

In the opinion of Bond Counsel, assuming compliance with the provisions of the Internal Revenue Code of 1986, as amended (the "Code"), as described herein, and subject to the conditions described in "TAX MATTERS" herein, interest on the Series 2003 Bonds will not be includable in the gross income of the owners thereof for federal income tax purposes under existing law. The District's Enabling Act provides that the Series 2003 Bonds, their transfer and the income therefrom, including any profit made on the sale thereof, shall be exempt from taxation by the Commonwealth of Virginia and by any political subdivision thereof. See "TAX MATTERS" herein for certain provisions regarding the Code that may affect the tax treatment of interest on the Series 2003 Bonds for certain bondholders.

\$55,890,000

Hampton Roads Sanitation District, Virginia Wastewater Refunding Revenue Bonds, Series 2003

Dated: Date of Issue

Due: October 1, as shown below

The Series 2003 Bonds are being issued under a Trust Agreement between the District and The Bank of New York, New York, New York, as trustee (the "Bond Trustee"), for the purpose of refunding all of the District's outstanding Wastewater Refunding and Capital Improvement Revenue Bonds, Series 1993.

The Series 2003 Bonds are issuable as registered bonds without coupons and will be initially registered only in the name of Cede & Co., as nominee of The Depository Trust Company, New York, New York ("DTC"), serving as securities depository for the Series 2003 Bonds. The Series 2003 Bonds will be available to purchasers in denominations of \$5,000 and any whole multiple thereof only under the book-entry system maintained by DTC through brokers and dealers which are, or which act through, DTC Participants. Principal and interest will be paid by the Bond Trustee as bond registrar to DTC or its nominee which will remit the payments to the DTC Participants for subsequent disbursement. See "THE SERIES 2003 BONDS-Book-Entry Only System" herein. Interest on the Series 2003 Bonds is payable semiannually on each April 1 and October 1, commencing April 1, 2004.

The Series 2003 Bonds are not subject to optional redemption prior to their respective maturities.

THE SERIES 2003 BONDS ARE SPECIAL OBLIGATIONS OF THE DISTRICT PAYABLE SOLELY FROM MONIES PAID BY THE MEMBERS OF THE OBLIGATED GROUP ON OBLIGATION NO. 2 AND THE NET REVENUES AND OTHER FUNDS PLEDGED TO SECURE THE SERIES 2003 BONDS UNDER THE TRUST AGREEMENT OR OBLIGATION NO. 2 UNDER THE MASTER INDENTURE. THE SERIES 2003 BONDS SHALL NOT BE DEEMED TO CONSTITUTE A DEBT, OR A PLEDGE OF THE FAITH AND CREDIT, OF THE COMMONWEALTH OF VIRGINIA OR OF ANY COUNTY, CITY, TOWN OR POLITICAL SUBDIVISION THEREOF. THE ISSUANCE OF THE SERIES 2003 BONDS SHALL NOT DIRECTLY OR INDIRECTLY OR CONTINGENTLY OBLIGATE THE COMMONWEALTH OF VIRGINIA OR ANY COUNTY, CITY, TOWN OR POLITICAL SUBDIVISION THEREOF TO LEVY OR TO PLEDGE ANY FORM OF TAXATION WHATEVER THEREFOR.

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

MATURITIES, AMOUNTS, INTEREST RATES AND YIELDS

Base CUSIP Number: 409327

<u>Year</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield</u>	<u>CUSIP Suffix</u>	<u>Year</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield</u>	<u>CUSIP Suffix</u>
2004	\$5,925,000	2.000%	1.08%	BC6	2010	\$3,845,000	5.000%	2.95%	BJ1
2005	6,950,000	4.000	1.25	BD4	2011	4,010,000	3.375	3.23	BK8
2006	7,160,000	2.625	1.60	BE2	2012	4,150,000	3.500	3.46	BL6
2007	3,390,000	2.750	1.95	BF9	2013	4,295,000	3.500	3.58	BM4
2008	3,470,000	2.750	2.30	BG7	2014	4,460,000	4.000	3.70	BN2
2009	3,590,000	5.000	2.66	BH5	2015	4,645,000	4.000	3.82	BP7

The Series 2003 Bonds are offered when, as and if issued, subject to the approving opinion of Sidley Austin Brown & Wood LLP, New York, New York, Bond Counsel, and to certain other conditions. It is expected that the Series 2003 Bonds will be available for delivery to The Depository Trust Company in New York, New York, on or about December 10, 2003.

HAMPTON ROADS SANITATION DISTRICT

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Associate Counsel

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Independent Accountants

BB&T CAPITAL MARKETS,
a division of Scott & Stringfellow, Inc.
Financial Advisor

SIDLEY AUSTIN BROWN & WOOD LLP
Bond Counsel

THE BANK OF NEW YORK
Master Trustee, Bond Trustee and Bond Registrar

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

The Series 2003 Bonds are exempt from registration under the Securities Act of 1933, as amended. As obligations of a political subdivision of the Commonwealth of Virginia, the Series 2003 Bonds are also exempt from registration under the securities laws of Virginia.

