amount or a lesser principal amount of Outstanding Auction Rate Bonds as set forth in (d)(i)(E) below if the Auction Rate determined as provided herein shall be equal to the rate specified in such Bid.

(b) Submission By Broker-Dealers 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 Auction Rate Bonds that are the subject of such Order;

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

(1) the principal amount of Auction Rate Bonds, if any, subject to any Hold Order placed by such Existing Owner;

(2) the principal amount of Auction Rate Bonds, if any, subject to any Bid placed by such Existing Owner and the rate specified in such Bid; and

(3) the principal amount of Auction Rate Bonds, if any, subject to any Sell Order placed by such Existing Owner; and

(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 Auction Rate Bonds 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 Auction Rate Bonds held by such Existing Owner and not subject to an Order submitted to the Auction Agent.

(iv) Neither the City and County, the Paying Agent 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 Auction Rate Bonds 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 Auction Rate Bonds held by such Existing Owner, and if the aggregate principal amount of Auction Rate Bonds subject to such Hold Orders exceeds the aggregate principal amount of Auction Rate Bonds held by such Existing Owner, the aggregate principal amount of Auction Rate Bonds subject to each such Hold Order shall be reduced pro rata to cover the aggregate principal amount of Outstanding Auction Rate Bonds held by such Existing Owner;

(B) (1) any Bid shall be considered valid up to and including the excess of the principal amount of Outstanding Auction Rate Bonds held by such Existing Owner over the aggregate principal amount of Auction Rate Bonds subject to any Hold Orders referred to in clause (A) of this paragraph (v);

(2) subject to subclause (1) 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 Auction Rate Bonds 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 Auction Rate Bonds subject to each Bid with the same rate shall be reduced pro rata to cover the stated amount of Auction Rate Bonds equal to such excess;

(3) subject to subclauses (1) and (2) 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

(4) in any such event, the aggregate principal amount of Outstanding Auction Rate Bonds, 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 Auction Rate Bonds held by such Existing Owner over the aggregate principal amount of Auction Rate Bonds 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 Auction Rate Bonds 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 Auction Rate Bonds 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 Auction Rate Bonds 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 Auction Rate Bonds 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 Auction Rate Bonds over the sum of the aggregate principal amount of Outstanding Auction Rate Bonds subject to

Submitted Hold Orders (such excess being hereinafter referred to as the “Available Auction Rate Bonds”); and

(B) from such Submitted Orders whether:

(1) the aggregate principal amount of Outstanding Auction Rate Bonds 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:

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

(3) the aggregate principal amount of Outstanding Auction Rate Bonds subject to Submitted Sell Orders;

(in the event such excess or such equality exists, other than because the sum of the principal amounts of Auction Rate Bonds in subclauses (2) and (3) above is zero because all of the Outstanding Auction Rate Bonds are subject to Submitted Hold Orders, such Submitted Bids in subclause (1) 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:

(1) (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 Auction Rate Bonds subject to such Submitted Bids; and

(2) (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 (1) above would continue to hold an aggregate principal amount of Outstanding Auction Rate Bonds which, when added to the aggregate principal amount of Outstanding Auction Rate Bonds to be purchased by such Potential Owners described in subclause (2) above, would equal not less than the Available Auction Rate Bonds.

(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 Auction Rate Bonds 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 Auction Rate Bonds 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 Auction Rate Bonds

Existing Owners shall continue to hold the principal amount of Auction Rate Bonds that are subject to Submitted Hold Orders, and, based on the determinations made pursuant (c)(i) above. 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 Auction Rate Bonds 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 Auction Rate Bonds 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 Auction Rate Bonds 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 Auction Rate Bonds subject to such Submitted Bid, unless the aggregate principal amount of Outstanding Auction Rate Bonds subject to all such Submitted Bids shall be greater than the principal amount of Auction Rate Bonds (the "remaining principal amount") equal to the excess of the Available Auction Rate Bonds over the aggregate principal amount of Auction Rate Bonds 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 Auction Rate Bonds subject to such Submitted Bid, but only in an amount equal to the aggregate principal amount of Auction Rate Bonds obtained by multiplying the remaining principal amount by a fraction the numerator of which shall be the principal amount of Outstanding Auction Rate Bonds 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 Auction Rate Bonds 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 Auction Rate Bonds obtained by multiplying the excess of the aggregate principal amount of Available Auction Rate Bonds over the aggregate principal amount of Auction Rate Bonds 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 Auction Rate Bonds subject to such Submitted Bid and the denominator of which shall be the sum of the principal amounts of Outstanding Auction Rate Bonds 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 Auction Rate Bonds 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 Auction Rate Bonds 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 Auction Rate Bonds 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 Auction Rate Bonds subject to such Submitted Bid or Submitted Sell Order, but in both cases only in an amount equal to the aggregate principal amount of Auction Rate Bonds obtained by multiplying the aggregate principal amount of Auction Rate Bonds 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 Auction Rate Bonds 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 Auction Rate Bonds subject to all such Submitted Bids and Submitted Sell Orders.

(iii) If all Outstanding Auction Rate Bonds 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 Auction Rate Bonds 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 Auction Rate Bonds to be purchased or sold by any Existing Owner or Potential Owner so that the principal amount of Auction Rate Bonds purchased or sold by each Existing Owner or Potential Owner shall be equal to an Authorized Denomination, even if such allocation results in one or more of such Potential Owners not purchasing any Auction Rate Bonds.

(e) Determinations

Based on the results of each Auction, the Auction Agent shall determine the aggregate principal amount of Auction Rate Bonds to be purchased and the aggregate principal amount of Auction Rate Bonds 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 Auction Rate Bonds to be sold differs from such aggregate principal amount of Auction Rate Bonds 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, Auction Rate Bonds.

(f) Certain Orders Not Permitted. The City and County may not submit an Order in any Auction. The Auction Agent shall have no duty or liability in monitoring or enforcing compliance with this provision.

Notice of Payment Defaults and Cures; Payment of Service Charges

(a) The City and County shall pay to the Paying Agent, on behalf of the Owners of the Auction Rate Bonds, in same day funds out of amounts in the Sewer Fund, for payment to the Auction Agent, (i) when due, an amount equal to the Auction Agent Fee as calculated in the Auction Agency 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. on the Business Day immediately succeeding each Interest Payment Date, the Paying Agent will determine if a Payment Default has occurred. If a Payment Default has occurred, the Paying Agent shall notify the Auction Agent and Broker-Dealer by 1:00 p.m. of such Payment Default. If a Payment

Default has been cured, the Paying Agent shall so notify the Auction Agent and the Broker-Dealer by 5:00 p.m. on the day such Payment Default is cured.

Calculation of Maximum Rate, All Hold Rate and Default Rate

The Auction Agent shall calculate the Maximum Interest Rate, the Maximum Rate and the All Hold Rate on each Auction Date.

Computation of Interest

The amount of interest distributable to Owners of Auction Rate Bonds in respect of each \$50,000 in principal amount thereof for any Interest Period or part thereof shall be calculated by applying the Applicable Auction Rate Bonds Rate for such Interest Period or part thereof to the principal amount of \$50,000, multiplying such product by the actual number of days in the Interest Period or part thereof concerned divided by the Applicable Number of Days and truncating the resultant figure to the nearest one cent. In the event an Interest Payment Date occurs in any Interest Period on a date other than the first day of such Interest Period, the Paying Agent, 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 Paying Agent is required to make the foregoing calculation not later than the close of business on each Auction Date.

Notification of Rates, Amounts and Payment Dates

(a) The Paying Agent is required to determine the aggregate amount of interest distributable on the next succeeding Interest Payment Date to the Holders of the Auction Rate Bonds. So long as the ownership of the Auction Rate Bonds is maintained in book-entry form by the Depository, the Paying Agent is required to advise the Depository of a change of Record Date for the Auction Rate Bonds at least two Business Days prior thereto.

(b) Promptly after the date of original issuance of the Series 2003 Bonds and each Interest Payment Date, and in any event at least 10 days prior to each Interest Payment Date, the Paying Agent shall:

(i) so long as no Payment Default has occurred and is continuing and the ownership of the Auction Rate Bonds is maintained in book-entry form by the Depository, 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 and notify the Auction Agent of any discrepancy therein; and

(ii) advise the Depository, so long as the ownership of the Auction Rate Bonds is maintained in book-entry form by the Depository, of the Applicable Auction Rate Bonds Rate and the Interest Amount in respect of the next succeeding Auction Period.

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, two Business Days next preceding the earlier of the new Interest Payment Date or the old Interest Payment Date, the Paying Agent shall, by such means as the Paying Agent 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 Auction Rate Bonds is maintained in book-entry form by the Depository.

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 Applicable 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 or market convention such that Auction Rate Bonds paying the Maximum Rate, Auction Rate Bonds paying the All Hold Rate and Auction Rate Bonds paying the Default Rate shall have, respectively, equal market values before and after such Change of Preference Law or market convention. Prior to any such adjustment, the City and County shall give notice thereof to each Rating Agency, and no such adjustment shall be made unless such adjustment will not adversely affect the rating on any of the Series 2003

Bonds. 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 or market convention, 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 Auction Rate Bonds;
- (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 Auction Rate Bonds.

(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 Applicable Index used to determine the Default Rate by delivering to the City and County, the Paying Agent and the Auction Agent at least 10 days prior to the Auction Date on which the Market Agent desires to effect such change a Favorable Opinion and a notice in the form required by the Series 2003 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 Applicable Index used to determine the Default Rate, which shall be specified in such notice.

Conversion

The Auction Rate Bonds may be converted to bear interest at a Fixed Rate to their final maturity or may be converted to bear interest at an Adjustable Rate, in either case upon the delivery by the City and County to the Paying Agent of a Favorable Opinion. Any Conversion Date shall be the Business Day next succeeding the last day of an Auction Period. Following any such Conversion Date, the Series 2003 Bonds so converted shall bear interest at an Adjustable Rate or a Fixed Rate, as applicable, determined as provided in the Series 2003 Certificate.

Not later than the 15th day preceding a Conversion Date, notice of the conversion shall be given by first class mail by the Paying Agent to the Auction Agent and the Holders of all such Bonds being converted. Such notice shall inform the Auction Agent and the Owners of (i) the proposed Conversion Date; (ii) the conditions to the conversion; and (iii) the matters required to be stated with respect to mandatory tender and purchases of Series 2003 Bonds being converted.

If, as of 12:00 Noon on the Conversion Date, (1) sufficient funds are not available to purchase all Series 2003 Bonds which are then required to be purchased, or (2) the Favorable Opinion is not received by the City and County, the conversion shall not be effective, the Series 2003 Bonds so being converted shall continue to be outstanding as Auction Rate Bonds, and the Paying Agent shall, not later than 4:00 p.m., provide notice of the failed conversion to the Auction Agent and the Owners of such Bonds. The Auction Rate Bonds that were the subject of the failed conversion shall bear interest at the Maximum Rate, determined by the Auction Agent as provided herein, for the Auction Period beginning on the date of such failed conversion.

Mandatory Tender Upon Conversion; Certain Notices

Any Series 2003 Bonds to be converted to bear interest at a Fixed Rate or Adjustable Rate shall be subject to mandatory tender for purchase on the Conversion Date, at a price equal to the principal amount thereof plus accrued interest, if any, to the Conversion Date.

Any notice of conversion given to Owners shall, in addition to the other matters to be stated therein, also specify that all Outstanding Series 2003 Bonds subject to such conversion are subject to mandatory tender and will be purchased on the Conversion Date by payment of a purchase price equal to the principal amount thereof plus accrued interest, if any, to the Conversion Date; that the Holder of the Series 2003 Bonds has no right to retain such Bonds on and after the Mandatory Tender Date, but that such Holder shall be required to tender or be deemed to

have tendered the Auction Rate Bonds for payment on the Mandatory Tender Date; and that if the conditions to such conversion are not satisfied, such Bonds will not be subject to tender and will remain outstanding as Auction Rate Bonds.

On any Conversion Date, the Paying Agent shall pay the purchase price of the Series 2003 Bonds required to be tendered for purchase, surrendered as provided above properly endorsed for transfer in blank with all signatures guaranteed, to the selling Owners thereof on or before 3:00 p.m.

All Series 2003 Bonds to be purchased on any Conversion Date shall be required to be delivered to the designated office of the Paying Agent, or its designated agent for such purposes, at or before 12:00 Noon on such date. If the Owner of any Series 2003 Bonds that is subject to purchase fails to deliver such Bonds to the Paying Agent, or its designated agent for such purposes, for purchase on the purchase date, and if the Paying Agent, or its designated agent for such purposes, is in receipt of the purchase price therefor, such Bonds shall nevertheless be deemed tendered and purchased on the Conversion Date and shall be Undelivered Bonds pursuant and registration of the ownership of such Bond shall be transferred to the purchaser thereof as provided below. The Paying Agent shall, as to any Undelivered Series 2003 Bonds, (i) promptly notify the Remarketing Agent, the Auction Agent and the Registrar of such non-delivery and (ii) the Registrar shall place a stop transfer against an appropriate amount of Series 2003 Bonds registered in the name of the Owner(s) on the Series 2003 Bond Register. The Registrar shall place such stop transfer(s) commencing with the lowest serial number Series 2003 Bonds registered in the name of such holder(s) (until stop transfers have been placed against an appropriate amount of Series 2003 Bonds) until the appropriate tendered Series 2003 Bonds are delivered to the Paying Agent, or its designated agent. Upon such delivery, the Registrar shall make any necessary adjustments to the Series 2003 Bond Register. Pending delivery of such tendered Series 2003 Bonds, the Paying Agent, or its designated agent, shall hold the purchase price therefor uninvested in a segregated subaccount for the benefit of such Owners.

Inadequate Funds for Tenders; Failed Conversion

If the funds available for purchases of Series 2003 Bonds are inadequate for the purchase of all Series 2003 Bonds tendered on any Conversion Date, or if a proposed conversion to a Fixed Rate or Adjustable Rate otherwise fails as provided above, the Paying Agent shall: (a) return all tendered Series 2003 Bonds to the Owners thereof; (b) return all moneys received for the purchase of such Bonds to the persons providing such moneys; and (c) notify the City and County, the Auction Agent and the Remarketing Agent of the return of such Bonds and moneys and the failure to make payment for tendered Series 2003 Bonds. After any such failed conversion the Series 2003 Bonds subject to the failed conversion shall remain outstanding as Auction Rate Bonds, Auctions shall be conducted beginning on the first Auction Date occurring more than two Business Days after the failed Conversion Date, and interest payable thereon shall be determined and paid according to the auction rate provisions described above.

Undelivered Bonds

Any Series 2003 Bonds which are required to be tendered on a Conversion Date and that are not delivered on the Conversion Date, and for the payment of which there has been irrevocably held in trust in a segregated subaccount for the benefit of such Owner an amount of money sufficient to pay the purchase price, including any accrued interest due to (but not after) such purchase date with respect to such Bonds, shall be deemed to have been purchased, and shall be Undelivered Bonds. In the event of a failure by an Owner to tender its Series 2003 Bonds on or prior to the required date, said Owner of such Undelivered Bonds shall not be entitled to any payment other than the purchase price due on the purchase date and Undelivered Bonds in the hands of such non-delivering Owner shall no longer accrue interest or be entitled to the benefits of the Resolution, except for the payment of the purchase price due on the purchase date; *provided, however*, that the indebtedness represented by such Bonds shall not be extinguished, and the Paying Agent and Registrar shall transfer, authenticate and deliver such Bonds as provided below. The Paying Agent shall give telephonic notice to the Registrar, promptly confirmed by mail, of all Undelivered Bonds.

With respect to any Undelivered Bond, the Paying Agent, acting hereunder and pursuant to the power of attorney granted by such Owner by its acceptance of such Bonds, shall do or cause the Registrar to do the following:

- (a) Assign, endorse, and register the transfer of such Bonds to the purchaser or purchasers thereof;

- (b) Authenticate and deliver a new Series 2003 Bond or Series 2003 Bonds, as appropriate, to the purchaser or purchasers thereof;
- (c) Execute an acknowledgment that the Owner of Undelivered Bonds holds such Undelivered Bond for the benefit of the new purchaser or purchasers thereof, who shall be identified in such acknowledgment;
- (d) Promptly notify by first class mail the Owner of such Undelivered Bond that:
 - (i) the Paying Agent has acted pursuant to such power of attorney to transfer the Undelivered Bond and to perform the other acts set forth herein;
 - (ii) the Undelivered Bond is no longer Outstanding; and
 - (iii) funds equal to the applicable purchase price for such Bond are being held on behalf of such Owner, without interest, in the segregated subaccount established for such purpose by and with the Paying Agent.
- (e) Enter on the Series 2003 Bond Register that the Undelivered Bond is no longer Outstanding; and
- (f) Subject to the other provisions of the Resolutions, hold the purchase price for such Bond in the subaccount established for such purpose, without interest, and pay such purchase price and any unpaid interest due on the purchase date to such Owner upon presentation of the certificate representing the Undelivered Bond. Series 2003 Bonds presented on or before 12:00 Noon on any Business Day are to be paid on or before the close of business on that day.

Prior Owners of Series 2003 Bonds purchased or deemed purchased pursuant hereto shall not be entitled to interest thereon which accrues on and after the related purchase date, provided moneys are on hand in the subaccount established therefor to pay the purchase price and any unpaid interest due on the purchase date.

Changes in Auction Periods or Auction Date

- (a) Changes in Auction Period or Periods:
 - (i) While any of the Series 2003 Bonds are outstanding as Auction Rate Bonds, the Market Agent:
 - (A) in order to conform with then-current market practice with respect to similar securities, shall; or
 - (B) in order to accommodate economic and financial factors that may affect or be relevant to the length of the Auction Period and the interest rate borne by the Auction Rate Bonds and upon receipt of a Favorable Opinion and with the written consent of the City and County,

may change, from time to time, the length of one or more Auction Periods (an “Auction Period Adjustment”). The City and County shall not consent to such change in the length of the Auction Period, if such consent is required above, unless the City and County 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. The Market Agent shall initiate the Auction Period Adjustment by giving written notice to the Paying Agent, the Auction Agent, the City and County and the Depository at least 10 days prior to the Auction Date for such Auction Period.

- (ii) Any such changed Auction Period shall not be less than 7 days.
- (iii) The Auction Period Adjustment shall not be allowed unless Sufficient Clearing Bids existed at both the Auction before the date on which the notice of the proposed change was given as provided herein and the Auction immediately preceding the proposed change.

(iv) The Auction Period Adjustment shall take effect only if (A) the Paying Agent and the Auction Agent receive, by 11:00 a.m. on the Business Day before the Auction Date for the first such Auction Period, a certificate from the Market Agent, authorizing the Auction Period Adjustment specified in such certificate and (B) Sufficient Clearing Bids exist at the Auction on the Auction Date for such first Auction Period. If the condition referred to in (A) above is not met but the condition referred to in (B) is met, the Applicable Auction Rate Bonds Rate for the next Auction Period shall be determined pursuant to the Auction Procedures and the Auction Period shall be the Auction Period determined without reference to the proposed change. If the condition referred to in (A) is met but the condition referred to in (B) above is not met, the Applicable Auction Rate Bonds Rate for the next Auction Period shall be the Maximum Rate and the Auction Period shall be the Auction Period determined without reference to the proposed change. In connection with any Auction Period Adjustment, the Auction Agent shall provide such further notice to such parties as is specified in the Auction Agent Agreement.

(b) Changes in the Auction Date: While any of the Series 2003 Bonds are outstanding as Auction Rate Bonds, 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 Auction Rate Bonds and with the written consent of the City and County,

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" herein with respect to one or more specified Auction Periods. The City and County shall not consent to such change in the Auction Date, if such consent is required in subparagraph (b)(ii) above, unless the City and County 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 with a certificate demonstrating the need for change in reliance on such factors. 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 Paying Agent, the Auction Agent, the City and County and the Depository.

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

Notices

(a) 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 Auction Rate Bonds is maintained in book-entry form by the Depository, the Auction Agent with notice of any change in the Statutory Corporate Tax Rate.

(b) The City and County shall provide the Paying Agent and, so long as no Payment Default has occurred and is continuing and the ownership of the Auction Rate Bonds is maintained in book-entry form by the Depository, the Auction Agent with notice of any change in the Maximum Interest Rate.

(c) If any Auction Rate Bonds are to be redeemed and those Auction Rate Bonds are held by DTC, the Paying Agent shall include in the notice of the call for redemption delivered to DTC (i) under an item entitled "Publication Date for DTC Purposes" three Business Days after the Auction Date next preceding such Redemption Date and (ii) an instruction to DTC to (1) determine on such Publication Date after the Auction held on the immediately preceding Auction Date has settled, the DTC Participants whose DTC positions will be redeemed and the principal amount of such Auction Rate Bonds to be redeemed from each such position (the "DTC Redemption Information"), and (2) notify the Auction Agent immediately after such determination of the positions of the DTC Participants in such Auction Rate Bonds immediately prior to such Auction settlement, the position of the DTC Participants in such Auction Rate Bonds immediately follow such Auction settlement, and the DTC Redemption Information. Publication Date means three Business Days after the Auction Date preceding such Redemption Date.

Notice of Payment Default

(a) If the Paying Agent determines that a Payment Default has occurred the Paying Agent shall promptly notify the City and County thereof.

(b) So long as the ownership of the Auction Rate Bonds is maintained in book-entry form by the Depository, upon the occurrence of a Payment Default the Paying Agent shall immediately send a notice thereof to the Auction Agent, the Broker-Dealer and the Market Agent by telecopy or similar means.

(c) So long as the ownership of the Auction Rate Bonds is maintained in book-entry form by the Depository, the Paying Agent shall immediately send notice to the Auction Agent and the Broker-Dealer by telecopy or similar means if a Payment Default is cured.

Appendix C

Summary of Certain Provisions of the Bond Resolution

The Bond Resolution contains terms and conditions relating to the issuance of Bonds, including various covenants and security provisions, certain of which are summarized below. This summary does not purport to be comprehensive or definitive and is subject to all of the provisions of the Bond Resolution, to which reference is hereby made. Copies of the Bond Resolution are available from the City and County.

Certain Definitions

Certain definitions contained in the Bond Resolution are summarized below. This summary does not purport to be comprehensive or definitive, and is subject to all provisions of the Bond Resolution, to which reference is hereby made. Copies of the Bond Resolution are available from the Department of Budget and Fiscal Services or the Department of Environmental Services of the City and County.

“Accrued Debt Service” means as of any date of computation and with respect to the Bonds of any Series, an amount equal to the sum of: (i) interest on such Bonds accrued and unpaid and to accrue to the end of the then current calendar month, and (ii) principal, Sinking Fund Installment and redemption premium which are due and unpaid for such Bonds and that portion of the principal, unsatisfied balance of any Sinking Fund Installment (as determined in accordance with the Bond Resolution) and redemption premium for such Bonds next due which would have accrued to the end of such calendar month if deemed to accrue monthly from a date one year prior to its due date.

“Act” means Chapter 49, Hawaii Revised Statutes, and all laws amendatory or supplemental thereto.

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

“Assumed Long-Term Fixed Rate” means, with respect to Variable Rate Bonds, (i) a numerical rate of interest that such Bonds would have borne if issued as Fixed Rate Bonds with the same maturity and taking into account Sinking Fund Installments; or (ii) if the City and County has in connection with such Variable Rate Bonds entered into an Interest Rate Exchange Agreement which provides that the City and County is to pay to another person an amount determined based upon a fixed rate of interest on a notional amount and which requires the Counterparty to pay to the City and County an amount equal to the amount by which interest on the notional amount stated therein at the rate borne by such Variable Rate Bonds exceeds the interest payable on such notional amount at a rate stated therein, the fixed rate or other rate of interest set forth in or determined in accordance with such agreement. With respect to the Bonds described in clause (i) of the preceding sentence, an Authorized Officer is to certify or cause the Remarketing Agent for such Series of Variable Rate Bonds or other qualified person to certify such Assumed Long-Term Fixed Rate on the issue date of such Bonds, taking into account such market factors as such Authorized Officer or such Remarketing Agent or such qualified person deems necessary or appropriate.

“Authorized Officer” means the Director of Budget and Fiscal Services, any Deputy Director of Budget and Fiscal Services, the Director of Environmental Services or any other officer of the City and County designated by resolution of the City Council.

“Bond Anticipation Notes” means bond anticipation notes which the City and County may issue for purposes of the Wastewater System if the requirements set forth in the Bond Resolution for such issuance are satisfied.

“Bond Counsel” means an attorney or a firm of attorneys of nationally recognized standing in the field of law relating to municipal bonds selected by the City and County.

“Bondholder” or *“holder of a Bond”* or *“Holder”* means the registered owner of any Bond which at the time is registered other than to bearer, or such holders’ duly authorized attorney in fact, representative or assigns.

“Capital Appreciation Bond” means any Bond as to which interest is compounded on each Valuation Date therefor and is payable only at the maturity or prior redemption thereof.

“City Charter” means the 1973 Revised Charter of the City and County of Honolulu (1994 Edition), as the same may be amended from time to time.

“City Code” means the Revised Ordinances of Honolulu 1990, as the same may be amended from time to time.

“City Council” mean the City Council of the City and County.

“Code” means the Internal Revenue Code of 1986, as amended, and any successor statutes thereto, and any applicable regulations thereunder.

“Common Reserve Subaccount Requirement” means as of any date of computation, an amount equal to the greatest amount of Aggregate Debt Service for the then current or any future Fiscal Year on all Outstanding Bonds entitled to the benefit of the Common Reserve Subaccount; provided however, that if upon issuance of a Series of Bonds entitled to the benefit of the Common Reserve Subaccount, such amount would require moneys to be credited to the Common Reserve Subaccount from such Bond proceeds in an amount in excess of the maximum amount permitted under the Code, the Common Reserve Subaccount Requirement will mean an amount equal to the sum of the Common Reserve Subaccount Requirement immediately preceding issuance of such Bonds and the maximum amount permitted under the Code to be deposited therein from the proceeds of such Bonds, as certified by an Authorized Officer; provided further, however, that for purposes of this definition, Aggregate Debt Service is to be computed with respect to each Variable Rate Bond entitled to the benefit of the Common Reserve Subaccount by using the Assumed Long-Term Fixed Rate applicable thereto.

“Consulting Engineer” means the engineer or engineering firm or corporation retained from time to time pursuant to the Bond Resolution to perform the acts and carry out the duties provided for such Consulting Engineer in the Bond Resolution.

“Costs” means all costs of any Improvement and include, but are not be limited to, all costs and estimated costs of the issuance of the Bonds, all architectural, engineering, inspection, financial and legal expenses, the cost of causing the payment of the principal or interest or both of the Bonds to be insured or guaranteed, the initial cost of any Support Facility or Interest Rate Exchange Agreement obtained or permitted by the Act, and interest which it is estimated will accrue during the construction of any Improvements and for six (6) months thereafter.

“Debt Service” means, as of any particular date of computation, with respect to any Bonds and with respect to any period, the aggregate of the amounts to be paid or set aside in such period for the payment (or retirement) of the principal and Redemption Price (if any) of, and interest on, such Bonds; provided, however, that the term “Debt Service” does not include interest on Bonds to the extent it is to be paid from amounts on credit to a Series Improvement Interest Subaccount, amounts on credit to the Debt Service Subaccount or any other provisions made for the payment of interest.

“Department” means the Department of Environmental Services of the City and County as established by the City Charter, or the successor thereto.

“Depositary” means any bank, national banking association or trust company selected and appointed by an Authorized Officer in accordance with the Bond Resolution as a depositary of moneys and Investment Securities held under the provisions of the Bond Resolution.

“Depository” means The Depository Trust Company, New York, New York, or its nominee, or any other person, firm, association or corporation designated in the Series Resolution authorizing a Series of Bonds or a Series Certificate relating to such Series of Bonds to serve as securities depository for the Bonds of such Series.

“Director of Budget and Fiscal Services” means the Director of Budget and Fiscal Services of the City and County appointed pursuant to and having the powers as set forth in the Act and the City Charter, or any successor.

“*Director of Environmental Services*” means the Director of the Department of Environmental Services of the City and County appointed pursuant to and having the powers as set forth in the Act and the City Charter, or any successor.

“*Exempt Obligation*” means an obligation of any state or territory of the United States of America, any political subdivision of any state or territory of the United States of America, or any agency, authority, public benefit corporation or instrumentality of such state, territory or political subdivision, the interest on which is excludable from gross income under Section 103 of the Code, and which at the time an investment therein is made or such obligation is deposited in any fund or account under the Bond Resolution, is rated, without regard to qualification of such rating by symbols such as “+” or “-” or numerical notation, “Aa” or better by Moody’s and “AA” or better by S&P, or, if such obligation is not rated by Moody’s or S&P, or, if such obligation is rated by neither Moody’s nor S&P, has been assigned a comparable rating by another nationally recognized rating service, but in no event rated lower than the lowest rating on Outstanding Bonds assigned by Moody’s or S&P.

“*First Resolution Obligations*” means bonds, notes and other evidence of indebtedness issued under and pursuant to the First Bond Resolution.

“*Fiscal Year*” means the 12 month period established by the City and County or provided by law from time to time as its fiscal year, and which, as of the date of adoption of the Bond Resolution, is the 12-month period commencing on July 1 of any year and ending on June 30 of the following year.

“*Government Obligation*” means a direct obligation of the United States of America, an obligation the principal of, and interest on, which are guaranteed by the United States of America, provided, that the full faith and credit of the United States of America is pledged to any such direct obligation or guarantee.

“*Improvements*” means the acquisition, purchase, construction, reconstruction, improvement, betterment or extension of the Wastewater System.

“*Interest Rate Exchange Agreement*” means an agreement entered into by the City and County relating to Bonds of one or more Series which provides that during the term of such agreement the City and County is to pay to the Counterparty an amount based on the interest accruing at a fixed or variable rate per annum on a notional amount and that the Counterparty is to pay to the City and County either (i) an amount based on the interest accruing on such notional amount at a fixed, capped or variable rate per annum, in each case computed according to a formula set forth in such agreement, or that one will pay to the other any net amount due under such agreement, or (ii) an amount based on the amount by which the rate per annum at which such Bonds bear interest exceeds a rate per annum stated in such agreement.

“*Investment Agreement*” means an agreement for the investment of moneys with a Qualified Financial Institution.

“*Investment Securities*” means any of the following, if and to the extent that the same are legal for the investment of funds of the Department:

- (i) Government Obligations;
- (ii) Investment Agreements;
- (iii) Direct obligations and fully guaranteed certificates of beneficial interest of the Export-Import Bank of the United States; consolidated debt obligations and letter of credit-backed issues of the Federal Home Loan Banks; participation certificates and senior debt obligations of the Federal Home Loan Mortgage Corporation (“FHLMCs”); debentures of the Federal Housing Administration; mortgage-backed securities (except stripped mortgage securities which are valued greater than par on the portion of unpaid principal) and senior debt obligations of Fannie Mae (“FNMA’s”); participation certificates of the General Services Administration; guaranteed mortgage-backed securities and guaranteed participation certificates of the Government National Mortgage Association (“GNMA’s”); guaranteed participation certificates and guaranteed pool certificates of the Small Business Administration; debt obligations and letter of credit-backed

issues of the Student Loan Marketing Association; local authority bonds of the U.S. Department of Housing & Urban Development; guaranteed Title XI financings of the U.S. Maritime Administration; guaranteed transit bonds of the Washington Metropolitan Area Transit Authority; Resolution Funding Corporation securities.

(iv) direct obligations of any state or territory of the United States of America or any subdivision or agency thereof whose unsecured, uninsured and unguaranteed general obligation debt is rated, at the time of purchase, "Aa" or better by Moody's and "AA" or better by S&P, or any obligation fully and unconditionally guaranteed by any state, subdivision or agency whose unsecured, uninsured and unguaranteed general obligation debt is rated, at the time of purchase, "Aa" or better by Moody's and "AA" or better by S&P;

(v) commercial paper (having original maturities of not more than 270 days) rated, at the time of purchase, "P-1" by Moody's and "A-1" or better by S&P;

(vi) Federal funds, unsecured certificates of deposit, time deposits or bankers acceptances (in each case having maturities of not more than 365 days) of any domestic bank including a branch office of a foreign bank which branch office is located in the United States, provided legal opinions are received to the effect that full and timely payment of such deposit or similar obligation is enforceable against the principal office or any branch of such bank, which, at the time of purchase, has a short-term "Bank Deposit" rating of "P-1" by Moody's and a "Short-Term CD" rating of "A-1" or better by S&P.

(vii) deposits of any bank or savings and loan association which has combined capital, surplus and undivided profits of not less than \$3 million, provided such deposits are continuously and fully insured by the Bank Insurance Fund or the Savings Association Insurance Fund of the Federal Deposit Insurance Corporation ("FDIC");

(viii) investments in money-market funds rated "Aaa" by Moody's, and "AAAm" or "AAAm-G" by S&P;

(ix) repurchase agreements collateralized by Government Obligations, GNMMAs, FNMMAs or FHLMMCs with any registered broker/dealer subject to the Securities Investors' Protection Corporation jurisdiction or any commercial bank insured by the FDIC, if such broker/dealer or bank has an uninsured, unsecured and unguaranteed obligation rated in the top two rating tiers by Moody's, and "AA-1" or "AA-" or better by S&P, provided:

(a) a master repurchase agreement or specific written repurchase agreement governs the transaction; and

(b) the securities are held free and clear of any lien by the Depository or an independent third party acting solely as agent ("Agent") for the Depository, and such third party is (i) a Federal Reserve Bank, or (ii) a bank which is a member of the Federal Deposit Insurance Corporation and which has combined capital, surplus and undivided profits of not less than \$50 million, and the Depository has received written confirmation from such third party that it holds such securities, free and clear of any lien, as agent for the Depository; and

(c) a perfected first security interest under the Uniform Commercial Code, or book entry procedures prescribed at 31 C.F.R. 306.1 et seq. or 31 C.F.R. 350.0 et seq. in such securities is created for the benefit of the Depository; and

(d) the repurchase agreement has a term of 3 years or less, and the Depository or the Agent will value the collateral securities no less frequently than weekly and will liquidate

the collateral securities if any deficiency in the required collateral percentage is not restored within two business days of such valuation; and

(e) the fair market value of the securities in relation to the amount of the repurchase obligation, including principal and interest, is equal to at least 100%;

(x) investments in any mutual fund whose portfolio is limited to Government Obligations and the investments described in clause (ii) of Investment Securities; and

(xi) student loan resource securities including student loan auction rate securities, student loan asset-backed notes, student loan program revenue notes and bonds, and securities issued pursuant to Rule 144A of the Securities Act of 1933, including any private placement issues, issued with either bond insurance or overcollateralization guaranteed by the United States Department of Education, provided all insurers maintain an "Aaa" by Moody's, "AAA" by S&P or equivalent rating by other rating agencies.

"*Moody's*" means Moody's Investors Service, Inc., its successors and their assigns, and, if such corporation for any reason no longer performs the functions of a securities rating agency, "Moody's" is deemed to refer to any other nationally recognized rating agency, if any, designated by the Director of Budget and Fiscal Services.

"*Net Revenue Requirement*" means, with respect to any Fiscal Year or any period, an amount equal to the greater of: (i) the sum of (a) the Aggregate Debt Service under the First Bond Resolution and the Aggregate Debt Service in such Fiscal Year or such period, and (b) the Required Deposits for such Fiscal Year or such period; or (ii) 1.10 times the Aggregate Debt Service (as defined in the First Bond Resolution) under the First Bond Resolution and 1.10 times the Aggregate Debt Service in such Fiscal Year or such period, plus 1.00 times the aggregate Support Facility Reimbursement Obligations outstanding as of the end of such Fiscal Year or such period.

"*Net Revenues*" means, with respect to any period, the Revenues during such period less amounts required to pay Operation and Maintenance Expenses.

"*Operation and Maintenance Expenses*" means the costs and expenses of operating and maintaining the Wastewater System, including, without limiting the generality of the foregoing, (i) all expenses includable in the operation and maintenance expense accounts of the Department relating to the Wastewater System according to generally accepted accounting principles, exclusive of depreciation and amortization of property values or losses, (ii) to the extent not included in the preceding clause (i) or paid from Bond proceeds or otherwise, the Department's share of the costs and expenses of operating and maintaining any plants and properties jointly owned with others, and (iii) the amounts, if any, payable to the United States Treasury Department pursuant to Section 148 of the Code.

"*Opinion of Counsel*" means with respect to the City and County a written opinion of counsel selected by the Director of Budget and Fiscal Services who is not an employee of the City and County, and which, with respect to Federal income tax law and securities law relating to obligations issued by state and local governmental units, is Bond Counsel. Any Opinion of Counsel may be based (insofar as it relates to factual matters or information which is in the possession of the City and County) upon a written certificate of the City and County unless such counsel knows, or in the exercise of reasonable care should have known, that such written certificate is erroneous.

"*Outstanding*" or "*outstanding*" when used with reference to Bonds means, as of any date, Bonds theretofore or thereupon issued pursuant to the Bond Resolution, except: (a) any Bonds canceled by a Paying Agent or paid at or prior to such date; (b) Bonds in lieu of or in substitution for which other Bonds have been delivered pursuant to the Bond Resolution; (c) Bonds deemed to be no longer outstanding under the Bond Resolution as provided in the Bond Resolution and (d) Option Bonds tendered or deemed tendered in accordance with the provisions of the Series Resolution or the Series Certificate relating to such Bonds.

"*Parity Support Facility Reimbursement Obligation*" means the obligation of the City and County described in the Bond Resolution to directly reimburse the Support Facility Provider of any Support Facility for amounts paid by such Support Facility Provider under such Support Facility or a Counterparty under an Interest Rate

Exchange Agreement for amounts paid thereunder, on a parity with the obligation of the City and County to pay the Bonds, whether or not such obligation to reimburse is evidenced by a promissory note or other similar instrument.

“*Paying Agent*” means, as to Bonds of any particular Series, the Director of Budget and Fiscal Services or the bank or trust company designated for the payment of the principal and Redemption Price, if any of, and interest on, the Bonds of such Series in the Series Resolution authorizing the issuance of such Series or the Series Certificate relating to such Series.

“*Record Date*” means, with respect to any Series of Bonds, (i) with respect to the payment of interest, the 15th day (whether or not a Business Day) of the month preceding an interest payment date; (ii) with respect to notice of redemption, the 45th day (whether or not a Business Day) preceding the date of redemption; or (iii) such other day as may be provided in the Series Resolution authorizing the issuance of such Series or the Series Certificate relating to such Series.

“*Refunded Municipal Obligations*” means Exempt Obligations which are rated in the highest rating category by Moody’s and S&P and provision for the payment of the principal of and interest on which has been made by an irrevocable deposit with a trustee or escrow agent of Governmental Obligations, which are held by a bank or trust company organized and existing under the laws of the United States of America or any state, the District of Columbia or possession thereof in the capacity as custodian, the maturing principal of and interest on which Government Obligations will be sufficient to pay, when due, the principal of and interest on such Exempt Obligations.

“*Reimbursable Obligations*” means reimbursable general obligation bonds issued and delivered or to be issued and delivered by the City and County to finance certain costs related to the Wastewater System, the debt service on which the Department is required by State law to reimburse the City and County’s General Fund.

“*Reimbursable Obligation Requirement*” means, with respect to any period of time, the amount required to be credited to the Reimbursable Obligation Account pursuant to the ordinances and resolutions of the City Council authorizing the issuance and delivery of Reimbursable Obligations.

“*Required Deposits*” means, for any period, (i) the Required Deposits under the First Bond Resolution exclusive of transfers from the Sewer Fund to the Subordinate Obligation Account; and (ii) the amounts, if any, required: (a) to be paid into the Rebate Subaccount, the Common Reserve Subaccount, each Separate Series Reserve Subaccount, and the Third Lien Obligation Subaccount, and (b) to pay Support Facility Reimbursement Obligations.

“*Required Deposits under the First Bond Resolution*” means, for any period, amounts required, if any, to be paid into the Common Reserve Subaccount, each Separate Reserve Subaccount, the Third Lien Obligation Account and Reimbursable Obligation Account under the First Bond Resolution; and to pay Support Facility Reimbursement Obligations under the First Bond Resolution.