No dealer, salesman or any other person who has been authorized to give any information or to make any representation, other than the information and representations contained herein, in connection with the offering of the Series 2003 Bonds, and, if given or made, such information or representations must not be relied upon. This Official Statement does not constitute an offer to sell or solicitation of an offer to buy any of the Series 2003 Bonds in any jurisdiction to any person to whom it is unlawful to make such offer or solicitation in such jurisdiction.

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Official Statement

Hampton Roads Sanitation District, Virginia

Relating to its \$55,890,000 Wastewater Refunding Revenue Bonds, Series 2003

INTRODUCTION

The purpose of this Official Statement, which includes the cover page hereof, the map and the appendices hereto, is to set forth information concerning the Hampton Roads Sanitation District (the "District" or "HRSD") and the District's \$55,890,000 Wastewater Refunding Revenue Bonds, Series 2003 (the "Series 2003 Bonds").

There follows in this Official Statement a brief description of the Series 2003 Bonds and the District, including its service area, governance and information regarding its operations and finances. Appendices A and B contain additional information regarding the District's operations and financial condition.

AUTHORIZATION

The Series 2003 Bonds are being issued in accordance with the provisions of Chapter 66 of the Acts of Assembly of Virginia of 1960, as amended (the "Enabling Act"). The Hampton Roads Sanitation District Commission (the "Commission") on October 28, 2003 authorized by resolution the issuance of the Series 2003 Bonds. The Series 2003 Bonds are issued under a Trust Agreement, dated as of December 1, 2003, by and between the District and The Bank of New York, New York, New York, as trustee (the "Bond Trustee"). The Series 2003 Bonds are special obligations of the District payable solely from certain revenues and other funds pledged to secure the Series 2003 Bonds under the Trust Agreement or Obligation No. 2 ("Obligation No. 2"), issued under a Master Trust Indenture, dated as of December 1, 1993, as amended (the "Master Indenture"), by and between the District and The Bank of New York, New York, New York, as successor trustee (the "Master Trustee"), and from moneys paid by the Members of the Obligated Group (as defined in the Master Indenture) on Obligation No. 2. The District will also enter into a Supplemental Indenture for Obligation No. 2, dated as of December 1, 2003, with the Master Trustee, providing for the issuance of Obligation No. 2. Obligation No. 2 will be issued and delivered to the Bond Trustee upon the delivery of the Series 2003 Bonds.

Currently, the District is the only Member of the Obligated Group, and the District's obligations under the Master Indenture and Obligation No. 2 will not be general obligations of the District but will be limited as to payment to Net Revenues (defined herein) derived from certain property operated by the District as its Wastewater System (the "Wastewater System"). See "SECURITY AND SOURCE OF PAYMENT" herein.

PURPOSE AND REFUNDING PLAN

Proceeds of the Series 2003 Bonds will be used to (a) refund all of the District's Wastewater Refunding and Capital Improvement Revenue Bonds, Series 1993, outstanding in the aggregate principal amount of \$57,205,000 (the "Refunded Bonds") and (b) pay the costs of issuing the Series 2003 Bonds. The District will realize from the refunding a reduction in its total and present value aggregate debt service requirements and at the

same time shorten the final maturity of its revenue bonds from October 1, 2023 (the final maturity of the Refunded Bonds) to October 1, 2015 (the final maturity of the Series 2003 Bonds).

The District will deposit a portion of the proceeds of the Series 2003 Bonds and other available funds of the District in an escrow account (the "Escrow Fund") established by the District with The Bank of New York, New York, New York, as bond trustee (the "Series 1993 Bond Trustee"). The proceeds and other available funds will be invested in United States Treasury Obligations (the "Federal Securities") that mature in amounts and pay interest at rates sufficient to pay, when due, the principal of and a 2% redemption premium, and accrued interest through their redemption date, on the Refunded Bonds. The Refunded Bonds will be called for redemption on December 19, 2003. Upon the deposit of the Federal Securities and cash to the Escrow Fund, the Refunded Bonds will no longer have any lien on the revenues of the District. Neither the principal of nor the interest on the Federal Securities held in the Escrow Fund will be available to pay debt service on the Series 2003 Bonds.

The sufficiency of the maturing principal and interest on the Federal Securities and the uninvested cash deposited in the Escrow Fund to pay the principal, redemption premium and accrued interest on the Refunded Bonds on their redemption date will be verified by McGladrey & Pullen, LLP. See "VERIFICATION OF MATHEMATICAL COMPUTATIONS" herein.

SOURCES AND USES OF FUNDS

The estimated sources and uses of funds in connection with the refunding are as follows:

Sources

Bond Proceeds	\$55,890,000
Net Original Issue Premium.....	1,906,850
District Funds.....	1,503,602
Escrow Fund Earnings	9,000
Total Sources	<u>\$59,309,452</u>

Uses

Deposit to the Escrow Fund.....	\$58,963,700
Issuance Expenses(1).....	345,752
Total Uses	<u>\$59,309,452</u>

(1) Includes underwriting discount.

THE SERIES 2003 BONDS

Description

The Series 2003 Bonds will be dated, bear interest and mature as set forth on the cover page of this Official Statement. The Series 2003 Bonds are issuable as registered bonds without coupons in the denomination of \$5,000 or any whole multiple thereof as provided in the Trust Agreement. Interest will be payable semiannually on April 1 and October 1, the first interest payment being due April 1, 2004. The principal of and the interest on the Series 2003 Bonds will be payable as described below under "Book-Entry Only System."