“*Revenue Bond Index*” means the 30 year Revenue Bond Index of *The Bond Buyer*, a publication in New York, New York, or any successor publication maintaining such Index or in the event *The Bond Buyer* or any successor publication does not maintain such Index, an equivalent index with the same or similar components as the Revenue Bond Index.

“*Revenues*” means (i) the Revenues under the First Bond Resolution; (ii) all income from investments of moneys held under the Resolution including investment income on the Improvement Second Account created by the Resolution but not including any earnings on the Rebate Subaccount or Third Lien Obligation Subaccount; and (iii) all payments made by Counterparties pursuant to Interest Rate Exchange Agreements.

“*Revenues under the First Bond Resolution*” means the moneys, including any moneys collected from the City and County or any department thereof other than the Department, derived by the Department from the rates, rentals, fees and charges prescribed for the use and services of, and the facilities and commodities furnished by, the Wastewater System, including, without limiting the generality of the foregoing, (i) all income, receipts, profits, and other moneys derived from the furnishing or supplying of the services, facilities and commodities through the Wastewater System; (ii) all income from investments of moneys held under the First Bond Resolution including investment income on the Improvement Second Account but not including any earnings on the Rebate Account, the

Subordinate Obligation Account or the Reimbursable Obligation Account; (iii) all payments made by Counterparties pursuant to Interest Rate Exchange Agreements; and (iv) moneys and Investment Securities transferred from the Rate Stabilization Account to the Sewer Fund within 90 days following the end of a Fiscal Year. “*Revenues under the First Bond Resolution*” will not include, (i) deposits subject to refund until such deposits have become the property of the City and County; (ii) contributions in-aid-of construction and assessment, impact and other similar fees imposed and collected by the City and County which are targeted to pay the Costs of specific Improvements; (iii) income, fees, charges, receipts, profits or other moneys derived by the Department from the ownership or operation of any separate utility system; (iv) any gifts, grants, donations or other moneys received by the City and County for purposes of the Wastewater System from any State or Federal agency or other person if such gifts, grants, donations or other moneys are the subject of any limitation or reservation: (a) imposed by the donor or grantor; or (b) imposed by law or administrative regulation to which the donor or grantor is subject, limiting the application of such funds; (v) amounts retained in the Sewer Fund for working capital and operating reserves pursuant to the First Bond Resolution; (vi) moneys and Investment Securities transferred from the Sewer Fund to the Rate Stabilization Account within 90 days following the end of a Fiscal Year; or (vii) Wastewater System Facility Charges.

“*S&P*” means Standard & Poor’s Ratings Group, a division of The McGraw-Hill and Companies, Inc., its successors and their assigns, and, if such corporation for any reason no longer performs the functions of a securities rating agency, S&P is deemed to refer to any other nationally recognized rating agency designated by the Director of Budget and Fiscal Services.

“*Serial Bonds*” means Bonds which mature serially and which are not Term Bonds.

“*Series,*” “*Series of Bonds*” or “*Bonds of a Series*” means all Bonds designated as being of the same series issued and delivered on original issuance in a simultaneous transaction, and any Bonds thereafter delivered in lieu thereof or in substitution therefor pursuant to the Bond Resolution.

“*Sinking Fund Installment*” means an amount so designated which is established pursuant to the Bond Resolution. The portion of any such Sinking Fund Installment remaining after the deduction of any such amounts credited pursuant to the Bond Resolution toward the same (or the original amount of any such Sinking Fund Installment if no such amounts have been credited toward the same) will constitute the unsatisfied balance of such Sinking Fund Installment for the purpose of calculation of Sinking Fund Installments due on a future date.

“*Subordinate Obligations*” means the Bonds and any other bonds, notes or other evidences of indebtedness issued in compliance with the provisions of the First Bond Resolution as obligations subordinate to the First Resolution Obligations, other than Reimbursable Obligations.

“*Subordinate Obligation Requirement*” means with respect to any period of time, the amount required to be deposited in the Subordinate Obligation Account pursuant to the First Bond Resolution, indenture or other instruments of the City and County adopted by or entered into by the City and County in accordance with the Bond Resolution and providing for all payments with respect to Subordinate Obligations.

“*Supplemental Resolution*” means any resolution adopted by the City Council and becoming effective pursuant to and in compliance with the provisions of the Bond Resolution which amends or supplements the provisions of the Bond Resolution, any Series Resolution or any other Supplemental Resolution.

“*Support Facility*” means an irrevocable letter of credit, surety bond, loan agreement, standby purchase agreement or other agreement, facility or insurance or guaranty arrangement issued or extended by one or more Support Facility Providers, pursuant to which the City and County is entitled to obtain moneys to pay the principal or Redemption Price of Bonds due in accordance with their terms or tendered for purchase or redemption, plus accrued interest thereon to the date of payment, purchase or redemption thereof in accordance with the Bond Resolution and with the Series Resolution authorizing such Bonds or a Series Certificate relating to such Bonds, whether or not the City and County is in default.

“*Support Facility Provider*” means a bank, a trust company, a national banking association, an organization subject to registration with the Board of Governors of the Federal Reserve System under the Bank Holding Company Act of 1956 or any successor provisions of law, a federal branch pursuant to the International

Banking Act of 1978 or any successor provisions of law, a savings bank, a savings and loan association, an insurance company or association chartered or organized under the laws of any state of the United States of America, the Government National Mortgage Association or any successor thereto, the Federal National Mortgage Association or any successor thereto, or any other federal agency or instrumentality approved by the City and County or a Counterparty.

“Support Facility Reimbursement Obligation” means the obligation of the City and County described in the Bond Resolution to directly reimburse the Support Facility Provider of a Support Facility for amounts paid thereunder or a Counterparty under an Interest Rate Exchange Agreement for amounts paid thereunder, whether or not such obligation to reimburse is evidenced by a promissory note or other similar instrument.

“Tax-exempt Bonds” means Bonds the interest on which is intended by the City and County to be excluded from gross income of the holders of such Bonds for federal income taxation purposes pursuant to the Code.

“Term Bonds” means Bonds the retirement or the redemption of which is to be provided for from moneys credited to the Debt Service Subaccount pursuant to the Bond Resolution.

“Third Lien Obligations” means any bonds, notes or other evidences of indebtedness of the City and County payable from the Revenues, other than the First Resolution Obligations, the Bonds and the Reimbursable Obligations, issued in accordance with and complying with the provisions of the Bond Resolution.

“Variable Rate Bonds” means any Bonds issued bearing interest at a rate per annum subject to adjustment from time to time based on the terms thereof, based upon an index, or otherwise calculated in a manner which precludes the actual rate for the entire term of such Bonds from being ascertainable in advance as provided for in the Bond Resolution.

“Wastewater System” means all plants and properties, both real and personal and tangible and intangible, now or hereafter existing, under the management, control or jurisdiction of the Department, used for, useful in, or pertaining to the collection, pretreatment, advanced primary treatment, primary treatment, secondary treatment, tertiary treatment, purification, conveyance, storage, drainage, discharge and disposal of sewage, water, wastewater, stormwater, influent, effluent, or other liquids or suspended solids, or incidental or necessary to the preservation of the City and County’s or the Department’s wastewater conveyance facilities, wastewater treatment plants, wastewater disposal facilities, storm drains and sewers, sewage pump stations, sewage treatment plants, sewers, interceptors, outfall and other related facilities and plants, and the integrity thereof. The terms used in the preceding sentence have the meanings as ascribed to them in the City Code. Without limiting the generality of the foregoing, the Wastewater System includes: (1) the existing plants and properties comprising the Wastewater System under the management, control or jurisdiction of the Department, as of the date of adoption of the Bond Resolution; and (2) all Improvements thereafter constructed or otherwise acquired, purchased or annexed.

“Wastewater System Facility Charge” has the meaning specified in the City Code.

Pledge Made in the Bond Resolution

The Bonds are payable solely from and secured by the funds pledged therefor under the Bond Resolution. The City and County has pledged as security for the payment of the principal of, Redemption Price, if any, and interest on the Bonds in accordance with their terms and the provisions of the Bond Resolution, subject only to the provisions of the Bond Resolution permitting the application thereof for the purposes and on the terms and conditions set forth in the Bond Resolution: (i) the proceeds of sale of the Bonds pending application thereof in accordance with the provisions of the Bond Resolution or of a Series Resolution or a Series Certificate; (ii) the Net Revenues; and (iii) the Subordinate Obligation Account but excluding all Subaccounts therein unless specifically pledged by the Bond Resolution, a Series Resolution or a Series Certificate, (iv) the Debt Service Subaccount, (v) with respect to any Series of Bonds entitled to the benefit of a Separate Series Reserve Subaccount, such Separate Series Reserve Subaccount, and (vi) with respect to any Series of Bonds entitled to the benefit of the Common Reserve Subaccount, the Common Reserve Subaccount, including the investments, if any, in such Account and Subaccounts; and the Bondholders shall have to the extent permitted by law, a lien on, and a security interest in, such proceeds, Net Revenues, and Subaccounts for such purpose and subject to such provisions of the Resolution.

The Rebate Subaccount and the Third Lien Subaccount are not pledged to the payment of the principal and redemption price (if any) of, and interest on, the Bonds.

So long as First Resolution Obligations are outstanding for purposes of the First Bond Resolution, the pledge of the Net Revenues made by the Bond Resolution is subordinate and junior in all respects to the pledge of the Net Revenues made by the First Bond Resolution. The pledge of the Net Revenues made by the Bond Resolution is also prior and superior to the pledge which may be made by any resolution, indenture or other instrument authorizing and securing Third Lien Obligations and Reimbursable Obligations. On and after such date, if any, that First Resolution Obligations are no longer outstanding for purposes of the First Bond Resolution, the pledge of the Net Revenues made by the Bond Resolution will be prior and superior in all respects to any pledge of the Net Revenues made by any resolution, indenture or other instruments, including the pledge which may be made by any resolution, indenture or other instrument authorizing and securing Third Lien Obligations and Reimbursable Obligations. There will be additionally pledged on and after such date as security for the payment of the principal and Redemption Price (if any) of, and interest on, the Bonds in accordance with their terms and the provisions of the Bond Resolution, subject only to the provisions of the Bond Resolution permitting the application thereof for the purposes and on the terms and conditions set forth in the Bond Resolution, (i) the Sewer Fund but excluding all Accounts and Subaccounts therein unless specifically pledged by the Bond Resolution, a Series Resolution or a Series Certificate, (ii) the Renewal and Replacement Account, (iii) the Rate Stabilization Account and (iv) the Wastewater General Account.

The Bond Resolution provides that each of the obligations, duties, limitations and restraints imposed upon the City and County by the Bond Resolution is deemed to be a covenant between the City and County and every Holder of the Bonds, and the Bond Resolution and every provision and covenant set forth in the Bond Resolution is deemed to be and constitute a continuing contract and agreement between the City and County and the Holders from time to time of the Bonds issued under the Bond Resolution, to secure the full and final payment of the principal and redemption price of and interest on all Bonds which may from time to time be issued, executed, and delivered under the Bond Resolution. The covenants and agreements set forth in the Bond Resolution to be performed by the City and County are for the equal and proportionate benefit, security and protection of all Holders of the Bonds without preference, priority or distinction as to payment or security or otherwise of any of the Bonds over any of the others for any reason or cause whatsoever except as expressly provided in the Bond Resolution, in a Series Resolution, a Series Certificate or a Supplemental Resolution, or in the Bonds.

Additional Bonds

Basic Test. One or more Series of Bonds (exclusive of Refunding Bonds) may be issued at any time and from time to time for any lawful use or purpose relating to the Wastewater System, including, without limitation, payment of all or a portion of the Costs of Improvements, but only upon compliance as to each such Series with the provisions set forth in the Bond Resolution, including, among other things, delivery to the Director of Budget and Fiscal Services of the following documents or moneys or securities:

1. A written certificate of the City and County stating the amount required to be in the Common Reserve Subaccount after issuance of the Bonds then to be issued, and that after deposit in the Common Reserve Subaccount of the amount, if any, to be deposited therein in connection with the issuance of such Bonds, the amounts on deposit in the Common Reserve Subaccount will not be less than the Common Reserve Subaccount Requirement.

2. A written certificate of the City and County stating the amount required to be in the Separate Series Reserve Subaccount created, if any, to provide additional security for the Bonds of such Series after issuance of the Bonds then to be issued, and that after deposit in such Separate Series Reserve Subaccount of the amount to be deposited therein in connection with the issuance of such Bonds, the amounts on deposit in such Separate Series Reserve Subaccount will not be less than the Separate Series Reserve Subaccount Requirement for such Separate Series Reserve Subaccount.

3. Either (I) a written certificate of the City and County based: (i) on audited figures or (ii) to the extent audited figures are not available, on figures taken by an independent certified public accountant from the Department's books and records; showing that the Net Revenues for: (a) the most recent Fiscal Year, or (b) any consecutive 12-months' period out of 24 months immediately preceding the

month in which such Bonds are issued were not less than the greater of: (x) the sum of (1) the maximum of the sum of the Aggregate Debt Service on all First Resolution Obligations issued and outstanding under and pursuant to the First Bond Resolution and the Aggregate Debt Service on all Bonds then Outstanding and on the proposed Series of Bonds in any Fiscal Year and the 12-month period selected and (2) the Required Deposits for such Fiscal Year or the 12-month period selected; and (y) the sum of (1) 1.10 times the maximum of the sum of the Aggregate Debt Service on all First Resolution Obligations issued and outstanding under and pursuant to the First Bond Resolution and the Aggregate Debt Service on all Bonds then Outstanding and on the proposed Series of Bonds in any Fiscal Year and the 12-month period selected, and (2) 1.00 times the aggregate Support Facility Reimbursement Obligations outstanding under the First Bond Resolution and the Bond Resolution as of the date of the written certificate of the City and County, or (II) a written certificate of the City and County or Certificate of the Consulting Engineer that the Net Revenues to be derived in each of the five (5) Fiscal Years following the earlier of: (i) the end of the period during which interest is capitalized or, if no interest is to be capitalized, the Fiscal Year in which the proposed Series of Bonds are issued, and (ii) the date on which substantially all Improvements to be financed with the proceeds of the proposed Series of Bonds are expected to commence operations, or, if the proceeds of such Series of Bonds will not be used to fund the Costs of Improvements, the Fiscal Year in which the proposed Series of Bonds are issued, are estimated to be not less than the greater of: (x) the sum of (1) the maximum of the sum of the Aggregate Debt Service on all First Resolution Obligations issued under and pursuant to the First Bond Resolution and the Aggregate Debt Service on all Bonds then Outstanding and on the proposed Series of Bonds in any such Fiscal Year, and (2) the Required Deposits for any such Fiscal Year; and (y) the sum of (1) 1.10 times the maximum of the sum of the Aggregate Debt Service on all First Resolution Obligations issued under and pursuant to the First Bond Resolution and the Aggregate Debt Service on all Bonds then Outstanding and on the proposed Series of Bonds in any such Fiscal Year, and (2) 1.00 times the aggregate Support Facility Reimbursement Obligations outstanding under the First Bond Resolution and the Bond Resolution as of the date of such written certificate of the City and County or certificate of the Consulting Engineer, as the case may be.

Certain Adjustments. The Bond Resolution permits and requires certain adjustments to be made in determining whether the Basic Test described above for the issuance of Bonds other than Refunding Bonds is met.

1. In determining Debt Service on Variable Rate Bonds then Outstanding and Variable Rate Bonds then proposed to be issued for purposes of the Basic Test described above, the interest rate is to be calculated as: (i) if any Variable Rate Bonds are then Outstanding and have been Outstanding for at least 24 months, the highest average interest rate borne by such Variable Rate Bonds for any 30-day period or if no such Variable Rate Bonds are then Outstanding, the Revenue Bond Index at the time of calculation.

2. Bond Anticipation Notes then Outstanding are to be treated as Bonds. In determining Debt Service on such Bond Anticipation Notes, such Bond Anticipation Notes are assumed to mature in 30 years and bear interest equal to the Revenue Bond Index at the time of calculation.

3. Third Lien Obligations and Reimbursable Obligations originally issued with a maturity of five (5) years or less are assumed to mature in 30 years and bear interest equal to the Revenue Bond Index at the time of calculation.

4. In preparing the certificate required by the Basic Test described above, the Authorized Officer or the Consulting Engineer, as applicable, may make adjustments to the Net Revenues as follows:

a. If any changes have been made in the schedule of rates and charges imposed by the City and County for commodities and services furnished by the Wastewater System which are in effect at the time of adoption of the Series Resolution authorizing the issuance of the Bonds then being issued and were placed into effect subsequent to the start of the Fiscal Year or the 12-month period selected pursuant to item 3 of the *Basic Test* described above, the Authorized Officer, may, if such changes result in increases in such rates and charges, and must, if such changes result in reductions in such rates and charges, adjust the Net Revenues for such period to reflect any change in such Net Revenues which would have occurred if the schedule of rates and charges in effect at the time of the adoption of the Series Resolution providing for the issuance of

such Bonds had been in effect during the portion of such period in which such schedule was not in effect.

b. If customers are being served by the Department at the time of adoption of the Series Resolution authorizing the issuance of the Bonds then being issued and who were added to the Wastewater System subsequent to the start of the Fiscal Year or the 12-month period selected pursuant to item 3 of the *Basic Test* described above, the Authorized Officer may adjust the Net Revenues for such period to reflect any change in such Net Revenues which would have occurred if the additional customers had been served during the portion of the period in which such customers were not served.

c. If residential, commercial, industrial or institutional customers which are in existence are not then served by the Wastewater System at the time of adoption of the Series Resolution authorizing the issuance of the Bonds then being issued, but are then expected to be served during the five (5) Fiscal Years covered by such certificate, the Authorized Officer or the Consulting Engineer, as applicable, must estimate the effect which such new customers would have had on the Net Revenues for the period selected pursuant to item 3 of the *Basic Test* described above, if such new customers had been served during the entire period and may adjust the Net Revenues for such period to give effect to such new customers. Any such estimate will be based upon the operating experience and records of the Department with respect to the Wastewater System and upon any available financial and quarterly statistics deemed pertinent by the Authorized Officer or the Consulting Engineer, as applicable.

d. If any long-term, guaranteed contracts with customers of the Wastewater System are in effect at the time of adoption of the Series Resolution authorizing the issuance of the Bonds then being issued and which were entered into subsequent to the start of the Fiscal Year or 12-month period selected pursuant to item 3 of the *Basic Test* described above, the Authorized Officer may adjust the Net Revenues for such period to reflect any change in such Net Revenues which would have occurred if such contracts had been in effect for the entire period.

e. In rendering the certificate required pursuant to item 3 of the Basic Test, the Authorized Officer or the Consulting Engineer, as applicable, must deem the Operation and Maintenance Expenses for the Wastewater System for the first Fiscal Year of the five (5) year period to be equal to such Operation and Maintenance Expenses for the Fiscal Year immediately preceding the Fiscal Year in which the proposed Series of Bonds is to be delivered, and thereafter the Authorized Officer or the Consulting Engineer, as applicable, must adjust, if deemed necessary, for any increased Operation and Maintenance Expenses which are estimated to occur during any subsequent Fiscal Year during the five (5) year period and are, in the judgment of the Authorized Officer or the Consulting Engineer, as applicable, essential to maintaining and operating the Wastewater System.

f. In rendering any certificate pursuant to the Bond Resolution, the Authorized Officer or the Consulting Engineer, as applicable, may rely upon estimates from other sources which the Authorized Officer or the Consulting Engineer, considers reliable, making such adjustments and provisions for contingencies based on similar projects and other considerations as deemed appropriate by such Authorized Officer or the Consulting Engineer.

Refunding Bonds

The City and County may issue a Series of refunding Bonds at any time for the purpose of refunding (including by purchase) all or any portion of Bonds Outstanding, including amounts to pay principal, redemption premium and interest to the date of maturity or redemption (or purchase) and the expense of issuing the refunding Bonds and of effecting such refunding if the conditions set forth in the Bond Resolution are complied with, including all of the conditions of the *Basic Test* described above, except that condition 3 need not be complied with if the maximum annual Debt Service in any Fiscal Year on the refunding Bonds proposed to be issued does not

exceed maximum annual Debt Service in any Fiscal Year on the refunded Bonds by more than 10%. All adjustments described above in *Certain Adjustments* are applicable to the issuance of refunding Bonds.