Book-Entry Only 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 registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered bond certificate will be issued for each maturity of the Series 2003 Bonds and will be deposited with DTC.

DTC, the world's largest depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provision of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation, (NSCC, GSCC, MBSCC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

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 (the "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. Beneficial Owners are, however, 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 Direct and Indirect 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 Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorized representative of DTC. The deposit of Series 2003 Bonds with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any 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 Direct and Indirect 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.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Series 2003 Bonds unless authorized by a Direct Participant in accordance with DTC's procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the District 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, premium, if any, and interest payments on the Series 2003 Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the District on the payable date in accordance with their respective holdings shown on DTC's records. 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 nor its nominee, or the District, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal, premium, if any, and interest to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the District, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

The information in this section concerning DTC and DTC's book-entry system has been obtained from sources that the District believes to be reliable, but the District takes no responsibility for the accuracy thereof.

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

The District may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, certificates for the Series 2003 Bonds will be printed and delivered.

Redemption Provisions

The Series 2003 Bonds are not subject to redemption at the option of the District prior to their respective maturities.

SECURITY AND SOURCE OF PAYMENT

THE SERIES 2003 BONDS ARE SPECIAL OBLIGATIONS OF THE DISTRICT PAYABLE SOLELY FROM MONEYS PAID BY THE MEMBERS OF THE OBLIGATED GROUP ON OBLIGATION NO. 2 AND THE NET REVENUES AND OTHER FUNDS PLEDGED TO SECURE THE SERIES 2003 BONDS UNDER THE TRUST AGREEMENT OR OBLIGATION NO. 2 UNDER THE MASTER INDENTURE. THE SERIES 2003 BONDS SHALL NOT BE DEEMED TO CONSTITUTE A DEBT, OR A PLEDGE OF THE FAITH AND CREDIT, OF THE COMMONWEALTH OF VIRGINIA OR OF ANY COUNTY, CITY, TOWN OR POLITICAL SUBDIVISION THEREOF. THE ISSUANCE OF THE SERIES 2003 BONDS SHALL NOT DIRECTLY OR INDIRECTLY OR CONTINGENTLY OBLIGATE THE COMMONWEALTH OF VIRGINIA OR ANY COUNTY, CITY, TOWN OR POLITICAL SUBDIVISION THEREOF TO LEVY OR TO PLEDGE ANY FORM OF TAXATION WHATEVER THEREFOR.

General

Principal of and interest on the Series 2003 Bonds will be payable from moneys paid by the District pursuant to the Trust Agreement and the Obligated Group pursuant to Obligation No. 2. Payment of Obligation No. 2 will be the joint and several special obligation under the Master Indenture of each Member of the Obligated Group.

With respect to any Member of the Obligated Group that is a Governmental Entity (a "Governmental Member of the Obligated Group"), including the District, any actions, payments, covenants, obligations or other things to be done or performed under the Master Indenture will be based upon the use of the property of a Designated Unit (as defined below) of such Governmental Member of the Obligated Group and not the property of the Governmental Member of the Obligated Group generally and any Obligation issued pursuant to the Master Indenture will be payable solely from the Net Revenues of such Designated Unit. The term "Designated Unit" means any enterprise owned and operated by a Governmental Member of the Obligated Group which has been designated as a Designated Unit under the provisions of the Master Indenture.

Currently, the District is the only Member of the Obligated Group and the Wastewater System is the only Designated Unit under the Master Indenture. Obligation No. 2 and the District's obligations under the Trust

Agreement will be special obligations, limited as to payment to Net Revenues of the Wastewater System of the District.

To the extent permitted by law, the Master Indenture permits any Person which is not a Member of the Obligated Group to become a Member of the Obligated Group upon compliance with certain financial and other requirements. The Master Indenture also permits, upon compliance with certain requirements, any Member of the Obligated Group other than the District, to withdraw from the Obligated Group. In addition, to the extent permitted by law, the District may add additional Designated Units and cause any future Designated Unit other than the Wastewater System to cease to be a Designated Unit, subject to compliance with the provisions of the Master Indenture. See "Parties Becoming Members of the Obligated Group," "Operating Units Becoming Designated Units" and "Withdrawal from the Obligated Group; Cessation of Status as Designated Unit" under "SUMMARY OF THE MASTER INDENTURE" in Appendix C.

In the opinion of Bond Counsel to the District, in order for an entity other than the District to become a Member of the Obligated Group or for the District to designate an additional Designated Unit under the Master Indenture other than the Wastewater System, it would be necessary for the Virginia General Assembly to enact legislation.