The City and County may also issue a Series of refunding Bonds at any time for the purpose of refunding (including by purchase) all or any portion of outstanding Third Lien Obligations or Reimbursable Obligations, including amounts to pay principal, redemption premium and interest to the date of maturity or redemption (or purchase) and the expense of issuing the refunding Bonds and of effecting such refunding if the conditions set forth in the Bond Resolution are complied with, including all of the conditions of the *Basic Test* described above.

Bond Anticipation Notes

Bond Anticipation Notes may be issued by the City and County at such time as the City and County shall have by a Series Resolution duly adopted authorized the issuance of Bonds under the Bond Resolution. No Bond Anticipation Notes may be issued unless there has been filed with the Director of Budget and Fiscal Services on or prior to the date of issuance of such Bond Anticipation Notes, a written certificate of the City and County to the effect that, based on market conditions expected to be prevailing at the time of issuance of the Series of Bonds in anticipation of which such Bond Anticipation Notes are issued and on other reasonable assumptions set forth in such written certificate, the provisions of the Bond Resolution for the issuance of additional Bonds other than refunding Bonds are expected to be complied with at the time of issuance of such Series of Bonds. The maximum maturity of any Bond Anticipation Notes, including the renewals thereof, must not exceed five (5) years from the date of the original Bond Anticipation Note. The principal of Bond Anticipation Notes may be paid from the proceeds of such Bond Anticipation Notes (or any renewal thereof) or from the proceeds of the Bonds in anticipation of which such Bond Anticipation Notes were issued. The interest on such Bond Anticipation Notes may be secured by a lien on and pledge of, and be paid from, the Net Revenues on a parity with the lien on and pledge of the Net Revenues created in the Bond Resolution for the payment and security of the Bonds. The principal of Bond Anticipation Notes will be secured by a lien on and pledge of the proceeds of the Bonds in anticipation of which such Bond Anticipation Notes were issued and any such pledge will have priority over any other pledge of such proceeds created by the Bond Resolution. Bond Anticipation Notes issued under the Bond Resolution are to be treated as Bonds for all purposes of the Bond Resolution, and are to be payable from the Debt Service Subaccount, except to the extent that the principal of any such Bond Anticipation Note is paid from the proceeds of other Bond Anticipation Note or from the proceeds of Bonds.

Third Lien Obligations

The City and County may issue Third Lien Obligations which are payable out of, and which may be secured by a pledge of, such amounts in the Third Lien Obligation Subaccount as may from time to time be available for the purpose of payment. The City and County may, by resolution, provide for various priorities in the liens and pledges securing Third Lien Obligations, and nothing in the Bond Resolution shall be construed so as to require that the payment of, or pledges securing, Third Lien Obligations be on a parity *inter se*.

The City and County may also issue Third Lien Obligations: (i) to refund any Third Lien Obligations issued as provided in the Bond Resolution; (ii) to refund Outstanding Bonds; or (iii) to refund any Reimbursable Obligations. Such Third Lien Obligations issued for refunding purposes may be payable out of, and may be secured by a pledge of, such amounts in the Third Lien Obligation Subaccount or Wastewater General Account as may from time to time be available therefor.

The Bond Resolution requires that any resolution, indenture or other instrument securing or evidencing each issue of Third Lien Obligations must contain provisions (which shall be binding on all holders of such Third Lien Obligations) not more favorable to the holders of such Third Lien Obligations than as described below:

(1) In the event of any insolvency or bankruptcy proceedings, and any receivership, liquidation, reorganization or other similar proceedings in connection therewith, relative to the City and County or the Department, or to the property of the City and County or property operated by the Department, and in the event of any proceedings for voluntary liquidation, dissolution or other winding up of the City and County or the Department, the Holders of all Bonds then Outstanding will be entitled to receive payment in full of all principal and interest on all such Bonds before the holders of the Third Lien Obligations are entitled to receive any payment from the trust estate under the Bond Resolution consisting

of the Net Revenues and funds held under the Bond Resolution (the “Trust Estate” for these purposes) on account of principal (and premium, if any) or interest on the Third Lien Obligations.

(2) In the event that any issue of Third Lien Obligations is declared due and payable before its expressed maturity because of the occurrence of an event of default (under circumstances when the provisions of (1) above are not applicable), the Holders of all Bonds Outstanding at the time such Third Lien Obligations so become due and payable because of such occurrence of such an event of default will be entitled to receive payment in full of all principal and interest on all such Bonds before the holders of the Third Lien Obligations are entitled to receive any accelerated payment from the Trust Estate of principal (and premium, if any) or interest on the Third Lien Obligations.

(3) If any Event of Default with respect to the Bonds has occurred and be continuing (under circumstances when the provisions of (1) above are not applicable), the Holders of all Bonds then Outstanding will be entitled to receive payment in full of all principal and interest on all such Bonds before the holders of the Third Lien Obligations are entitled to receive any accelerated payment from the Trust Estate of principal (and premium, if any) or interest on the Third Lien Obligations.

(4) No Bondholder shall be prejudiced in his right to enforce subordination of the Third Lien Obligations by any act or failure to act on the part of the City and County.

(5) The Third Lien Obligations may provide that the provisions of (1), (2), (3) and (4) above are solely for the purpose of defining the relative rights of the Bondholders on the one hand, and the holders of Third Lien Obligations on the other hand, and nothing therein shall impair, as between the City and County and the owners of the Third Lien Obligations, the obligation of the City and County to pay to the owners thereof the principal thereof and premium, if any, and interest thereon in accordance with its terms, nor shall anything therein prevent the holders of the Third Lien Obligations from exercising all remedies otherwise permitted by applicable law or thereunder upon default thereunder, subject to the rights under (1), (2), (3) and (4) above of the Holders of Bonds to receive cash, property or securities otherwise payable or deliverable to the holders of the Third Lien Obligations; and the Third Lien Obligations may provide that, insofar as a trustee or paying agent for such Third Lien Obligations is concerned, the foregoing provisions shall not prevent the application by such trustee or paying agent of any moneys deposited with such trustee or paying agent for the purpose of the payment of or on account of the principal (and premium, if any) and interest on such Third Lien Obligations if such trustee or paying agent did not have knowledge at the time of such application that such payment was prohibited by the foregoing provisions.

Any issue of Third Lien Obligations may have such rank or priority with respect to any other issue of Third Lien Obligations as may be provided in the resolution, indenture or other instrument securing such issue of Third Lien Obligations and may contain such other provisions as are not in conflict with the provisions of the Bond Resolution.

Reimbursable Obligations

The obligation for the payment of Reimbursable Obligations shall be: (i) after and inferior to the lien and security interest for the payment of Bonds and those Third Lien Obligations which are payable from the Third Lien Obligation Subaccount; and (ii) prior and superior to the lien and security interest for the payment of those Third Lien Obligations which are payable from the Wastewater General Account. Reimbursable Obligations are payable from the Reimbursable Obligation Account.

Support Facilities and Interest Rate Exchange Agreements

In connection with the issuance of any Series of Bonds and to the extent permitted by law, the City and County may obtain or cause to be obtained from one or more Support Facility Providers one or more Support Facilities providing for payment of all or a portion of the purchase price or principal, premium, if any, or interest due or to become due on specified Bonds of such Series, or providing for the purchase of such Bonds or a portion of such Bonds by such Support Facility Providers, or providing, in whole or in part, for the funding of the Common Reserve Subaccount or a Separate Series Reserve Subaccount pursuant to the Bond Resolution.

In connection with the issuance of any Series of Bonds or to better manage its assets and liabilities and, to the extent permitted by law, the City and County may enter into with one or more Counterparties one or more Interest Rate Exchange Agreements; *provided* that no such Interest Rate Exchange Agreement shall adversely affect the exclusion from gross income for purposes of federal income taxation of interest on the Tax-exempt Bonds of any Series.

The City and County may enter into agreements with one or more Support Facility Providers or Counterparties to provide for, among other things: (i) the payment of fees and expenses to such Support Facility Providers or Counterparties; (ii) the terms and conditions of such Support Facility or Interest Rate Exchange Agreement and the Series of Bonds affected thereby; and (iii) the security, if any, to be provided to such Support Facility Providers or Counterparties. The City and County may secure the Support Facility or Interest Rate Exchange Agreement by an agreement providing for the purchase of the Bonds secured thereby with such adjustments to the rate of interest, method of determining interest, maturity, or redemption provisions as specified in the Series Resolution or the Series Certificate. Debt Service with respect to any Bonds so secured is to be calculated for purposes of the definition of Common Reserve Subaccount Requirement by using the Assumed Long-Term Fixed Rate.

The City and County may also agree in any agreement with the Support Facility Provider of such Support Facility or the Counterparty under an Interest Rate Exchange Agreement to reimburse directly such Support Facility Provider or Counterparty for any amounts paid under the terms of such Support Facility or Interest Rate Exchange Agreement, together with interest thereon (the "Support Facility Reimbursement Obligation"); *provided, however*, that no Support Facility Reimbursement Obligation is to be created, for purposes of the Bond Resolution, until amounts are paid under such Support Facility or Interest Rate Exchange Agreement, as the case may be. Any such Support Facility Reimbursement Obligation may be secured by a lien on and pledge of the Net Revenues on a parity with the lien on and pledge of the Net Revenues created by the Bond Resolution with respect to the Bonds (a "Parity Support Facility Reimbursement Obligation"). Any such Parity Support Facility Reimbursement Obligation will be deemed to be a part of the Series of Bonds to which the Support Facility which gave rise to such Parity Support Facility Reimbursement Obligation relates. Payment of Support Facility Reimbursement Obligation may be made out of the Sewer Fund as provided in the Bond Resolution.

Any Support Facility deposited in the Common Reserve Subaccount or the long-term debt of the Support Facility Provider of such Support Facility must, in each case, be in the highest rating category each Rating Agency, and if rated by A.M. Best & Company, also be rated in the highest rating category by A.M. Best & Company or its successors. In the event any Support Facility deposited in the Common Reserve Subaccount or the long-term debt of the issuer of any Support Facility deposited in the Common Reserve Subaccount falls below the highest rating category of each Rating Agency, and A.M. Best & Company, if rated by A.M. Best & Company, the City and County must, within 120 days, obtain a new Support Facility which is rated in the highest category of each Rating Agency or for which the long-term debt of the issuer of such new Support Facility is rated in the highest rating category of each Rating Agency and A.M. Best & Company, if rated by A.M. Best & Company; *provided, however*, that if the new Support Facility is not obtained within 120 days, the City and County must deposit in the Common Reserve Subaccount Net Revenues in the amount provided in the Bond Resolution. If a disbursement is made pursuant to a Support Facility deposited in the Common Reserve Subaccount, the City and County must: first, reinstate the full amount of such Support Facility; and second, if necessary deposit Net Revenues in the Common Reserve Subaccount in the amount of the disbursement made under such Support Facility, in either case such that the amount in the Common Reserve Subaccount is equal to the Common Reserve Subaccount Requirement within a period of time not longer than would be required to restore the Common Reserve Subaccount by application of moneys in the Sewer Fund. The City and County may at any time deposit cash or Investment Securities as replacement for one or more Support Facilities.

The City and County must obtain and maintain in effect one or more Support Facilities for Option Bonds. The City and County must obtain a replacement Support Facility to replace any Support Facility for Option Bonds that is expiring, not renewed or terminated. Procedures for such replacement, maintenance and notices to Bondholders, rating agencies or other persons are to be provided in the Series Resolution authorizing the Series of Bonds or the Series Certificate relating to such Bonds.

Funds and Accounts

The City and County has established by ordinances the Sewer Fund and the Sewer Revenue Bond Improvement Fund (the "Improvement Fund"). The First Bond Resolution establishes the following accounts in the Sewer Fund:

Wastewater System Facility Charge Account,
Debt Service Account,
Common Reserve Account,
Rebate Account,
Rate Stabilization Account,
Subordinate Obligation Account,
Reimbursable Obligation Account,
Renewal and Replacement Account, and
Wastewater General Account.

None of the accounts in the Sewer Fund except the Subordinate Obligation Account is pledged as security for the payment of debt service on the Bonds. Such pledge of the Subordinate Obligation Account is subject to the terms and provisions of and the exceptions provided in the First Bond Resolution and the Bond Resolution.

The Bond Resolution establishes the following subaccounts in the Subordinate Obligation Account:

Debt Service Subaccount,
Common Reserve Subaccount,
Rebate Subaccount, and
Third Lien Obligation Subaccount.

The Bond Resolution permits the establishment of one or more Separate Series Reserve Subaccounts in the Subordinate Obligation Account. The Bond Resolution also permits the establishment of one or more Series Improvement Subaccounts in the Improvement Second Account and requires the establishment of one or more Series Improvement Interest Subaccounts in the Improvement Second Account if interest on the Bonds of a Series is to be paid from the proceeds of such Bonds during the period of construction of any Improvements and for six months thereafter.

Sewer Fund

Revenues and Wastewater System Facility Charges are to be collected by the Department and are to be deposited into the Sewer Fund. Under the First Bond Resolution, the Department will, in each month, (i) after making the transfer, if any, to the Wastewater System Facility Charge Account of all moneys received as Wastewater System Facility Charges, (ii) after paying or setting aside a sufficient amount to pay the Operating and Maintenance Expenses, (iii) after making the transfer to the Rebate Account under the First Bond Resolution, (iv) after transferring a sufficient amount to the Debt Service Account under the First Bond Resolution to equal debt service on First Resolution Obligations, (v) after transferring a sufficient amount to the Common Reserve Account and each Separate Series Reserve Account under the First Bond Resolution to eliminate any deficiency therein, and (vi) after maintaining in the Sewer Fund a reasonable and necessary amount for working capital and operating reserves, transfer from the Sewer Fund to the Subordinate Obligation Account a sufficient amount required by the Bond Resolution to pay all accrued and unpaid amounts and amounts to accrue and become payable during the succeeding calendar month which are payable from the Subordinate Obligation Account.

Subordinate Obligation Account

Moneys transferred from the Sewer Fund to the Subordinate Obligation Account are to be applied on the 5th day prior to the end of each month, unless otherwise provided below, in the following order of priority:

- (1) To the Rebate Subaccount such amount as is necessary to pay the rebate amount due the United States Treasury Department under Section 148 of the Code or to set aside as a reserve for such payment;

(2) To the Debt Service Subaccount, if and to the extent required so that the balance in the Debt Service Subaccount shall equal the Accrued Debt Service for all Bonds Outstanding and the interest accrued on all Bond Anticipation Notes outstanding on said date;

(3) (a) To the Common Reserve Subaccount, if and to the extent required either (i) an amount such that the balance in the Common Reserve Subaccount will equal the Common Reserve Subaccount Requirement on said date, or (ii) an amount such that if the same amount were deposited in each month the amount of any deficiency in the Common Reserve Subaccount would be eliminated at the end of the sixth (6th) month following the first credit; and (b) to each Separate Series Reserve Subaccount, if and to the extent required either (i) an amount such that the balance in each Separate Series Reserve Subaccount shall equal the Separate Series Reserve Subaccount Requirement for each Separate Series Reserve Subaccount on said date, or (ii) an amount such that if the same amount were deposited in each month the amount of any deficiency in each Separate Series Common Reserve Subaccount shall be eliminated at the end of the sixth (6th) month following the first credit; provided, however, that such transfers shall be pro rata, based on the proportion of the Common Reserve Subaccount Requirement and each Separate Series Reserve Subaccount Requirement to the sum of the Common Reserve Subaccount Requirement and all Separate Series Reserve Subaccount Requirements;

(4) To the Third Lien Obligation Subaccount, the amount, if any, equal to all Third Lien Obligation Requirements theretofore accrued and unpaid and not met from any other source and to accrue and become payable during the succeeding calendar month and not met from any other source.

The Bond Resolution permits the City and County to pay directly out of the Third Lien Obligation Subaccount reimbursements to providers of Support Facilities whose Support Facilities have been drawn upon in the same priority and order as payments from the Third Lien Obligation Subaccount to the Debt Service Subaccount, the Common Reserve Subaccount, each Separate Series Reserve Subaccount or other Funds, Accounts and Subaccounts as provided in a Series Resolution as if such payments were part of such Funds, Accounts and Subaccounts.

Purposes of the Various Subaccounts in Subordinate Obligation Account

Debt Service Subaccount. The principal and Redemption Price of and interest on the Bonds and interest on Bond Anticipation Notes are to be paid out of the Debt Service Subaccount in the Sewer Fund to each Paying Agent on or before the respective due dates.

Amounts accumulated in the Debt Service Subaccount by reason of the payment of any Sinking Fund Installment may be applied by the City and County, on or prior to the 60th day preceding the due date of such Sinking Fund Installment, to: (i) the purchase of Bonds of the maturity for which such Sinking Fund Installment was established, or (ii) the redemption of such Bonds at the applicable Redemption Price, if then redeemable by their terms. All such purchases of Bonds are to: (i) be made at prices not exceeding the applicable Redemption Price of such Bonds plus accrued interest; (ii) be made as arranged by the City and County in such manner and from such sellers or brokers at such prices as the City and County may determine; and (iii) be made to insure that delivery of the Bonds so purchased will not occur later than the 60th day next preceding the redemption date to which the Sinking Fund Installment is to be applied. The applicable Redemption Price of any Bonds (or principal amount of maturing Bonds) so purchased or redeemed is deemed to constitute part of the Debt Service Subaccount until such Sinking Fund Installment date, for the purpose of calculating the amount of such Subaccount. As soon as practicable after the 60th day preceding the due date of any such Sinking Fund Installment, the City and County must proceed to call for redemption on such due date Bonds of the maturity for which such Sinking Fund Installment was established (except in the case of Bonds maturing on a Sinking Fund Installment date) in such amount as is necessary to complete the retirement of the unsatisfied balance of such Sinking Fund Installment after making allowance for any Bonds purchased or redeemed pursuant to the Bond Resolution which the City and County has applied as a credit against such Sinking Fund Installment as provided in the Bond Resolution.

Upon any purchase or redemption pursuant to the Bond Resolution of Bonds of any Series and maturity for which Sinking Fund Installments shall have been established: (i) if the principal amount of the Bonds so purchased is less than or equal to the next succeeding Sinking Fund Installment for such Series there is to be credited to the next such Sinking Fund Installment an amount equal to the principal amount of the Bonds of such Series so

purchased; and (ii) if the principal amount of the Bonds so purchased is greater than the next succeeding Sinking Fund Installment, there is to be credited toward each such Sinking Fund Installment thereafter to become due an amount bearing the same ratio to such Sinking Fund Installment as the total principal amount of such Bonds so purchased or redeemed bears to the total principal amount of all such Sinking Fund Installments to be so credited or, at the option of the City and County, an amount equal to the next succeeding Sinking Fund Installment. The portion of any such Sinking Fund Installment remaining after the deduction of any such amounts credited toward the same (or the original amount of any such Sinking Fund Installment if no such amounts have been credited toward the same) will constitute the unsatisfied balance of such Sinking Fund Installment for the purpose of calculation of Sinking Fund Installments due on a future date.

The amount, if any, credited to the Debt Service Subaccount from a Series Improvement Interest Subaccount is to be applied to the payment of interest on the Bonds as the same becomes due and payable as provided in the Bond Resolution.

Common Reserve Subaccount. If on the day preceding any principal or interest payment date, the amount in the Debt Service Subaccount is less than the Accrued Debt Service for all Bonds then Outstanding which are entitled to the benefit of the Common Reserve Subaccount, the City and County will pay out of the Common Reserve Subaccount to each Paying Agent for such Bonds the amount necessary to satisfy the deficiency for payment to the holders of such Bonds. Amounts so applied are to be derived first, from cash or Investments Securities on credit to the Common Reserve Subaccount and second, from draws or demands on Support Facilities held as a part of the Common Reserve Subaccount, such draws or demands to be made *pro rata* among all such Support Facilities based on the respective available amounts under such Support Facilities and upon the terms and conditions set forth in such Support Facilities.

Whenever the amounts on deposit in the Common Reserve Subaccount exceed the Common Reserve Subaccount Requirement, the City and County will withdraw the amount of such excess and deposit such excess to the credit of the Debt Service Subaccount or the Sewer Fund, as the City and County may determine.

Whenever the amount (exclusive of Support Facilities) in the Common Reserve Subaccount, together with the amount in the Debt Service Subaccount attributable to Bonds entitled to the benefit of the Common Reserve Subaccount, is sufficient to pay in full the principal or Redemption Price, if any, of and interest on all such Outstanding Bonds in accordance with their terms, the funds on credit to the Common Reserve Subaccount are to be transferred to the Debt Service Subaccount and applied to make such payment. Prior to such transfer, all Investment Securities held in the Common Reserve Subaccount will be liquidated by the City and County to the extent necessary to provide for timely payment of the principal or Redemption Price, if any, of and interest on such Bonds.

When a Series of Bonds entitled to the benefit of the Common Reserve Subaccount is refunded in whole or in part or is otherwise deemed paid within the meaning of the Bond Resolution, moneys may be withdrawn from the Common Reserve Subaccount to pay or provide for the payment of such Bonds or refunded Bonds, as the case may be; provided that immediately after such withdrawal or transfer there must be on credit to the Common Reserve Subaccount for those Bonds of the Series of Bonds not refunded an amount equal to the Common Reserve Subaccount Requirement for the Bonds entitled to the benefit of the Common Reserve Subaccount then Outstanding after taking into account such refunding or payment.

The City and County may determine in the Series Resolution authorizing a Series of Bonds or a Series Certificate related to a Series of Bonds that such Series of Bonds will not be entitled to the benefit of the Common Reserve Subaccount, in which case no amount will be required from the proceeds of such Series of Bonds for credit to the Common Reserve Subaccount and no amount will be payable from the Common Reserve Subaccount to pay amounts due or payable with respect to such Series of Bonds.

The Common Reserve Subaccount Requirement is to be calculated or recalculated: (i) at the time of issuance of a Series of Bonds (or Bond Anticipation Notes); (ii) at the time a Series of Bonds is retired in its entirety; (iii) at such other time as in the Opinion of Counsel is required to maintain the exclusion of interest on the Tax-exempt Bonds from gross income for federal income taxation purposes.

Separate Series Reserve Subaccounts. If on the day preceding any principal or interest payment date, the amount in the Debt Service Subaccount is less than Accrued Debt Service for the Bonds of a Series then

Outstanding which are entitled to the benefit of a Separate Series Reserve Subaccount, the City and County will pay out of such Separate Series Reserve Subaccount to the Paying Agent for such Bonds the amount necessary to satisfy the deficiency for payment to the holders of such Bonds. Amounts so applied shall be derived first, from cash or Investments Securities on credit to such Separate Series Reserve Subaccount and second, from draws or demands on Support Facilities held as a part thereof, such draws or demands to be made *pro rata* among all such Support Facilities based on the respective available amounts under such Support Facilities and upon the terms and conditions set forth in such Support Facilities.

Whenever the amounts on deposit in any Separate Series Reserve Subaccount exceed the applicable Separate Series Reserve Subaccount Requirement, the City and County will withdraw the amount of such excess and deposit such excess to the credit of the Debt Service Subaccount or the Sewer Fund, as the City and County may determine.

Whenever the amount (exclusive of Support Facilities) in any Separate Series Reserve Subaccount, together with the amount in the Debt Service Subaccount attributable to Bonds entitled to the benefit of such Separate Series Reserve Subaccount, is sufficient to pay in full the principal or Redemption Price, if any, of and interest on all such Outstanding Bonds in accordance with their terms, the funds on credit to such Separate Series Reserve Subaccount are to be transferred to the Debt Service Subaccount and applied to make such payment. Prior to such transfer, all Investment Securities held in such Separate Series Reserve Subaccount will be liquidated by the City and County to the extent necessary to provide for timely payment of the principal or Redemption Price of and interest on such Bonds.

When a Series of Bonds entitled to the benefit of the Separate Series Reserve Subaccount is refunded in whole or in part or are otherwise deemed paid within the meaning of the Bond Resolution, moneys may be withdrawn from such Separate Series Reserve Subaccount to pay or provide for the payment of such Bonds or refunded Bonds, as the case may be; *provided* that immediately after such withdrawal or transfer there must be on credit to such Separate Series Reserve Subaccount an amount equal to the Separate Series Reserve Subaccount Requirement for the Bonds then Outstanding which are entitled to the benefit of such Separate Series Reserve Subaccount after taking into account such refunding or payment.

Each Separate Series Reserve Subaccount Requirement is to be calculated or recalculated: (i) at the time of issuance of a Series of Bonds (or Bond Anticipation Notes); (ii) at the time a Series of Bonds is retired in its entirety; (iii) at such other time as in the Opinion of Counsel is required to maintain the exclusion of interest on the Tax-exempt Bonds from gross income for federal income taxation purposes.

Certain provisions of the Bond Resolution relating to Separate Series Reserve Subaccount may be modified in whole or in part with respect to any Series of Bonds entitled to the benefits of a Separate Series Reserve Subaccount.

Rebate Subaccount. If and to the extent required by the Code, an Authorized Officer must periodically, at such times as may be required to comply with the Code, determine the amount required to be rebated or otherwise paid to the Department of the Treasury of the United States of America with respect to each Series of Tax-exempt Bonds and thereafter (i) transfer from any of the Funds, Accounts and Subaccounts pledged or held under the Bond Resolution, other than the Debt Service Subaccount, the Third Lien Obligation Subaccount and the Reimbursable Obligation Account and credit to the Rebate Subaccount an amount equal to all or a portion of such amount to be rebated with respect to such Series of Bonds and (ii) pay out of the Rebate Subaccount to the Department of the Treasury of the United States of America the amount, if any, required by the Code to be rebated or otherwise paid. Moneys in the Rebate Subaccount and the Subaccounts therein are not available for the benefit of the Holders of the Bonds and are not pledged to the payment of the Bonds or the interest thereon.

If and to the extent necessary to comply with any covenant established in a Series Resolution authorizing a Series of Bonds or in a Series Certificate relating to such Series of Bonds regarding maintaining the exclusion of interest on Tax-exempt Bonds from gross income for Federal income taxation purposes, the City and County may establish a Subaccount in the Rebate Subaccount with respect to such Series of Bonds or provide for the establishment such Subaccount in such Series Resolution or in such Series Certificate.

Third Lien Obligation Subaccount. The City and County must at all times maintain in the Third Lien Obligation Subaccount an amount equal to the Third Lien Obligation Requirement. Moneys on deposit in the Third Lien Obligation Subaccount will be applied by the City and County solely in accordance with the provisions of, and subject to the priorities and limitations and restrictions provided in the Bond Resolution, indenture or other instrument of the City and County securing or evidencing such Third Lien Obligations. Any moneys credited to the Third Lien Obligation Subaccount are immediately free and clear of the lien and pledge created by the Bond Resolution.

Purposes of the Various Subaccounts Outside Subordinate Obligation Account

Sewer Fund - Rate Stabilization Account. The amount of moneys and Investment Securities to be maintained from time to time in the Rate Stabilization Account is to be provided for in the Annual Budget. Moneys and Investment Securities may be transferred to the Rate Stabilization Account as provided in the Annual Budget from (i) the Sewer Fund in the order of priority provided in the Bond Resolution, or (ii) the Wastewater General Account as provided in the Bond Resolution. Moneys and Investment Securities credited to the Rate Stabilization Account are to be transferred to the Sewer Fund at the times and in the amounts as may be provided in the Annual Budget for the purposes of stabilizing the rates and charges of the Wastewater System.

Sewer Fund - Renewal and Replacement Account. Moneys on credit to the Renewal and Replacement Account may be applied to the cost of the construction of improvements to or reconstruction of the Wastewater System, emergency repairs of the Wastewater System, and major or extraordinary repairs, renewals or replacements of the Wastewater System, in each case to be set forth in the Annual Budget; (i) to restore or prevent physical damage to the Wastewater System or any part thereof; (ii) for the safe and efficient operation of the Wastewater System; or (iii) to prevent loss of Revenues.

If on the day preceding any interest payment date the moneys in the Debt Service Subaccount after making the transfer from the Common Reserve Subaccount as provided for in the Bond Resolution and from the Wastewater General Account as provided for in the First Bond Resolution, are insufficient to pay the interest, principal and redemption price becoming due on the Bonds, the City and County, after making all transfer required by the First Bond Resolution, must transfer from the Renewal and Replacement Account for credit to the Debt Service Subaccount the amount necessary (or all the moneys in such Account if less than the amount necessary) to satisfy such deficiency.

If on each January 1 and July 1 the moneys, Investment Securities and the amount of Support Facilities in the Common Reserve Subaccount are less than the Common Reserve Subaccount Requirement, and the transfer referred to in the preceding paragraph has been made, the City and County, after making all transfers required by the First Bond Resolution, must transfer from the Renewal and Replacement Account for credit to the Common Reserve Subaccount the amount necessary (or all the moneys in such Account if less than the amount necessary) to satisfy such deficiency.

Sewer Fund - Reimbursable Obligation Account. The City and County must at all times maintain in the Reimbursable Obligation Account an amount equal to the Reimbursable Obligation Requirement. Moneys on deposit in the Reimbursable Obligation Account will be applied by the City and County solely to reimburse the General Fund of the City and County for payment of debt service due on Reimbursable Obligations issued or to be issued by the City and County with respect to the Wastewater System. Any moneys deposited in the Reimbursable Obligation Account are immediately free and clear of the lien and pledge created by the Bond Resolution.

Sewer Fund - Wastewater General Account. The City and County, after making all transfers required by the First Bond Resolution, must transfer from the Wastewater General Account to the Debt Service Subaccount, the Common Reserve Subaccount and each Separate Series Reserve Subaccount the amount necessary (or all the moneys in the Wastewater General Account if less than the amount necessary) to satisfy any deficiencies in such subaccounts required by the Bond Resolution.

Amounts in the Wastewater General Account not required to meet a deficiency referred to in the preceding paragraph or other deficiency as provided in the First Bond Resolution may be applied to the following purposes in the following order of priority:

- (1) the Costs of Improvements, or the provision of one or more reserves therefor;
- (2) for transfer to the Rate Stabilization Account in the Sewer Fund such amounts as may be provided in the Annual Budget for the purpose of stabilizing rates and charges;
- (3) the purchase at such price or prices as the City and County may deem advisable or redemption of any Bonds and expenses of such purchase or redemption at any time; and
- (4) for any other lawful purpose of the City and County.

Sewer Revenue Bond Improvement Fund - Improvement Second Account. As soon as practicable on the date of delivery of the Bonds of a Series, the amount required pursuant to the Series Resolution or Series Certificate will be deposited in the Improvement Fund for credit to the Improvement Second Account. In addition, the City and County will deposit in the Improvement Fund for credit to the Improvement Second Account such moneys other than proceeds of the Bonds as the City and County may determine to be proper or appropriate to pay the Costs of Improvements.

The Series Resolution authorizing the issuance of any Series of Bonds (exclusive of Refunding Bonds) may create and establish one or more separate special series improvement subaccounts (a "Series Improvement Second Subaccount") in the Improvement Second Account, with such designation as may be appropriate. In the event any interest on such Bonds is to be capitalized from the proceeds of such Bonds, a special series subaccount must be created in the Improvement Second Account (a "Series Improvement Interest Subaccount") with such designation as may be appropriate.

Moneys, including proceeds of the Bonds of a Series, which are credited to a Series Improvement Subaccount are to be applied to the payment of the Costs as are specified in the applicable Series Resolution or Series Certificate. Any balance remaining in such Series Improvement Second Subaccount upon completion of payment of such Costs may be used for any lawful purpose of the City and County; *provided* that the City and County has obtained an Opinion of Counsel that any such application will not impair the exemption from Federal income taxation of interest on any of the Tax-exempt Bonds.

Moneys credited to a Series Improvement Second Interest Subaccount are to be used for the purpose of paying interest on the Bonds of designated Series. On or before the 5th day preceding the end of the month next preceding the maturity of an installment of interest on the Bonds for the payment of which moneys have been credited to such Series Improvement Second Interest Subaccount, the City and County must transfer from a Series Improvement Second Interest Subaccount to the Debt Service Subaccount an amount which, together with any moneys theretofore held in the Debt Service Subaccount, are sufficient to pay such next maturing installment of interest on such Bonds.

Payments from the Improvement Second Account are to be made as specified in the Series Resolution authorizing the issuance of a Series of Bonds or a Series Certificate related to a Series of Bonds.

Moneys, including proceeds of the Bonds, in the Improvement Second Account, pending their application as provided in the Bond Resolution and Series Resolution and Series Certificate, are subject to a prior and paramount lien and charge in favor of the Holders of the Bonds, and the Holders of the Bonds have a valid claim on such moneys for the further security of the Bonds until paid out or transferred as provided in the Bond Resolution. In the event that there is an insufficiency in the Debt Service Subaccount to pay Debt Service after all transfers, other than a transfer from the Wastewater System Facility Charge Account, have been made pursuant to and in accordance with the Bond Resolution, the City and County must transfer from the Improvement Second Account such amount (or all remaining amounts in such Improvement Second Account) as is deemed necessary by the Director of Budget and Fiscal Services for deposit in the Debt Service Subaccount, which, together with the amounts then on credit to the Debt Service Subaccount, is sufficient to pay Debt Service.

Sewer Fund - Wastewater System Facility Charge Account. In the event that there is an insufficiency in the Debt Service Subaccount to pay Debt Service after all transfers have been made pursuant to and in accordance with the First Bond Resolution and the Bond Resolution, the City and County must transfer from the Wastewater System Facility Charge Account such amount (or all remaining amounts in the Wastewater System Facility Charge

Account) as is deemed necessary by the Director of Budget and Fiscal Services for deposit in the Debt Service Subaccount, which, together with the amounts then on deposit in the Debt Service Subaccount, is sufficient to pay Debt Service. The amount of any such transfer must at the earliest practicable date be reimbursed to the Wastewater System Facility Charge Account as provided in the Bond Resolution.

Amounts held in the Wastewater System Facility Charge Account are to be expended for the purposes specified in Section 6-47.1 of the City Code.

Investment of Funds

Moneys in the Debt Service Subaccount may, to the fullest extent practicable and reasonable, be invested and reinvested solely in noncallable Investment Securities which are Government Obligations, FNMA's or FHLMA's (as such terms are defined in the definition of Investment Securities) and which mature or are subject to redemption at the option of the holder thereof on or prior to the respective dates when the moneys in Debt Service Subaccount will be required for the purposes intended. Moneys in the Common Reserve Subaccount or any Separate Series Reserve Subaccount not required for immediate disbursement for the purpose for which the Common Reserve Subaccount or such Separate Series Reserve Subaccount is created may, to the fullest extent practicable and reasonable, be invested and reinvested solely in, and obligations credited to the Common Reserve Subaccount or such Separate Series Reserve Subaccount must be, investments specified in items (i) to (vi), inclusive, of the definition of Investment Securities and which mature or are available at par at or prior to five (5) years from the date of investment thereof.

Moneys in the Sewer Fund not required for immediate disbursement for the purpose for which such Fund is created may, to the fullest extent practicable and reasonable, be invested and reinvested, to the extent allowed by law, solely in, and obligations deposited in such Fund will be, Investment Securities which mature or are subject to redemption or payment at par at the option of the holder thereof, not later than such times as will be necessary to provide moneys when needed to provide payments from such Fund.

Moneys in the Improvement Second Account, other than a Series Improvement Second Interest Subaccount therein, not required for immediate disbursement for the purposes for which such Account is created may, to the fullest extent practicable and reasonable, be invested and reinvested to the extent allowed by law, solely in, and obligations deposited in such Account will be, Investment Securities which mature or are subject to redemption or payment at par at the option of the holder thereof not later than such times as shall be necessary to provide moneys when needed to provide payments from such Account.

Moneys in a Series Improvement Second Interest Subaccount in the Improvement Second Account not required for immediate disbursement for the purposes for which such Account is created may, to the fullest extent practicable and reasonable, be invested and reinvested to the extent allowed by law, solely in, and obligations deposited in such Account shall be, noncallable Investment Securities which are Government Obligations, FNMA's or FHLMA's (as such terms are defined in the definition of Investment Securities) that mature or are subject to redemption at the option of the holder thereof not later than such times as shall be necessary to provide moneys when needed to provide payments from such Account.

To the extent permitted in the Bond Resolution, all income received from the investment or reinvestment of moneys in the Funds, Accounts and Subaccounts established under the Bond Resolution will be deposited in the respective Fund, Account and Subaccount from which such investments are made and applied as a credit against the next succeeding deposit or credit required to be made pursuant to the Bond Resolution; provided however, that except as to the Third Lien Obligation Subaccount and the Reimbursable Obligation Account, all or a portion of the income received from the investment or reinvestment of moneys in any such Fund, Account and Subaccount may be deposited in the Sewer Fund or the Improvement Second Account, including a Series Improvement Second Interest Subaccount therein; and *provided, further, however*, that all income received from the investment or reinvestment of moneys in any Series Improvement Second Interest Subaccount must be deposited in the Debt Service Subaccount.

Neither the Director of Budget and Fiscal Services nor any Paying Agent shall be liable for any depreciation in value of any investments made by the City and County.

Valuation of Investment Securities

In computing the amount in any Fund, Account or Subaccount, Investment Securities therein are to be valued at cost or accreted value, whichever is lower, exclusive of accrued interest. The City and County is to determine the value of Investment Securities held in any Fund, Account or Subaccount as frequently as it deems necessary, but not less often than annually.

Depositaries

All moneys held by the City and County or any Depositary under the provisions of the Bond Resolution are to be held in trust and applied only in accordance with the provisions of the Bond Resolution, and each of the Funds, Accounts and Subaccounts established by the Bond Resolution shall be a trust fund.

Each Depositary must be a bank or trust company organized under the laws of any state of the United States or a national banking association having capital stock, surplus and undivided earnings of \$5,000,000 or more and willing and able to accept such office on reasonable and customary terms and authorized by law to act in accordance with the provisions of the Bond Resolution.

Concerning Depositaries and Paying Agents

Qualifications and Appointment. The Director of Budget and Fiscal Services may appoint one or more Paying Agents and Depositaries as of the date of issuance and delivery of the first Series of Bonds and may at any time or from time to time appoint one or more other Paying Agents or other Depositaries having the qualifications of a depository, as described in the Bond Resolution; provided however, the Director of Budget and Fiscal Services may be designated Paying Agent and/or Depositary. Each Paying Agent, other than the Director of Budget and Fiscal Services, and each Depositary, other than the Director of Budget and Fiscal Services, shall signify its acceptance of the duties and obligations imposed upon it by the Bond Resolution by executing and delivering to the City and County and the Director of Budget and Fiscal Services a written acceptance thereof.

Paying Agents and Depositaries May Buy, Hold, Sell or Deal in Bonds and Other Indebtedness of the City and County. Each Paying Agent and each Depositary and its respective directors, officers, employees or agents, may in good faith buy, sell, own, hold and deal in any of the Bonds issued under the provisions of the Bond Resolution and may join any action which any Holder of a Bond may be entitled to take, with like effect as if such Paying Agent or Depositary were not a Paying Agent or any Depositary, as the case may be, under the Bond Resolution. Any Paying Agent or any Depositary may in good faith hold any other form of indebtedness of the City and County; own, accept or negotiate any drafts, bills of exchange, acceptances or obligations of the City and County, and make disbursements for the City and County and enter into any commercial or business arrangement therewith.

Reimbursement of Paying Agents and Depositaries for Fees, Expenses and Charges. Each Paying Agent and each Depositary shall be entitled to reasonable fees and to reimbursement by the City and County for all expenses and charges reasonably incurred by it in the performance of its duties under the Bond Resolution. No Paying Agent nor Depositary shall have a lien for such fees and reimbursement on the moneys pledged to secure the Bonds under the Bond Resolution at any time held by it, prior to the lien or claim of the Holders of the Bonds on all such moneys.