Pursuant to the Master Indenture, as security for the payment of the amounts due on Obligation No. 2 (and any other Obligations issued under the Master Indenture), each Governmental Member of the Obligated Group will pledge its Net Revenues to the Master Trustee and each Member of the Obligated Group that is not a Governmental Entity will grant a security interest in its Gross Receipts to the Master Trustee. Currently, there is no Member of the Obligated Group that is not a Governmental Entity. "Net Revenues" means all revenues derived by a Governmental Member of the Obligated Group from its Designated Units except such part thereof as may be required to pay the cost of maintaining, repairing and operating such Designated Units. "Gross Receipts" means all revenues, income, receipts and money (other than proceeds of borrowing) received in any period by or on behalf of any Member of the Obligated Group that is not a Governmental Entity. Any such pledge of Net Revenues or security interest in Gross Receipts is subject to Permitted Liens that exist prior to or that may be created subsequent to the time the Series 2003 Bonds are issued.

The realization of amounts to be derived upon the enforcement of any pledge or security interest securing the Series 2003 Bonds will depend upon the exercise of various remedies specified in the Trust Agreement and the Master Indenture. These and other remedies may, in many respects, require judicial action of a nature that is often subject to discretion and delay. Under existing laws the remedies specified in the Trust Agreement and the Master Indenture may not be readily available or may be limited. A court may decide not to order the specific performance of the covenants contained in those documents. The various legal opinions to be delivered concurrently with the delivery of the Series 2003 Bonds will be qualified as to the enforceability of the various legal instruments by limitations imposed by state and federal laws, rulings and decisions affecting remedies and by bankruptcy, fraudulent conveyance, reorganization and other laws affecting the enforcement of creditor's rights generally.

Pursuant to the Master Indenture, the Members of the Obligated Group are subject to covenants under the Master Indenture relating to maintenance of a specified Long-Term Debt Service Coverage Ratio and restricting, among other things, incurrence of Indebtedness, existence of liens on Property, consolidation and merger, disposition of assets, addition of Members to the Obligated Group and withdrawal from the Obligated Group. See "Limitation on Creation of Liens"; "Limitations on Indebtedness"; "Long-Term Debt Service Coverage Ratio"; "Sale, Lease or Other Disposition of Operating Assets; Disposition of Cash and Investments"; "Consolidation, Merger, Sale or Conveyance"; "Parties Becoming Members of the Obligated Group" and "Withdrawal from the Obligated Group; Cessation of Status as Designated Unit" under "SUMMARY OF THE MASTER INDENTURE" in Appendix C.

Additional Indebtedness

THE MASTER INDENTURE PERMITS ANY MEMBER OF THE OBLIGATED GROUP TO ISSUE OR INCUR ADDITIONAL INDEBTEDNESS EVIDENCED BY OBLIGATIONS THAT WILL SHARE THE SECURITY FOR OBLIGATION NO. 2 ON A PARITY WITH OBLIGATION NO. 2. SUCH ADDITIONAL OBLIGATIONS WILL NOT BE SECURED BY THE MONEY OR INVESTMENTS IN ANY FUND OR

ACCOUNT HELD BY THE BOND TRUSTEE FOR THE SECURITY OF THE SERIES 2003 BONDS. See "SUMMARY OF THE MASTER INDENTURE - Indebtedness, Authorization, Issuance and Terms of Obligations" in Appendix C.

Subordinate Obligations

Beginning in 1993, the District has borrowed over \$96.5 million from the Virginia Water Facilities Revolving Fund and issued in evidence of its obligations to repay such loans eleven issues of subordinate obligations under the Master Indenture (collectively, the "Subordinate Bonds"). The terms of the Subordinate Bonds generally state that the lien thereof on the Net Revenues of the District is in all respects subordinate and inferior to the lien thereon of Obligations, including Obligation No. 2, issued under the Master Indenture. Interest accrues on the disbursed principal of the outstanding Subordinate Bonds at interest rates ranging from 2.5% to 4.75% per annum, and principal and interest are payable in installments over the 20-year terms of the loans. The Subordinated Bonds have been issued for various improvements and upgrades at several of the District's treatment plants. See the table "DEBT SERVICE REQUIREMENTS FOR THE SERIES 2003 BONDS AND SUBORDINATE OBLIGATIONS" and "SUMMARY OF THE MASTER INDENTURE - Limitation on Creation of Liens" in Appendix C.

Rate Covenant

In the Master Indenture, each Member of the Obligated Group covenants to set rates and charges for facilities, services and products such that the Income Available for Debt Service for the Obligated Group, calculated at the end of each Fiscal Year, will be not less than the greater of (i) 120% of the Long-Term Debt Service Requirement for all Indebtedness except Subordinated Indebtedness for such Fiscal Year and (ii) 100% of the Long-Term Debt Service Requirement for Indebtedness including Subordinated Indebtedness for such Fiscal Year. For purposes of such covenant, "Income Available for Debt Service" means, with respect to the Obligated Group, the excess of its revenues over expenses before depreciation, amortization and interest expense on Long-Term Indebtedness, as determined in accordance with generally accepted accounting principles consistently applied. "Long-Term Debt Service Requirement" means generally the principal and interest due on Outstanding Long-Term Indebtedness of the Obligated Group during such period. See "SUMMARY OF THE MASTER INDENTURE -Long-Term Debt Service Coverage Ratio" in Appendix C.