Covenants

The City and County has covenanted and agreed in the Bond Resolution with the Holders of all Bonds issued pursuant to the Bond Resolution as follows:

Maintenance of the Properties of the Wastewater System; Keeping the System in Good Repair. The Department will: (i) maintain, preserve and keep, or cause to be maintained, preserved and kept, the properties of the Wastewater System and all additions and betterments thereto and extensions thereof, and every part and parcel thereof in good repair, working order and condition, (ii) from time to time make, or cause to be made, all necessary and proper repairs, renewals, replacements, additions, extensions and betterments thereto, so that at all times the business carried on in connection therewith shall properly and advantageously be conducted, and (iii) comply, or

cause to be complied with the terms and conditions of any permit or license for the Wastewater System or any part thereof issued by any federal or state governmental agency or body and with any federal or state law or regulation applicable to the construction, operation, maintenance and repair of the Wastewater System or requiring a license, permit or approval therefor.

Rates and Charges. The City and County will at all times fix, charge and collect such rates and other charges as shall be required in order that in each Fiscal Year the Net Revenues will be not less than the Net Revenue Requirement for such Fiscal Year (“Rate Covenant”). The failure in any Fiscal Year to comply with the foregoing Rate Covenant does not constitute an Event of Default if the City and County complies with requirements described in the next paragraph.

Prior to the end of each Fiscal Year the Director of Environmental Services or the Director of Budget and Fiscal Services if requested by the Director of Environmental Services must complete a review of the financial condition of the Department for the purpose of estimating whether the Net Revenues for such Fiscal Year and for the next succeeding Fiscal Year will be sufficient to comply with the Rate Covenant and must by a written certificate make a determination with respect to such compliance. Such review may take into consideration the completion of any uncompleted Improvement and the issuance of future Series of Bonds if necessary to finance the completion of such Improvements. Such written certificate must set forth a reasonably detailed statement of the actual and estimated Revenues, Operation and Maintenance Expenses, Aggregate Debt Service, and any other estimates or assumptions upon which such determination was based, and must be filed with the City Clerk on or before July 1 in each year. If it is determined in such written certificate that the Revenues may not be so sufficient, the Director of Environmental Services or the Director of Budget and Fiscal Services if requested by the Director of Environmental Services must forthwith make a study for the purpose of determining a schedule of fees, rates and charges which, in the opinion of the Director of Environmental Services or the Director of Budget and Fiscal Services, will cause sufficient Revenues to be collected in the following Fiscal Year to comply with the Rate Covenant and will cause additional Revenues to be collected in such following and later Fiscal Years sufficient to eliminate the amount of any deficiency at the earliest practicable time, or the Director of Environmental Services or the Director of Budget and Fiscal Services may elect to cause the Consulting Engineer to make such a study and render such opinion. The City Council shall as promptly as practicable but no later than the 120 days following such determination by the Director of Environmental Services or the Director of Budget and Fiscal Services, or receipt of the Consulting Engineer’s recommendation, adopt and place in effect a schedule of fees, rates and charges as so determined or recommended pursuant to the Bond Resolution.

Sale, Lease or Other Disposition of Properties of the Wastewater System. The properties of the Wastewater System may not be sold, mortgaged, leased or otherwise disposed of except as described below.

The properties of the Wastewater System may be sold, leased, or otherwise disposed of in their entirety if simultaneously with such sale, lease or other disposition thereof provision is made for the payment of all Bonds then Outstanding and such Bonds are no longer deemed Outstanding within the meaning of the Bond Resolution.

Any portion of the properties of the Wastewater System may be sold, leased, or otherwise disposed of on such terms and conditions as may be determined by the City and County if the value of such portion of the properties as of the date of such sale, lease or disposition does not exceed five percent (5%) of the net book assets of the Wastewater System as of the last day of the preceding Fiscal Year as shown in the most recent audited financial statements of the Department. Any part of the properties of the Wastewater System having a value as of the date of the sale, lease or disposition which exceeds 5% of the net book assets of the Wastewater System as of the last day of the preceding Fiscal Year as shown in the most recent audited financial statements of the Department may be sold, leased, or otherwise disposed of if the Consulting Engineer certifies to the City and County in writing that the terms and conditions of the proposed sale, lease or other disposition of any such properties are fair and reasonable, and that the estimated Revenues to be derived from the remaining properties of the Wastewater System, after taking into consideration the use by the Department of the proceeds of such proposed sale, lease or other disposition of such properties, will be sufficient to enable the City and County to comply with all covenants and conditions of the Bond Resolution. Proceeds of any sale, lease or other disposition of any portion of the properties of the Wastewater System pursuant to this provision are to be paid first into the Debt Service Account created by the First Bond Resolution and applied to the purchase or redemption of bonds thereunder, second into the Debt Service Subaccount and applied to the purchase or redemption of Bonds, and third into the Sewer Fund and applied by the City and

County for the purpose of constructing extensions, betterments or improvements to the Wastewater System as the City and County may determine.

Surplus lands, crops, timber, buildings and any other portion of the works, plant and facilities of the Wastewater System and real and personal property comprising a part thereof, which, in the opinion of the Director of Environmental Services, have become unserviceable, inadequate, obsolete, worn out, or unfit to be used in the operation of the Wastewater System, or no longer necessary, material to, or useful in such operation may be sold, leased, or otherwise disposed of. Proceeds of any such sale, lease or other disposition of any portion of the properties of the Wastewater System pursuant to this provision are to be paid into the Sewer Fund.

If permitted by the laws of the State, the City and County may transfer without consideration the properties comprising the Wastewater System to a public corporation or political subdivision of the State, provided such corporation or subdivision assumes all of the City and County's or the Department's obligations and duties under the Bond Resolution.

In the event that any part of the properties of the Wastewater System is transferred from the City and County through the operation of law (including condemnation), any moneys received by the City and County as a result of such transfer are to be paid: (i) if such proceeds are not in excess of \$250,000, into the Sewer Fund; or (ii) if such proceeds are in excess of \$250,000: (a) into the Debt Service Account created by the First Bond Resolution and applied to the purchase or redemption of bonds issued thereunder; (b) in the Debt Service Subaccount and applied to the purchase or redemption of Bonds; or (c) into the Renewal and Replacement Account and applied by the City and County for the purpose of constructing replacements, extensions, betterments or improvements to the Wastewater System, as the City and County shall determine.

Insurance. Except as provided for in the next paragraph, the Department must keep, or cause to be kept, the works, plants and facilities comprising the properties of the Wastewater System and the operations thereof insured to the extent available at reasonable at reasonable cost with responsible insurers, with policies payable to the City and County or the Department, against risks of direct physical loss, damage to or destruction of the above-ground structures, and the equipment and contents therein, of the Wastewater System arising from accidents, casualties or negligence, and other causes customarily insured against, at least to the extent that similar insurance is usually carried by utilities operating like properties, including liability insurance and workman's compensation insurance; provided, however, that any time while any contractor engaged in constructing any part of the Wastewater System is fully responsible for such insurance, the Department is not required to keep such part of the Wastewater System insured. All policies of insurance shall be for the benefit of the Holders of the Bonds and the City and County or the Department as their respective interests may appear.

In the event of any loss or damage to the properties of the Wastewater System covered by insurance, the Department will: (i) with respect to each such loss, promptly repair and reconstruct to the extent necessary to the proper conduct of the operations of the Wastewater System the lost or damaged portion thereof and shall apply the proceeds of any insurance policy or policies covering such loss or damage for that purpose to the extent required therefor, unless, in case of loss or damage involving \$250,000 or more, the Department determines that such repair and reconstruction will not be undertaken; and (ii) if the Department does not use the entire proceeds of such insurance to repair or reconstruct such lost or damaged property, the proceeds of such insurance policy or policies or any portion thereof not used for such repair or reconstruction, as the case may be, are to be paid into the Sewer Fund. If the Department does not obtain insurance from responsible insurers as provided for in the Bond Resolution, the City and County or the Department must self-insure; provided, however, that if the Department fails to carry insurance against any of the risks normally insured against by operators of facilities similar to the Wastewater System, it must secure the concurrence of an independent insurance consultant. In making its decision whether to concur in such self-insurance, the independent insurance consultant must (i) make an estimate of the added financial risks, if any, assumed by the Department as a result of the self-insurance; (ii) consider the availability of commercial insurance, the terms upon which such insurance is available and the costs of such available insurance, and the effect of such terms and costs upon the Department's costs and charges for its services; and (iii) determine whether the added financial risk, if any, being assumed by the Department is prudent in light of the savings to be realized from such self-insurance or in light of the general availability of insurance.

The Department may include insurance required by the Bond Resolution as part of a blanket insurance policy of the City and County.

Consulting Engineer. The City Council, the Director of Environmental Services or the Director of Budget and Fiscal Services may from time to time retain and appoint, as Consulting Engineer, an independent consulting engineer or engineering firm or corporation having special skill, knowledge and experience in analyzing the operations of wastewater systems, preparing rate analyses, forecasting the loads and revenues of wastewater systems, preparing feasibility reports respecting the financing of wastewater systems and advising on the operation of wastewater facilities, who shall be available to advise the Department, upon request, and to make such investigations and determinations as may be necessary from time to time under the provisions of the Bond Resolution.

Books of Account; Annual Audit. The Department will maintain and keep proper books of account relating to the Wastewater System and in accordance with generally accepted accounting principles. Within 180 days after the end of each Fiscal Year commencing with the Fiscal Year ending June 30, 2000, the Department will cause such books of account to be audited by an independent certified public accountant. The audit required by the Bond Resolution may be part of a comprehensive audit of the City and County, *provided* that the Wastewater System in such audit is treated as an "enterprise fund" and the revenues and expenses of the Wastewater System are stated in a manner which permits identification by category of the sources and uses of the Revenues. A copy of each audit report prepared in conformity with generally accepted accounting principles must be filed promptly with the City and County and sent to any Bondholder filing with the Director of Environmental Services a written request for a copy thereof. and to any Rating Agency which has rated any Bonds.

To Pay Bonds Punctually. The City and County will duly and punctually pay, or cause to be paid, but only from the Revenues, income and other funds specified in the Bond Resolution, the principal and Redemption Price (if any) of, and interest on, each and every Bond on the dates and at the places, and in the manner provided in the Bonds according to the true intent and meaning thereof, and the City and County will faithfully do and perform and at all times fully observe and keep any and all of its covenants, undertakings, stipulations and provisions contained in the Bonds and in the Bond Resolution.

Payment of Taxes and Other Claims. The Department must from time to time duly pay and discharge, or cause to be paid and discharged, all taxes, assessments and other governmental charges, or payments in lieu thereof, lawfully imposed upon the properties of the Wastewater System (or any part thereof) or upon the Net Revenues or income received therefrom when the same become due, as well as all lawful claims for labor, material and supplies, which, if not paid, might become a lien or charge upon said properties or any part thereof, or upon the Revenues derived from the ownership or operation of the Wastewater System, or which might in any way impair the security of the Bonds, except any such assessments, charges or claims which the Department in good faith contests as to validity.

Extension of Payment of Bonds. The City and County will not, directly or indirectly, extend or assent to the extension of the maturity of any of the Bonds or the time of payment of any claims for interest by the purchase of such Bonds, coupons, if any, or claims for interest or by any other arrangement and in case the maturity of any of the Bonds or the time for payment of any such claims for interest is extended, such Bonds or claims for interest will not be entitled, in case of any default under the Bond Resolution, to the benefit of the Bond Resolution or to any payment out of any assets of the City and County or the funds (except funds held in trust for the payment of particular Bonds or claims for interest pursuant to the Bond Resolution) held by the Paying Agents, except subject to the prior payment of the principal of all Bonds issued and Outstanding the maturity of which has not been extended and of such portion of the accrued interest on the Bonds as shall not be represented by such extended claims for interest.

Sound Improvements and Extensions. The Department will not expend any of the income, revenues, receipts, profits and other moneys derived by it from the ownership or operation of the Wastewater System for any renewals, replacements, additions, betterments and improvements to, or extensions of, the Wastewater System which, in the sole opinion of the Director of Environmental Services, will not properly and advantageously contribute to the conduct of the business of the Wastewater System in an efficient and economical manner unless required to do so to permit the continued operation of the Wastewater System or to preserve or protect the Wastewater System.

Annual Budget. Not later than May 31 before the beginning of any Fiscal Year the City and County or the Department will prepare a preliminary budget of Operation and Maintenance Expenses of the Wastewater System

and reserves therefor for the ensuing Fiscal Year. Each such budget and each Annual Budget will include, in addition to provisions for all anticipated Operation and Maintenance Expenses, provision for the payments required to be made to the Renewal and Replacement Account, provided that such payments shall in the aggregate at least equal the amount described below. Such preliminary budget and any Annual Budget may set forth such additional material as the City and County or the Department may determine.

Except as described below, on or before the 15th day of each such Fiscal Year, the City and County must finally adopt the Annual Budget for such year. The City and County may at any time adopt an amended Annual Budget for the remainder of the then current Fiscal Year. Copies of the Annual Budget and of any amended Annual Budget are to be made available for inspection by the Bondholders and are to be sent to each Rating Agency.

If for any reason the City and County does not adopt the Annual Budget before the 15th day of any Fiscal Year, the budget for the preceding Fiscal Year is deemed to be in effect for such Fiscal Year until the Annual Budget for such Fiscal Year is adopted. For any purpose of computation under the provisions of the Bond Resolution, the budget for the preceding year is deemed to have been adopted for any Fiscal Year until the Annual Budget for such year is adopted.

Every preliminary budget, Annual Budget and amended Annual Budget must: (i) set forth in reasonable detail amounts required for repair, replacement or reconstruction of the Wastewater System and major or extraordinary repairs, renewals or replacements of the Wastewater System, if any, for the period to be covered by such budget; (ii) specify the amounts to be deposited in the Renewal and Replacement Account, the Subordinate Obligation Account (including the Third Lien Obligation Subaccount therein), the Reimbursable Obligation Account and the Wastewater General Account, and the amounts to be maintained in the Sewer Fund for working capital and operating reserves and in the Rate Stabilization Account for rate stabilization purposes, if any, for such purposes for such period, (iii) specify the amounts to be transferred from the Wastewater General Account to the Rate Stabilization Account and to other Funds and Accounts; and (iv) project the amounts required for such purposes for the next five Fiscal Years in such format as the Director of Environmental Services may determine. A copy of each such report is to be filed and maintained in the records of the City and County.

Events of Default

Each of the following events constitutes an Event of Default under the Bond Resolution:

- (a) if payment of the principal and Redemption Price, if any, of any Bond, is not punctually made when due and payable, whether at the stated maturity thereof or upon proceedings for the redemption thereof (whether by voluntary redemption or a mandatory sinking fund redemption or otherwise);
- (b) if payment of the interest on any Bond is not punctually made when due;
- (c) if the provisions of any Series Resolution with respect to mandatory Sinking Fund Installment payments or the redemption of Term Bonds therefrom, as the case may be, are not punctually complied with at the time and in the manner specified in such Series Resolution;
- (d) if the City and County or the Department fails to duly and punctually perform or observe any other of the covenants, agreements or conditions contained in the Bond Resolution or in the Bonds, on the part of the City and County or the Department to be performed, and such failure continues for 90 days after written notice thereof from the Holders of not less than 20% of the Bonds then Outstanding; provided that, if such failure is such that it cannot be corrected within such 90-day period, it will not constitute an Event of Default if corrective action is instituted within such period and diligently pursued until the failure is corrected;
- (e) if the City and County: (i) admits in writing its inability to pay its debts generally as they become due; or (ii) files a petition in bankruptcy or seeking a composition of indebtedness under the provisions of any Federal or state bankruptcy or similar law; or (iii) makes an assignment for the benefit of its creditors; or (iv) files a petition or any answer seeking relief under the provisions

of any Federal or state bankruptcy or similar law; or (v) consents to the appointment of a receiver of the whole or any substantial part of the Wastewater System; or (vi) consents to the assumption by any court of competent jurisdiction under the provisions of any other law for the relief or aid of debtors of custody or control of the City and County or the Department, or of the whole or any substantial part of the Wastewater System; and

(f) if a default occurs under the First Bond Resolution.

Notice to Bondholders of Event of Default

Immediately after the occurrence of an Event of Default or within 30 days after any Paying Agent knows of any other Event of Default, the Paying Agent or Paying Agents shall give notice of all such Events of Default to the Bondholders, all other Paying Agents and Support Facility Providers, and each Rating Agency, in the manner as provided for in the Bond Resolution, unless such Events of Default shall have been cured before the giving of such notice.

Acceleration of Bonds; Rights of Insurers

If an Event of Default shall happen and shall not have been remedied, then and in every such case the Holders of not less than 25% in principal amount of the Bonds then Outstanding, by notice in writing to the City and County and the Director of Budget and Fiscal Services, may declare the principal of all the Bonds then Outstanding, and the interest accrued thereon, to be due and payable immediately, and upon any such declaration the same shall become and be immediately due and payable. The right of the Holders of not less than 25% in principal amount of the Bonds then Outstanding to make any such declaration, however, shall be subject to the condition that if, at any time after such declaration, but before the Bonds shall have matured by their terms, all overdue installments of interest upon the Bonds, together with interest on such overdue installments of interest to the extent permitted by law and all other sums then payable by the City and County under the Bond Resolution (except the principal of, and interest accrued since the next preceding interest date on, the Bonds due and payable solely by virtue of such declaration) shall either be paid by or for the account of the City and County or provision satisfactory to the Holders of a majority in principal amount of the Bonds then Outstanding shall be made for such payment, and all defaults under the Bonds or under the Bond Resolution (other than the payment of principal and interest due and payable solely by reason of such declaration) shall be cured or be secured to the satisfaction of the Holders of a majority in principal amount of the Bonds then Outstanding or provision deemed by such Holders of the Bonds to be adequate shall be made therefor, then and in every such case the Holders of at least a majority in principal amount of the Bonds then Outstanding, by written notice to the City and County, may rescind such declaration and annul such default in its entirety, but no such rescission shall extend to or affect any subsequent default or impair or exhaust any resulting right or power.

The bond insurers for all Outstanding Bonds and for the Series 2003 Bonds have certain consent rights in connection with any default which may constrain the rights of the Holders described above.

Inspection of Books and Records; the City and County to Account as Trustee for Express Trust

The City and County covenants that if an Event of Default shall have happened and shall not have been remedied, the books of record and account of the Department relating to the Wastewater System and all other records relating thereto shall at all times be subject to the inspection and use of the Holders of at least 25% in principal amount of the Bonds then Outstanding and of their respective agents and attorneys or of any committee therefor.

The City and County covenants that if an Event of Default shall have happened and shall not have been remedied, the City and County will continue to account, as a trustee of an express trust, for all Revenues and other moneys, securities and funds pledged under the Bond Resolution.

Application of Revenues in an Event of Default

During the continuance of an Event of Default as described in items (a) through (c) of the Events of Default described above or of any other Event of Default resulting in an Event of Default described in items (a) through (c)

of the Events of Default described above, the Revenues received by a receiver appointed pursuant to the Bond Resolution as the result of the taking of possession of the business and properties of the Wastewater System, are to be applied by the receiver: first, to the payment of all necessary and proper Operation and Maintenance Expenses of the Wastewater System and all other proper disbursements or liabilities made or incurred by the receiver; second, to the then due and overdue payments into the Debt Service Subaccount, including the making up of deficiencies therein; and last, for any lawful purpose in connection with the Wastewater System.

In the event that at any time the funds held by the receiver are insufficient for the payment of the principal and Redemption Price (if any) of, and interest then due on, the Bonds, such funds (other than funds held for the payment or redemption of particular Bonds or coupons) and all Revenues of the Department and other of its moneys received or collected for the benefit or for the account of Holders of the Bonds by the receiver are to be applied as follows:

- (1) Unless the principal of all of the Bonds shall have become due and payable,

First, to the payment of all necessary and proper Operation and Maintenance Expenses of the Wastewater System and all other proper disbursements or liabilities made or incurred by the receiver;

Second, to the payment to the persons entitled thereto of all installments of interest then due (including any interest on overdue principal) in the order of the maturity of such installments, earliest maturities first, and if the amounts available shall not be sufficient to pay in full any installment or installments of interest maturing on the same date, then to the payment thereof ratably, according to the amount due thereon, to the persons entitled thereto, without any discrimination or preference; and

Third, to the payment to the persons entitled thereto of the principal and premium, if any, due and unpaid upon the Bonds at the time of such payment without preference or priority of any Bond over any other Bonds, ratably, according to the amounts due respectively for principal and redemption premium, without any discrimination or preference.

- (2) If the principal of all of the Bonds shall have become due and payable,

First, to the payment of all necessary and proper Operation and Maintenance Expenses of the Wastewater System and all other proper disbursements or liabilities made or incurred by the receiver;

Second, to the payment of the principal and interest then due and unpaid upon the Bonds without preference or priority of principal over interest or of interest over principal, or of any installment of interest over any other installment of interest, or of any Bond over any other Bonds, ratably, according to the amounts due respectively for principal and interest, to the persons entitled thereto without any discrimination or preference.

Whenever moneys are to be applied as described in the foregoing paragraphs, such moneys shall be applied by the receiver at such times, and from time to time, as it in its sole discretion shall determine, having due regard to the amount of such moneys available for application and the likelihood of additional moneys becoming available for such application in the future.

If and whenever all overdue installments of interest on all Bonds, together with the reasonable and proper charges, expenses, and liabilities of the Holders of the Bonds, their respective agents and attorneys, and all other sums payable by the City and County under the Bond Resolution including the principal and Redemption Price (if any) of all Bonds which shall then be payable, shall either be paid in full by or for the account of the City and County or provision satisfactory to the receiver shall be made for such payment, and all defaults under the Bond Resolution or the Bonds shall be made good and secured to the satisfaction of the receiver or provision deemed by the receiver to be adequate therefor, the receiver shall pay over to the Department all of its moneys, securities, funds and Revenues then remaining unexpended in the hands of the Bondholders' Committee (except moneys, securities, funds or Revenues deposited or pledged, or required by the terms of the Bond Resolution to be deposited or pledged,

with the Director of Budget and Fiscal Services), control of the business and possession of the property of the Department shall be restored to the Department, and thereupon the City and County shall be restored to its former positions and rights under the Bond Resolution, and all Revenues shall thereafter be applied as provided for in the Bond Resolution. No such payment over to the Department by the receiver or resumption of this application of Revenues as provided in the Bond Resolution, shall extend to or affect any subsequent default under the Bond Resolution or impair any right consequent thereon.

Suits at Law or Equity and Mandamus and Appointment of a Receiver

If an Event of Default shall happen and shall not have been remedied, then and in every such case, but subject to the provisions, limitations and conditions as set forth in the Bond Resolution, the Holder of any Bond at the time Outstanding shall be entitled, for the equal benefit and protection of all Holders of the Bonds similarly situated to proceed, protect and enforce the rights vested in such Holder by the Bond Resolution by such appropriate judicial proceeding as such Holder shall deem most effectual to protect and enforce any such right, either by suit in equity or by action of law, whether for the specific performance of any covenant or agreement contained in the Bond Resolution, or in aid of the exercise of any power granted in the Bond Resolution, or to enforce any other legal or equitable right vested in the Holders of Bonds by the Bond Resolution or by law; provided, however, that no judicial proceeding shall be brought seeking the appointment of a receiver to take possession of the Wastewater System or to manage, receive and apply the Revenues unless the Holders of not less than a majority in principal amount of the Bonds then Outstanding or a Bondholders' Committee representing the Holders of not less than a majority in principal amount of the Bonds then Outstanding shall have joined in or consented to such proceeding.

Bondholders' Committee

If an Event of Default shall happen and shall not have been remedied, the Holders of not less than 25% in principal amount of the Bonds then Outstanding may call a meeting of the Holders of Bonds for the purpose of electing a Bondholders' Committee. Such meeting shall be called and proceedings thereat shall be conducted as provided for other meetings of Bondholders pursuant to the Bond Resolution. At such meeting the Holders of not less than a majority of the principal amount of the Bonds then Outstanding must be present in person or by proxy in order to constitute a quorum for the transaction of business, less than a quorum, however, having power to adjourn from time to time without any notice other than that required by the Bond Resolution. A quorum being present at such meeting, the Bondholders present in person or by proxy may, by the votes cast by the Holders of a majority in principal amount of the Bonds so present in person or by proxy, elect one or more persons who may or may not be Bondholders to the Bondholders' Committee which shall act as trustee for all Bondholders. The Bondholders present in person or by proxy at said meeting, or at any adjourned meeting thereof, shall prescribe the manner in which the successors of the persons elected to the Bondholders' Committee at such Bondholders' meeting shall be elected or appointed, and may prescribe rules and regulations governing the exercise by the Bondholders' Committee of the power conferred upon it, and may provide for the termination of the existence of the Bondholders' Committee.

Bondholders May Direct Proceedings; Rights of Insurers

The Holders of not less than a majority in principal amount of the Bonds at the time outstanding are authorized and empowered: (1) to direct the time, method, and place of conducting any proceeding for any remedy available to the holders of the Bonds; or (2) on behalf of the holders of the Bonds then outstanding, to consent to the waiver of any Event of Default or its consequences. No waiver or rescission shall extend to any subsequent or other default, or impair any right consequent thereon.

The bond insurers for all Outstanding Bonds and for the Series 2003 Bonds have certain consent rights in connection with any default which may constrain the rights of the Holders described above.

Abandonment of Proceedings; Adverse Determination

No delay or omission of any Holder of Bonds to exercise any right or power arising upon the occurrence of a default under the Bond Resolution, including an Event of Default, shall impair any right or power or shall be construed to be a waiver of any such default or to be an acquiescence therein. Every power and remedy given by the

Bond Resolution to the Holders of Bonds may be exercised from time to time and as often as may be deemed expedient by such Holders.

In case the Holders of the Bonds or a Bondholders' Committee formed pursuant to the Bond Resolution shall have proceeded to enforce any right under the Bond Resolution and such proceedings shall have been discontinued or abandoned for any reason, or shall have been determined adversely to the Holders of the Bonds or such Bondholders' Committee, then and in every such case the City and County, and the Holders of the Bonds shall be restored to their former positions and rights under the Bond Resolution, and all rights, remedies and powers of the Holders of the Bonds shall continue as if no such proceedings had been taken.

Remedies Subject to Rights of Holders of First Resolution Obligations

The Bond Resolution expressly limits the right of holders of the Bonds as described below.

(A) In the event of any insolvency or bankruptcy proceedings, and any receivership, liquidation, reorganization or other similar proceedings in connection therewith, relative to the City and County or the Department, or to property of the City and County or the Department, and in the event of any proceedings for voluntary liquidation, dissolution or other winding up of the City and County or the department, the Holders of all First Resolution Obligations then outstanding shall be entitled to receive payment in full of all principal and interest on all such First Resolution Obligations before the holders of the Bonds are entitled to receive any payment from the trust estate under the First Bond Resolution consisting of the Net Revenues and funds held under the First Bond Resolution (hereinafter referred to as the "Trust Estate") on account of principal (and premium, if any) or interest on the Bonds.

(B) In the event that any issue of Bonds is declared due and payable before its expressed maturity because of the occurrence of an event of default (under circumstances when the provisions of (A) above shall not be applicable), the Holders of all First Resolution Obligations outstanding at the time such Bonds so become due and payable because of such occurrence of such an event of default shall be entitled to receive payment in full of all principal and interest on all such First Resolution Obligations before the holders of the Bonds are entitled to receive any accelerated payment from the Trust Estate of principal (and premium, if any) or interest on the Bonds.

(C) If any event of default with respect to the First Resolution Obligations shall have occurred and be continuing (under circumstances when the provisions of (A) above shall not be applicable), the Holders of all First Resolution Obligations then outstanding shall be entitled to receive payment in full of all principal and interest on all such First Resolution Obligations before the holders of the Bonds are entitled to receive any accelerated payment from the Trust Estate of principal (and premium, if any) or interest on the Bonds.

(D) No First Resolution Obligation holder shall be prejudiced in his right to enforce subordination of the Bonds by any act or failure to act on the part of the City and County.

(E) The provisions of (A), (B), (C) and (D) above are solely for the purpose of defining the relative rights of the First Resolution Obligation holders on the one hand, and the holders of Bonds on the other hand, and nothing in the Bond Resolution shall impair, as between the City and County and the owners of the Bonds, the obligation of the City and County to pay to the owners thereof the principal thereof and premium, if any, and interest thereon in accordance with its terms, nor shall anything therein prevent the holders of the Bonds from exercising all remedies otherwise permitted by applicable law or under the Bond Resolution upon default thereunder, subject to the rights under (A), (B), (C) and (D) above of the Holders of First Resolution Obligations to receive cash, property or securities otherwise payable or deliverable to the holders of the Bonds. Insofar as a trustee or paying agent for the Bonds is concerned, the foregoing provisions shall not prevent the application by such trustee or paying agent of any moneys deposited with such trustee or paying agent for the purpose of the payment of or on account of the principal (and premium, if any) and interest on such Bonds if such trustee or paying agent did not have knowledge at the time of such application that such payment was prohibited by the foregoing provisions.

Amending and Supplementing of Resolution; Rights of Insurers

Amending and Supplementing of Resolution Without Consent of Holders of Bonds. The City and County, from time to time and at any time and without the consent or concurrence of any Holder of any Bond, may adopt a

Series Resolution (i) for the purpose of providing for the issuance of Bonds pursuant to the provisions as set forth in the Bond Resolution; (ii) to make any changes, modifications, amendments or deletions to the Bond Resolution which may be required to permit the Bond Resolution to be qualified under the Trust Indenture Act of 1939 of the United States of America; or (iii) if the rights of the Holders of the Bonds then Outstanding shall not be materially adversely affected thereby, a Supplemental Resolution (herein defined and referred to as a “Supplemental Resolution”) for any one or more of the following purposes:

1. to make any changes or corrections in the Bond Resolution as to which the City and County shall have been advised by counsel that the same are verbal corrections or changes or are required for the purpose of curing or correcting any ambiguity or defective or inconsistent provision or omission or mistake or manifest error contained in the Bond Resolution, or to insert in the Bond Resolution such provisions clarifying matters or questions arising under the Bond Resolution as are necessary or desirable;
2. to add additional covenants and agreements of the City and County for the purpose of further securing the payment of the Bonds;
3. to surrender any right, power or privilege reserved to or conferred upon the City and County by the terms of the Bond Resolution;
4. to confirm as further assurance any lien, pledge or charge, or the subjection to any lien, pledge, or charge, created or to be created by the provisions of the Bond Resolution;
5. to grant to or to confer upon the Holders of the Bonds any additional rights, remedies, powers, authority or security that lawfully may be granted to or conferred upon them; and
6. to modify in any other respect any of the provisions of the Bond Resolution.

Except for Series Resolutions authorizing the issuance of Bonds pursuant to the Bond Resolution, the City and County shall not adopt any Supplemental Resolution authorized by the foregoing provisions of the Bond Resolution unless in the Opinion of Counsel the adoption of such Supplemental Resolution is permitted by the Bond Resolution and the provisions of such Supplemental Resolution do not materially adversely affect the rights of the Holders of the Bonds then Outstanding.

Amendment of Resolution With Consent of Holders of the Bonds. With the consent of the Holders of not less than a majority of the Bonds then Outstanding, the City and County from time to time and at any time may adopt a resolution amendatory of or supplemental to the Bond Resolution for the purpose of adding any provisions to, or changing in any manner or eliminating any of the provisions of, the Bond Resolution, or modifying or amending the rights and obligations of the City and County thereunder, or modifying or amending in any manner the rights of the Holders of the Bonds then Outstanding; provided, however, that without the specific consent of the Holder of each such Bond which would be affected thereby, no Supplemental Resolution amending or supplementing the provisions of the Bond Resolution shall: (1) change the fixed maturity date for the payment of the principal of any Bond or the dates for the payment of interest thereon or the terms of the redemption thereof, or reduce the principal amount of any Bond or the rate of interest thereon or the Redemption Price (or the redemption premium) payable upon the redemption or prepayment thereof; or (2) reduce the aforesaid percentage of Bonds, the Holders of which are required to consent to any Supplemental Resolution amending or supplementing the provisions of the Bond Resolution; or (3) give to any Bond or Bonds any preference over any other Bond or Bonds secured by the Bond Resolution; or (4) authorize the creation of any pledge of the Revenues and other moneys pledged under the Bond Resolution, prior, superior or equal to the pledge of and lien and charge thereon created in the Bond Resolution for the payment of the Bonds except to the extent provided in the Bond Resolution; or (5) deprive any Holder of the Bonds in any material respect of the security afforded by the Bond Resolution; provided further, however, that without the specific consents of the Holders of not less than a majority in principal amount of the Term Bonds then Outstanding and affected thereby, no Supplemental Resolution amending or supplementing the provisions of the Bond Resolution shall (a) change the amount of any Sinking Fund Installments for the retirement of Term Bonds or the due dates of such installments or the terms for the purchase or redemption thereof from such installments, or (b) reduce the aforesaid percentage of Term Bonds, the Holders of which are required to consent to any such Supplemental Resolution. (Nothing in this paragraph contained, however, shall be construed as making necessary the approval of the Holders of the Bonds of the adoption of any Supplemental Resolution). A

modification or amendment with respect to the Sewer Fund or the Debt Service Subaccount or Common Reserve Subaccount or any Separate Series Reserve Subaccount therein shall not be deemed a change in the terms of payments; provided that no such modification or amendment shall, except upon the consent of the Holders of all Bonds then outstanding affected thereby, reduce the amount or amounts required to be credited to the Debt Service Subaccount or Common Reserve Subaccount or any Separate Series Reserve Subaccount or their respective successor.

The bond insurers for all Outstanding Bonds and for the Series 2003 Bonds have certain consent rights in connection with any amendment which may constrain the rights of the Holders described above.

The proof of the giving of any consent required and of the holding of Bonds for the purpose of giving consents shall be made in accordance with the Bond Resolution. It shall not be necessary that the consents of the Holders of the Bonds approve the particular form of wording of the proposed amendment or supplement or of the Supplemental Resolution affecting such amendment or supplement, but it shall be sufficient if such consents approve the substance of the proposed amendment or supplement. After the Holders of the required percentage of Bonds shall have filed their consents to the amending or supplementing of the Bond Resolution pursuant to the Bond Resolution, the City and County shall publish at least once a notice of such amending or supplementing of the Bond Resolution, in *The Bond Buyer*, published in New York, New York, or in lieu of publication in *The Bond Buyer*, in some other newspaper specializing in financial matters as provided for in the Bond Resolution and shall mail a copy of such notice, postage prepaid to each registered Holder of Bonds then Outstanding, at his address, if any, appearing upon the registry books, but failure to mail copies of said notice to any of said Holders shall not affect the validity of the Supplemental Resolution effecting such amendments or supplements or the consent thereto. A record, consisting of the papers required by the Bond Resolution, shall be proof of the matters therein stated until the contrary is proved. No action or proceeding to set aside or invalidate such Supplemental Resolution or any of the proceedings for its adoption shall be instituted or maintained unless such action or proceeding is commenced within 60 days after the publication and mailing of the notice required by the Bond Resolution.

The City and County shall furnish a notice of each amendment or supplement and a copy of the Supplemental Resolution effecting such amendment or supplement to each rating agency which has rated the Bonds at least 15 days prior to the effective day of the Supplemental Resolution.

Discharge of Liens and Pledges; Bonds No Longer Outstanding and Deemed to be Paid

Except as otherwise provided in the Bond Resolution with regard to Option Bonds, the obligations of the City and County under the Bond Resolution and the liens, pledges, charges, trusts, covenants and agreements of the City and County made or provided for in the Bond Resolution, shall be fully discharged and satisfied as to any Bond and such Bond shall no longer be deemed to be Outstanding under the Bond Resolution:

- (i) when such Bond shall have been canceled, or shall have been surrendered for cancellation or is subject to cancellation, or shall have been purchased by or behalf of the City and County from moneys held under the Bond Resolution; or
- (ii) as to any Bond not canceled or surrendered for cancellation or subject to cancellation or so purchased, when payment of the principal and redemption price (if any) of such Bond, plus interest on such principal to the due date thereof (whether such due date be by reason of maturity or upon redemption or prepayment, or otherwise) either (a) shall have been made or caused to be made in accordance with the terms thereof, or (b) shall have been provided for by irrevocably depositing with the Paying Agent for such Bond, in trust, and irrevocably appropriating and setting aside exclusively for such payment, either (1) moneys sufficient to make such payment or (2) noncallable Refunded Municipal Obligations or noncallable Investment Securities described in item (i) of the definition of Investment Securities as set forth in the Bond Resolution, maturing as to principal and interest in such amount and at such times as will insure, together with any cash deposit, the availability of sufficient moneys to make such payment, whichever the City and County deems to be in its best interest and as verified by an independent nationally recognized firm of certified public accountants in a report delivered to the City and County and the Director of Budget and Fiscal Services, and all necessary and proper fees, compensation and expenses of the Director of Budget and Fiscal Services and the Paying Agents pertaining to the Bond with respect to which such deposit is

made shall have been paid or the payment thereof provided for to the satisfaction of the Director of Budget and Fiscal Services and said Paying Agents.

At such time as a Bond shall be deemed to be no longer Outstanding under the Bond Resolution, as aforesaid, such Bond, except for the purposes of any payment from such moneys, Refunded Municipal Obligations or Investment Securities, shall no longer be secured by or entitled to the benefits of the Bond Resolution.

Notwithstanding the foregoing, in the case of a Bond which is to be redeemed or otherwise prepaid prior to its stated maturity, no deposit under clause (b) of subparagraph (ii) of the second preceding paragraph above shall constitute such payment, discharge and satisfaction as aforesaid until such Bond shall have been irrevocably designated for redemption or prepayment and proper notice of such redemption or prepayment shall have been previously given in accordance with the Bond Resolution or provision shall have been irrevocably made for the giving of such notice.

Any such moneys so deposited with the Paying Agents for the Bonds as provided in the Bond Resolution may at the direction of the City and County also be invested and reinvested in Investment Securities, maturing in the amounts and times as set forth in the Bond Resolution. All income from all Refunded Municipal Obligations and Investment Securities in the hands of the Paying Agents which is not required for the payment of the Bonds and interest and premium thereon with respect to which such moneys shall have been so deposited, shall be paid to the City and County for deposit in the Sewer Fund free and clear of any trust, lien, security interest, pledge or assignment securing any Bonds or otherwise existing under the Bond Resolution.

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

If moneys, Refunded Municipal Obligations or Investment Securities have been deposited or set aside with a Paying Agent pursuant to the Bond Resolution for the payment of a specific Bond and such Bond is deemed to have been paid and to be no longer Outstanding under the Bond Resolution as provided in the defeasance provisions of the Bond Resolution, but such Bond has not in fact been actually paid in full, no amendment to the defeasance provisions of the Bond Resolution may be made without the consent of the Holder of each Bond affected thereby.

The City and County may at any time surrender to a Paying Agent for a Series of Bonds for cancellation by it any Bonds of such Series previously executed and delivered, which the City and County may have acquired in any manner whatever, and such Bonds upon such surrender for cancellation shall be deemed to be paid and no longer Outstanding under the Bond Resolution.

Appendix D

Proposed Form of Continuing Disclosure [Excluding signatures and exhibit to Master Certificate]

MASTER CERTIFICATE OF THE DIRECTOR OF BUDGET AND FISCAL SERVICES OF THE CITY AND COUNTY OF HONOLULU, HAWAII, PROVIDING FOR CONTINUING DISCLOSURE

I, the undersigned, Roy K. Amemiya, Jr., being the duly appointed Director of Budget and Fiscal Services (the "Director") of the City and County of Honolulu, Hawaii (the "City and County"), DO HEREBY CERTIFY as follows:

ARTICLE I PURPOSE AND DEFINITIONS

Section 1.1. *Purpose.* This Certificate shall constitute a written undertaking for the benefit of the Holders of the Bonds, and is being executed and delivered solely to assist the Underwriters in complying with subsection (b)(5) of the Rule.