Debt Service Reserve Fund

While a Debt Service Reserve Fund is created under the Trust Agreement, the Debt Service Reserve Fund will not be funded when the Series 2003 Bonds are issued. If (a) the Liquidity Ratio (as defined in Appendix C) of the Obligated Group, as calculated based on (i) the Financial Statements of the Obligated Group as of the end of each Fiscal Year or (ii) the unaudited interim financial statements for the first six months of each Fiscal Year, is less than 1.35 or (b) the Long-Term Debt Service Coverage Ratio (as defined in Appendix C) is less than 1.35, the Trust Agreement requires that the District fund, within six (6) months after the end of such Fiscal Year or such six-month period, as applicable, the Debt Service Reserve Fund in an amount equal to the Debt Service Reserve Fund Requirement (as defined in Appendix C). If the Debt Service Reserve Fund is funded as described in the preceding sentence, amounts on deposit therein may be released upon the satisfaction of certain conditions as more fully described under the caption "SUMMARY OF THE TRUST AGREEMENT - Debt Service Reserve Fund; Qualified Reserve Fund Substitute" in Appendix C. Amounts, if any, on deposit in the Debt Service Reserve Fund are required to be transferred to the Bond Fund to the extent necessary to pay interest or principal (whether upon maturity or acceleration) on the Series 2003 Bonds if the money on deposit in the Bond Fund is insufficient for such purpose.

**DEBT SERVICE REQUIREMENTS
FOR THE SERIES 2003 BONDS AND
SUBORDINATE OBLIGATIONS
(\$000)**

Fiscal Year Ending June 30,	Series 2003 Bonds²			Subordinate Bonds Debt Service³	Total Debt Service
	<u>Principal¹</u>	<u>Interest</u>	<u>Debt Service</u>		
2004	\$ -	\$ 598	\$ 598	\$ 7,250	\$ 7,848
2005	5,925	1,881	7,806	7,253	15,059
2006	6,950	1,682	8,632	7,253	15,885
2007	7,160	1,449	8,609	7,255	15,864
2008	3,390	1,309	4,699	7,254	11,953
2009	3,470	1,215	4,685	7,253	11,938
2010	3,590	1,077	4,667	7,250	11,917
2011	3,845	891	4,736	7,249	11,985
2012	4,010	727	4,737	7,248	11,985
2013	4,150	587	4,737	7,245	11,982
2014	4,295	439	4,734	7,249	11,983
2015	4,460	275	4,735	7,247	11,982
2016	4,645	93	4,738	5,987	10,725
2017	-	-	-	3,857	-
2018	-	-	-	1,311	-
2019	-	-	-	1,310	-
2020	-	-	-	1,308	-
2021	-	-	-	823	-
2022	-	-	-	435	-
2023	-	-	-	204	-
2024	-	-	-	-	-
TOTAL	<u>\$55,890</u>	<u>\$12,224</u>	<u>\$ 68,114</u>	<u>\$102,241</u>	<u>\$170,354</u>

¹ Principal is due on October 1 in each of the indicated fiscal years.

² Numbers may not add to totals due to rounding.

³ As of June 30, 2003, \$77,601,000 was the unpaid principal balance of the Subordinate Bonds. See "SECURITY AND SOURCES OF PAYMENT – Subordinate Obligations" herein.

HAMPTON ROADS SANITATION DISTRICT

Authorization and Purpose

The District was created in 1940 by the Virginia General Assembly as a political subdivision of the Commonwealth of Virginia and was established as a governmental instrumentality to provide for the public health and welfare. Chapter 66, Acts of the Assembly of 1960, validated and confirmed prior legislation creating the District and repealed earlier acts of the Virginia General Assembly enacted with respect to the District.

The District was created for the specific purpose of abating pollution in the Hampton Roads area of Virginia through the interception of existing wastewater outfalls, the construction of wastewater treatment facilities and the installation of interceptors throughout the service area. Collection systems consisting of lateral sewers and subtrunk facilities which carry wastewater from industries, homes, apartments and businesses remains the responsibility of the various cities, counties and military establishments within the District.

History

The District traces its origins to 1925 when the Virginia Department of Health condemned a large oyster producing area in Hampton Roads. The closure resulted in the Virginia General Assembly creating in 1927 a "Commission to Investigate and Survey the Seafood Industry of Virginia." Subsequent studies recommended a public body to construct and operate a sewage system in the area.

In 1934, the Virginia General Assembly created the Hampton Roads Sanitation Disposal Commission with instructions to plan the elimination of pollution in Hampton Roads. Recommendations were made to the General Assembly which resulted in the Sanitary Districts Law of 1938, along with "an Act to provide for and create the Hampton Roads Sanitation District." In a referendum held on November 5, 1940, a majority of the voters approved the creation of the District.

The District's first construction project, the Warwick County Trunk Sewer, began on June 26, 1946. The District commenced operations on July 1, 1946 using facilities acquired from the United States Government. The District's first treatment plant, the Army Base Plant, commenced operations on October 14, 1947. Since that time, the facilities of the District have been expanded to provide wastewater treatment service to all major population centers within its boundaries.