Section 1.2. *Definitions.* The following terms used in this Certificate shall have the following respective meanings:

"*Annual Financial Information*" means, collectively, (i) the financial information and operating data with respect to the Department for each fiscal year of the Department of the type included in the Series 1998 Official Statement of the City and County under the headings "FINANCIAL STATEMENTS," and "PENDING LITIGATION;" and (ii) the information regarding amendments to this Certificate required pursuant to Sections 3.2(c) and (d) of this Certificate. Audited Financial Statements, if available, or Unaudited Financial Statements shall be included in the Annual Financial Information as described in Section 2.1(c) of this Certificate.

The descriptions contained in clause (i) above 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.

"*Audited Financial Statements*" means the annual financial statements, if any, of the Department, audited by such auditor as shall then be required or permitted by State law or the Charter of the City and County. Audited Financial Statements shall be prepared in accordance with GAAP; *provided, however*, that the Department may from time to time, if required by federal or State legal requirements, modify the accounting principles to be followed in preparing its financial statements. The notice of any such modification required by Section 3.2(d) of this Certificate shall include a reference to the specific federal or State law or regulation describing such accounting principles. Prior to the fiscal year ending June 30, 1999, Audited Financial Statements of the Department means the extracts of the audited financial statements of the City and County relating to the Sewer Fund and the Wastewater System Facility Charge Fund.

"*Beneficial Owner*" means any person who (i) has the power, directly or indirectly, to vote or consent with respect to, or dispose of ownership of, any Bonds (including a person who holds Bonds through a nominee, depository or other intermediary), or (ii) is treated as the owner of any Bonds for federal income tax purposes.

"*Bonds*" means any revenue bonds issued by the City and County under and pursuant to Resolution No. 98-195 duly adopted by the City Council of the City and County on November 10, 1998 and identified in a Series Certificate.

“*Counsel*” means Hawkins, Delafield & Wood or other nationally recognized bond counsel or counsel expert in federal securities laws.

“*Department*” means the Department of Environmental Services of the City and County.

“*Director*” means any duly appointed Director of Budget and Fiscal Services of the City and County.

“*GAAP*” means generally accepted accounting principles as prescribed from time to time for governmental units by the Governmental Accounting Standards Board.

“*Holder*” means any person who shall be the registered owner, or his duly authorized attorney-in-fact, representative or assign, of any Bond.

“*Material Event*” means any of the following events with respect to the Bonds, whether relating to the Department or otherwise, if material:

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

“*Material Event Notice*” means notice of a Material Event.

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

“*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. The NRMSIRs as of the date of this Certificate are Bloomberg L.P. (Princeton, NJ), Disclosure, Inc. (Bethesda, MD), Kenny Information Systems (New York, NY), Moody’s Investors Service (New York, NY), and Thomson Municipal Services Inc. (New York, NY). Filing information relating to such NRMSIRs is set forth in Exhibit A hereto.

“*Official Statement*” means the “final official statement,” as defined in paragraph (f)(3) of the Rule.

“*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 Certificate, including any official interpretations thereof issued either before or after the effective date of this Certificate which are applicable to this Certificate.

“*SEC*” means the United States Securities and Exchange Commission.

“*Series Certificate*” means any certificate executed by the Director as described in Section 3.3 of this Certificate extending the benefits of this Certificate to the Beneficial Owners, Holders and Underwriters of Bonds of a Series.

“*Series 1998 Official Statement*” means the Official Statement of the City and County relating to its Wastewater System Revenue Bonds (Second Bond Resolution), Junior Series 1998.

“*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 Certificate, there is no SID.

“*State*” means the State of Hawaii.

“*Supplemental Certificate*” means any certificate executed by the Director as described in Section 3.2 of this Certificate amending the provisions of this Certificate.

“*Unaudited Financial Statements*” means the same as Audited Financial Statements, except that they shall not have been audited.

“*Underwriter*” means any original underwriter of a Series of Bonds who is required to comply with the Rule and who is identified in a Series Certificate.

ARTICLE II THE UNDERTAKING

Section 2.1. *Annual Financial Information.* (a) The City and County shall provide Annual Financial Information with respect to each fiscal year of the Department, commencing with the fiscal year ending June 30, 1998, by no later than eight months after the end of the respective fiscal year, to each NRMSIR and the SID. The City and County may provide 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. The Department may provide Annual Financial Information in one document or multiple documents comprising a package, and at one time or in part from time to time.

(b) The City and County shall provide, in a timely manner, notice of any failure of the City and County 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.

(c) If Audited Financial Statements are not provided as part of Annual Financial Information by the date required by Section 2.1(a) of this Certificate, the City and County shall provide (i) as part of the Annual Financial Information, Unaudited Financial Statements in a format similar to the unaudited financial statements contained in the Series 1998 Official Statement under the heading “FINANCIAL STATEMENTS,” and (ii) Audited Financial Statements, when and if available, to each NRMSIR and the SID.

(d) The Department’s current fiscal year is July 1 of a calendar year to June 30 of the succeeding calendar year. The City and County promptly notify (i) each NRMSIR, and (ii) the SID of each change in its fiscal year.

Section 2.2. *Material Event Notices.* (a) If a Material Event occurs, the City and County shall provide, in a timely manner, a Material Event Notice to (i) either the MSRB or each NRMSIR, and (ii) the SID.

(b) Upon any legal defeasance of any Bonds of a Series, the City and County shall provide notice of such defeasance to (i) each NRMSIR or the MSRB and (ii) the SID, which notice shall state whether such Bonds have been defeased to maturity or to redemption and the timing of such maturity or redemption.

(c) Each Material Event Notice shall be so captioned and shall prominently state the title, date and CUSIP numbers of the Bonds.

Section 2.3. *Additional Disclosure Obligations.* The City and County 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 Department, and that under some circumstances compliance with this Certificate, without additional disclosures or other action, may not fully discharge all duties and obligations of the Department under such laws.

Section 2.4. *Additional Information.* Nothing in this Certificate shall be deemed to prevent the City and County from disseminating any other information, using the means of dissemination set forth in this Certificate or any other means of communication, or including any other information in any Annual Financial Information or Material Event Notice, in addition to that which is required by this Certificate. If the City and County chooses to include any information in any Annual Financial Information or Material Event Notice in addition to that which is specifically required by this Certificate, the City and County shall have no obligation under this Certificate to update such information or include it in any future Annual Financial Information or Material Event Notice.

Section 2.5. *No Previous Non-Compliance.* The City and County represents that 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.

Section 2.6. *Transmission of Information and Notices.* Unless otherwise required by law and, in the City and County's sole determination, subject to technical and economic feasibility, the City and County shall employ such methods of information and notice transmission as shall be requested or recommended by the herein-designated recipients of the Department's information and notices.

ARTICLE III TERMINATION, AMENDMENT, ENFORCEMENT, BENEFICIARIES AND DISSEMINATION AGENT

Section 3.1. *Termination.* (a) The City and County's obligations under this Certificate with respect to the Bonds shall terminate upon (i) a prior redemption or payment in full of all of the Bonds of such Series, or (ii) a legal defeasance of all of the Bonds of such Series.

(b) This Certificate, or any provision of this Certificate, shall be null and void in the event that there is delivered (i) to Director an opinion of Counsel, addressed to the City and County, to the effect that those portions of the Rule which require this Certificate, or any of the provisions of this Certificate, respectively, do not or no longer apply to the Bonds, whether because such portions of the Rule are invalid, have been repealed, or otherwise, as shall be specified in such opinion, and (2) copies of such opinion to each NRMSIR and the SID.

Section 3.2. *Amendment.* (a) This Certificate may be amended by a Supplemental Certificate of the Director, without the consent of the Holders of the Bonds, 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 Department or the type of business conducted thereby;

(2) this Certificate as so amended would have complied with the requirements of the Rule as of the date of this Certificate, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances;

(3) there shall have been delivered to the Director, an opinion of Counsel, addressed to the City and County, to the same effect as set forth in clause (2) above;

(4) there shall have been delivered to the Director, an opinion of Counsel or a determination by a person, in each case unaffiliated with the City and County (such as bond counsel) and acceptable to the City and County, addressed to the City and County, to the effect that the amendment does not materially impair the interests of the Holders of the Bonds; and

(5) the City and County shall have delivered copies of such opinion(s) and amendment to each NRMSIR and the SID.

(b) In addition to subsection (a) above, this Certificate may be amended and any provision of this Certificate may be waived by a Supplemental Certificate of the Director, 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 Certificate which is applicable to this Certificate, (2) there shall have been delivered to the Director an opinion of Counsel, addressed to the City and County, to the effect that performance by the City and County under this Certificate as so amended or giving effect to such waiver, as the case may be, will not result in a violation of the Rule as amended or officially interpreted and (3) the City and County shall have delivered copies of such opinion and amendment to each NRMSIR and the SID.

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

(d) If an amendment is made to the accounting principles to be followed in preparing financial statements, the Annual Financial Information for the 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. Notice of such amendment shall be provided by the City and County to (i) either the MSRB or each NRMSIR and (ii) the SID.

Section 3.3. *Benefit; Third-Party Beneficiaries; Enforcement.* (a) By execution of a Series Certificate identifying the Underwriters and the Bonds of a Series, the provisions of this Certificate shall inure solely to the benefit of such Underwriters and the Holders from time to time of such Bonds. Beneficial Owners of such Bonds shall be third party beneficiaries of this Certificate.

(b) Except as provided in this subsection (b), the provisions of this Certificate shall create no rights in any person or entity. The obligations of the City and County to comply with the provisions of this Certificate shall be enforceable by any Holder of outstanding Bonds; *provided, however*, that such right to enforce the provisions of this Certificate shall be limited solely to a right, by action in mandamus or for specific performance, to compel performance of the City and County's obligations under this Certificate. In consideration of the third-party beneficiary status of Beneficial Owners of Bonds pursuant to subsection (a) of this Section, Beneficial Owners shall be deemed to be Holders of Bonds for purposes of this subsection (b).

(c) Any failure by the City and County to perform in accordance with this Certificate shall not constitute a default under any ordinance or resolution of the City and County authorizing the Bonds of any Series or any certificate of the Director providing for the issuance of the Bond of a Series.

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

Section 3.4. *Dissemination Agent.* The Director, on behalf of the Department, shall disseminate the Annual Financial Information, the Audited Financial Statements, the Unaudited Financial Statements, the Material Event Notices and all other information and notices as described in this Certificate. The Director may appoint one or more agents to disseminate such information and notices.

Dated this 23rd day of December, 1998.

SERIES CERTIFICATE OF THE DIRECTOR OF BUDGET AND FISCAL SERVICES OF THE
CITY AND COUNTY OF HONOLULU, PROVIDING FOR CONTINUING DISCLOSURE

I, the undersigned, _____, being the duly appointed Director of Budget and Fiscal Services (the "Director") of the City and County of Honolulu (the "City and County"), DO HEREBY CERTIFY that: (i) this Certificate is a Series Certificate as defined in Section 1.1 and described in Section 3.3 of the Master Certificate of the Director of Budget and Fiscal Services of the City and County of Honolulu, Hawaii, Providing for Continuing Disclosure, dated December 23, 1998 (the "Master Certificate"); (ii) UBS PaineWebber Inc. and Citigroup Global Markets Inc., as the Underwriters of the \$_____ Wastewater System Revenue Bonds (Second Bond Resolution), Junior Series 2003A and 2003B of the City and County, dated the date of initial issuance there of (the "Series 2003 Bonds"), shall be beneficiaries of the Master Certificate; (iii) the Holders of the Series 2003 Bonds shall also be beneficiaries of the Master Certificate; (iv) the Beneficial Owners of Series 2003 Bonds shall be third-party beneficiaries of the Master Certificate; and (v) all capitalized terms used herein shall have the respective meanings as defined in the Master Certificate.

The NRMSIRs as of the date of this Series Certificate are set forth at:

www.sec.gov/info/municipal/nrmsir.htm.

Dated this _____, 2003.

Director of Budget and Fiscal Services
City and County of Honolulu

The above and foregoing certificate
is hereby approved as to form and legality
this _____, 2003.

Corporation Counsel
City and County of Honolulu

Appendix E

Proposed Form of Opinion of Bond Counsel

[Closing Date]

City and County of Honolulu
Honolulu, Hawaii

Re: City and County of Honolulu Wastewater System Revenue Bonds
(Second Bond Resolution) Junior Series 2003A and Junior Series 2003B
(Final Opinion)

Ladies and Gentlemen:

We have acted as bond counsel in connection with the issuance by the City and County of Honolulu (the "City and County") of \$109,200,000 aggregate principal amount of Wastewater System Revenue Bonds (Second Bond Resolution) Junior Series 2003A and \$109,200,000 aggregate principal amount of Wastewater System Revenue Bonds (Second Bond Resolution) Junior Series 2003B (collectively, the "Bonds"), pursuant to the provisions of Chapter 49, Hawaii Revised Statutes (the "Act"), the City Charter, a Bond Resolution and a Series Resolution of the City and County (collectively, the "Resolution"), and a Series Certificate of the Director of Budget and Fiscal Services of the City and County (the "Certificate"). Terms not otherwise defined herein shall have the meanings assigned to them in the Certificate.

In such connection, we have reviewed the Resolution, the Certificate, the Tax Certificate of the City and County, dated the date hereof (the "Tax Certificate"), an opinion of the Corporation Counsel of the City and County, certificates of the City and County and others, and such other documents, opinions and matters to the extent we deemed necessary to render the opinions set forth herein.

Certain agreements, requirements and procedures contained or referred to in the Resolution, the Certificate, the Tax Certificate and other relevant documents may be changed and certain actions may be taken or omitted under the circumstances and subject to the terms and conditions set forth in such documents (including, without limitation, refunding of the Bonds). No opinion is expressed herein as to any Bond or the interest thereon if any such change occurs or action is taken or omitted upon the advice or approval of counsel other than ourselves.

The opinions expressed herein are based on an analysis of existing laws, regulations, rulings and court decisions and cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken or omitted or events occurring after the date hereof. We have not undertaken to determine, or to inform any person, whether any such actions are taken or omitted or events do occur or any other matters come to our attention after the date hereof. Our engagement with respect to the Bonds has concluded with their issuance, and we disclaim any obligation to update this letter. We have assumed the genuineness of all documents and signatures presented to us (whether as originals or as copies) and the due and legal execution and delivery thereof by, and validity against, any parties other than the City and County. We have assumed, without undertaking to verify, the accuracy of the factual matters represented, warranted or certified in the documents, and of the legal conclusions contained in the opinions, referred to in the second paragraph hereof. Furthermore, we have assumed compliance with all covenants and agreements contained in the Resolution, the Certificate and the Tax Certificate, including (without limitation) covenants and agreements compliance with which is necessary to assure that future actions, omissions or events will not cause interest on the Bonds to be included in gross income for federal income tax purposes. We call attention to the fact that the rights and obligations under the Bonds, the Resolution, the Certificate and the Tax Certificate and their enforceability may be subject to bankruptcy, insolvency, reorganization, arrangement, fraudulent conveyance, moratorium and other laws relating to or affecting creditors' rights, to the application of equitable principles, to the exercise of judicial discretion in appropriate cases, and to the limitations on legal remedies against counties in the State of Hawaii. We express no opinion with respect to any indemnification, contribution, penalty, choice of law, choice of forum or waiver provisions contained in the

foregoing documents. Finally, we undertake no responsibility for the accuracy, completeness or fairness of any official statement or other offering material relating to the Bonds and express no opinion with respect thereto.

Based on and subject to the foregoing, and in reliance thereon, as of the date hereof, we are of the following opinions:

1. The Bonds constitute valid and binding special obligations of the City and County.
2. The Bonds are payable solely from and are secured by the Net Revenues and other funds pledged to the payment thereof pursuant to the Resolution, subject to the provisions of the Resolution permitting the application thereof for the purposes and on the terms and conditions set forth in the Resolution.
3. The Resolution has been duly adopted and constitutes the valid and binding obligation of the City and County, and the Certificate has been duly executed and delivered and constitutes the valid and binding obligation of the City and County.
4. Interest on the Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, and the Bonds and the income therefrom are exempt from all taxation by the State of Hawaii or any county or other political subdivision thereof, except inheritance, transfer, estate and certain franchise taxes. Interest on the Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum taxes, although we observe that it is included in adjusted current earnings when calculating corporate alternative minimum taxable income. We express no opinion regarding other tax consequences related to the ownership or disposition of, or the accrual or receipt of interest on, the Bonds.

Respectfully submitted,

ORRICK, HERRINGTON & SUTCLIFFE LLP

per

Appendix F

Specimen Bond Insurance Policy

FINANCIAL GUARANTY INSURANCE POLICY

MBIA Insurance Corporation

Armonk, New York 10504

Policy No. [NUMBER]

MBIA Insurance Corporation (the "Insurer"), in consideration of the payment of the premium and subject to the terms of this policy, hereby unconditionally and irrevocably guarantees to any owner, as hereinafter defined, of the following described obligations, the full and complete payment required to be made by or on behalf of the Issuer to [PAYING AGENT/TRUSTEE] or its successor (the "Paying Agent") of an amount equal to (i) the principal of (either at the stated maturity or by any advancement of maturity pursuant to a mandatory sinking fund payment) and interest on, the Obligations (as that term is defined below) as such payments shall become due but shall not be so paid (except that in the event of any acceleration of the due date of such principal by reason of mandatory or optional redemption or acceleration resulting from default or otherwise, other than any advancement of maturity pursuant to a mandatory sinking fund payment, the payments guaranteed hereby shall be made in such amounts and at such times as such payments of principal would have been due had there not been any such acceleration); and (ii) the reimbursement of a such payment which is subsequently recovered from any owner pursuant to a final judgment by a court of competent jurisdiction that such payment constitutes an avoidable preference to such owner within the meaning of any applicable bankruptcy law. The amounts referred to in clauses (i) and (ii) of the preceding sentence shall be referred to herein collectively as the "Insured Amounts." "Obligations" shall mean:

[PAR]

[LEGAL NAME OF ISSUE]

Upon receipt of telephonic or telegraphic notice, such notice subsequently confirmed in writing by registered or certified mail, or upon receipt of written notice by registered or certified mail, by the Insurer from the Paying Agent or any owner of an Obligation the payment of an Insured Amount for which is then due, that such required payment has not been made, the Insurer on the due date of such payment or within one business day after receipt of notice of such nonpayment, whichever is later, will make a deposit of funds, in an account with U.S. Bank Trust National Association, in New York, New York, or its successor, sufficient for the payment of any such Insured Amounts which are then due. Upon presentment and surrender of such Obligations or presentment of such other proof of ownership of the Obligations, together with any appropriate instruments of assignment to evidence the assignment of the Insured Amounts due on the Obligations as are paid by the Insurer, and appropriate instruments to effect the appointment of the Insurer as agent for such owners of the Obligations in any legal proceeding related to payment of Insured Amounts on the Obligations, such instruments being in a form satisfactory to U.S. Bank Trust National Association, U.S. Bank Trust National Association shall disburse to such owners, or the Paying Agent payment of the Insured Amounts due on such Obligations, less any amount held by the Paying Agent for the payment of such Insured Amounts and legally available therefor. This policy does not insure against loss of any prepayment premium which may at any time be payable with respect to any Obligation.

As used herein, the term "owner" shall mean the registered owner of any Obligation as indicated in the books maintained by the Paying Agent, the Issuer, or any designee of the Issuer for such purpose. The term owner shall not include the Issuer or any party whose agreement with the Issuer constitutes the underlying security for the Obligations.

Any service of process on the Insurer may be made to the Insurer at its offices located at 113 King Street, Armonk, New York 10504 and such service of process shall be valid and binding.

This policy is non-cancellable for any reason. The premium on this policy is not refundable for any reason including the payment prior to maturity of the Obligations.

In the event the Insurer were to become insolvent, any claims arising under a policy of financial guaranty insurance are excluded from coverage by the California Insurance Guaranty Association, established pursuant to Article 14.2 (commencing with Section 1063) of Chapter 1 of Part 2 of Division 1 of the California Insurance Code.

IN WITNESS WHEREOF, the Insurer has caused this policy to be executed in facsimile on its behalf by its duly authorized officers, this [DAY] day of [MONTH, YEAR].

MBIA Insurance Corporation

President

Attest:

Assistant Secretary