The Commission

The District operates under the direction of the Hampton Roads Sanitation District Commission (the "Commission") comprised of eight members appointed by the Governor for staggered terms of four years. Members of the Commission may be reappointed without limitation and may be suspended or removed by the Governor at his pleasure. The Commission annually elects one of its members as Chairman and another as Vice Chairman. The eight members of the Commission must be residents of the cities and counties of the District as follows: one member from each of the cities of Chesapeake, Hampton, Newport News, Norfolk, Portsmouth and Virginia Beach; one member from the City of Suffolk or Isle of Wight County; and one member from the City of Williamsburg or Poquoson, or Gloucester, James City, King William, King and Queen, Mathews, Middlesex, or York County or the Town of Urbanna.

The Commission is empowered, among other things, to (1) construct and to improve, extend, enlarge, reconstruct, maintain, equip, repair and operate a wastewater system or systems, either within or without or partly within and partly without the corporate limits of the District, and to construct wastewater improvements within the corporate limits of the District, (2) issue the District's bonds, payable solely from revenues, to pay all or part of the cost of a wastewater system, (3) fix, revise, charge and collect rates, fees and charges for the use of and for the services of any system operated by the District, (4) enter into contracts with any unit, including counties, cities and other authorities, relating to the furnishing of services of the District, and (5) acquire real or personal property necessary in connection with wastewater systems or wastewater improvements.

The members of the Commission followed by brief resumes are:

<u>Commissioners</u>	<u>Area Represented</u>	<u>Occupation</u>	<u>Term Expires June 7,</u>
William H. Pierce, <i>Chair</i>	City of Chesapeake	Retired military analyst for the U.S. Army	2004
R. Tyler Bland III, <i>Vice Chairman</i>	Cities of Williamsburg and Poquoson, Counties of James City, King William, King and Queen, Mathews, Middlesex and York and Town of Urbanna	Owner, Tidewater Realty	2005
Parris Delazio Carson	City of Suffolk	Retired Assistant Superintendent, Suffolk Public Schools	2005
Richard C. Conti	City of Norfolk	Executive Director, Nauticus	2007
B. Anne Davis	City of Portsmouth	Former President, Diesel Tech, Inc.	2007
Vishnu K. Lakdawala, Ph.D.	City of Virginia Beach	Associate Professor, Electrical and Computer Engineering, Old Dominion University	2006
Judith S. Scott	City of Newport News	General Counsel, Portfolio Recovery Associates, LLC	2006
James H. Shoemaker, Jr.	City of Hampton	Partner, Patten, Wornom, Hatten & Diamondstein, LLC	2004

William H. Pierce, Commission Chair. Mr. Pierce is a retired Senior Management Analyst from HQ Training & Doctrine Command (TRADOC), U.S. Army, Ft. Monroe, Virginia. He has served over 35 years as a Long Range Planner and Management Analyst who specialized in developing engineered manpower standards for an entire function, and is a former member of the Chesapeake City Council. He also served as a commissioner for both the Southeastern Public Service Authority of Virginia and Hampton Roads Transit, and as a member of the State Board of Mental Health, Mental Retardation and Substance Abuse Services. Mr. Pierce is a graduate of Auburn University, with a Master's Degree in Public Administration, and a B.S. degree from Troy State University. His community service includes Chesapeake Council of Civic Organizations, Hampton Roads Coalition of Civic Organizations, Chesapeake Committee on Aging, Chesapeake Committee on Groundwater, South Norfolk Civic League, and Chesapeake General Hospital. Mr. Pierce resides in the City of Chesapeake.

R. Tyler Bland, Commission Vice-Chair. Mr. Bland is the owner of Tidewater Realty, and was previously Mayor of the Town of West Point from 1992 to 1998. Mr. Bland also served on the West Point Town Council from 1990

to 1998. Currently he is a Director of the Bank of Essex and Rappahannock Community College Foundation. Mr. Bland is a graduate of Virginia Military Institute. Mr. Bland resides in the Town of West Point.

James H. Shoemaker, Jr., Commissioner. Mr. Shoemaker is a partner with the law firm of Patten, Wornom, Hatten, and Diamonstein. Mr. Shoemaker served as an officer in the United States Navy and United States Naval Reserve. Mr. Shoemaker is a graduate of Virginia Military Institute and the T.C. Williams School of Law at the University of Richmond. He is the past president and a current trustee of the Sarah Bonwell Hudgins Foundation, an organization dedicated to the well-being of the mentally handicapped. Mr. Shoemaker resides in Hampton.

Parris Delano Carson, Commissioner. Mr. Carson retired in 1997 as Assistant Superintendent for Pupil Personnel and Special Programs for Suffolk Public Schools. During his career, Mr. Carson served as Principal of Nansemond River High School, John F. Kennedy High School, and Smithfield High School. He was also an Assistant Principal and Teacher in Portsmouth's school system. Mr. Carson earned his B.S. degree in Biology from Elizabeth City State University, and a Master of Education degree from Virginia State University. He was named Outstanding Educator of Tidewater in 1991. He currently serves on the Boards of Meals-on-Wheels, Suffolk Even Start, Suffolk Education Foundation, and the Suffolk Community Health Center. Mr. Carson is also a member of the Mayor's Advisory Council on Youth Programs. Mr. Carson resides in the City of Suffolk.

Vishnu K. Lakdawala, Ph. D., Commissioner. Dr. Lakdawala obtained his undergraduate degree in Electrical Engineering from Bangalore University in India in 1972 and his Masters of Engineering Degree in High Voltage Engineering from Indian Institute of Science, India in 1974. He worked as Research and Development Engineer in Jyoti Limited for three years in the high voltage instrument transformers division. He received his Ph.D. in Electrical Engineering from the University of Liverpool, Liverpool, UK in 1980. After serving as Senior Research Associate in the Department of Electrical Engineering and Electronics in the University of Liverpool for a year, he joined Oak Ridge National Laboratory, Oak Ridge, Tennessee where he conducted research in the gaseous dielectrics area for a year. He moved to Norfolk in 1983, joining the Department of Electrical and Computer Engineering as Assistant Professor at Old Dominion University. After serving as the Graduate Program Director in the Department for ten years, he is currently the Chief Departmental Advisor and Associate Professor of Electrical and Computer Engineering. Dr. Lakdawala has published a number of journal and conference papers in the area of electrical insulation and high voltage switches and has three patents in the field of high power opening switches. Dr. Lakdawala resides in the City of Virginia Beach.

Judith S. Scott, Commissioner. Ms. Scott is General Counsel for Portfolio Recovery Associates, LLC, and works in the company's Norfolk Headquarters. She received her undergraduate degree from Virginia State University and her J.D. from Columbus School of Law of the Catholic University of America. Ms. Scott resides in the City of Newport News.

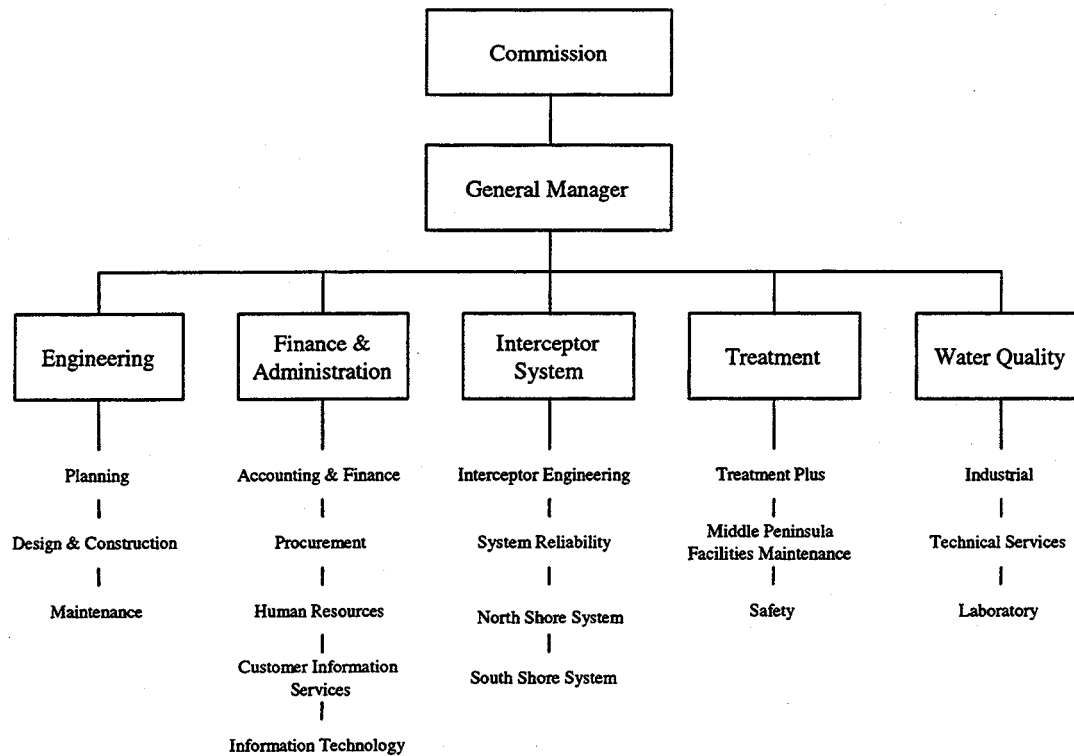
Richard Conti, Commissioner. Richard Conti has been the Executive Director of Nauticus, The National Maritime Center since September 1998. He served as Interim Director of the science and technology center facility in the year leading up to his permanent appointment. Before joining Nauticus, Mr. Conti was an analyst in the Norfolk City Manager's office and worked on numerous special projects and development projects, including the MacArthur Center project. He is a former U.S. Naval Aviator and is a graduate of the Navy Fighter Weapons School (TopGun). Mr. Conti earned a B.S. degree in Business Management from Tulane University and a Master's Degree in Public Administration from the University of Southern California. Mr. Conti resides in the City of Norfolk.

B. Anne Davis, Commissioner. Ms. Davis is the former President and CEO of Diesel Tech, Inc., a certified woman-owned firm specializing in diesel engine repair. The company had national and international experience in the public and private sectors before it closed in December 2002. Prior to founding Diesel Tech Inc., Ms. Davis held senior positions in health care and also has extensive management experience in banking. She currently serves as a senior leader on numerous associations and boards, as well as civic organizations. She is a former Commissioner and past Chairman of both the Portsmouth Industrial Development Authority and the Portsmouth Port and Industrial Commission. Ms. Davis is a resident of the City of Portsmouth.

Management and Staff

The administration of the District is under the control of a General Manager, supported by five directors and their staffs. The District had 681 employees as of June 30, 2003. Current staffing is sufficient to operate all existing facilities. None of its employees is currently represented by a union.

The District is managed through five departments which are organized into functional divisions as follows:



The principal responsibilities of these departments is summarized as follows:

- **Engineering Department**
 - **Construction:** Manages all construction projects
 - **Design:** Manages or provides design and maintenance of current drawings for all facilities
 - **Planning:** Long range facility planning
 - **Maintenance:** Automotive Maintenance, Carpenter, Electrical and Machine Shop operations
- **Finance & Administration**
 - **Accounting & Finance:** Accounting operations and treasury function
 - **Customer Information Services:** Billings, collections, maintenance of customer accounts and liaison with District customers
 - **Information Technology:** Data processing services, system support and management
 - **Human Resources:** Administration of human resources
 - **Procurement:** Acquisition of goods and services
- **Interceptor Systems**
 - **Interceptor Engineering:** Engineering related to maintenance and operation of the interceptor systems
 - **North Shore Operations:** Operates and maintains the interceptor system located in the Cities of Hampton, Newport News, Poquoson and Williamsburg, and the Counties of Gloucester, James City and York
 - **South Shore Operations:** Operates and maintains the interceptor system located in the Cities of Chesapeake, Norfolk, Portsmouth, Suffolk and Virginia Beach, and the County of Isle of Wight
 - **System Reliability:** Inspection, testing, reliability, integrity, enhancement, odor abatement, and inflow and infiltration elimination
- **Treatment**
 - **Treatment:** Operating and maintaining treatment plants
 - **Facilities Maintenance:** Coordinates preventive and major corrective maintenance programs for the Treatment Department
 - **Safety:** Coordinates the safety program for the District
- **Water Quality**
 - **Industrial Waste:** Controls all non-domestic waste discharged into the District's system
 - **Laboratory:** Performs all District analytical testing
 - **Technical Services:** Scientific/technical support of all District departments and administration of all District permits

The following individuals are responsible for the daily management and affairs of the District:

D. R. Wheeler, General Manager. Mr. Wheeler received a B.S. degree in Biology from Virginia Tech in 1968. Mr. Wheeler worked in several capacities at the Commonwealth of Virginia State Water Control Board for six years before accepting employment with the District as Director of Water Quality. Mr. Wheeler served as a department head for 22 years before being selected General Manager in 1996. Mr. Wheeler served as President of the Virginia Association of Municipal Wastewater Agencies for six years. He has served as a member of the Board of Directors of the Association of Municipal Sewerage Agencies for seven years and is now its Treasurer. Mr. Wheeler has also served on the Water Environment Research Foundation's Board of Directors. Mr. Wheeler has authored and/or co-authored several scientific articles and has spoken on numerous occasions at state and national conferences on regulatory and utility administration issues. Mr. Wheeler was an adjunct professor of Civil Engineering at Old Dominion University and taught there on a part-time basis.

Guy M. Aydlott, Director of Water Quality. Mr. Aydlott received a B.S. degree in Chemistry from Old Dominion University in 1974. Mr. Aydlott represents the District on numerous local, state and national committees dealing with environmental legislation, pretreatment policy and control of industrial and hazardous wastes. His national appointments include: Chair, Pretreatment and Hazardous Waste Committee for the Association of Metropolitan Sewerage Agencies (AMSA); Member, Common Sense Initiative Council and Metal Finishing Subcommittee; Member, EPA Effluent Guidelines Taskforce; Member US EPA National Advisory Committee for Environmental Policy and Technology (NACEPT) Sectors Subcommittee; Member, Standard Methods Review Committee; Member, EPA Sustainable Industry Project - Photo Image Steering Committee; and Member, Water Environment Federation Pollution Control Committee. He serves as Vice President of the Virginia Association of Municipal Wastewater Agencies (VAMWA), Commonwealth POTW Representative for the Governor's Water Policy Technical Action Committee and on the Board of Directors for the Elizabeth River Project, on the Board of Advisors for the Hampton Roads Chamber of Commerce, and is the Chair of the POTW Board of Directors for the EPA Strategic Goals Program. Mr. Aydlott, the author and co-author of associated publications and a member of numerous professional organizations, is listed in "Who's Who in U.S. Executives". He is also the recipient of Vice President Al Gore's "Silver Hammer" Award for eliminating waste in government. He joined the District as a Laboratory Technician in 1969 and was promoted to Chief of Industrial Waste in 1976 and to Director of Water Quality in 1997.

Keith W. Benson, P.E., Director of Interceptor Systems. Mr. Benson graduated from Old Dominion University in 1976, *magna cum laude*, with a Bachelors Degree in Civil Engineering Technology. He received a Master of Engineering Degree from Old Dominion University in 1981. Mr. Benson was a member of Tau Alpha Pi National Honor Society and the Virginia Epsilon Chapter of Alpha Chi. Mr. Benson joined the District in 1976 as a Civil Engineer in the Engineering Department. He was promoted to Assistant Director of the Interceptor Systems Department in 1983 and the Director of the Interceptor Systems Department in 1987. Mr. Benson is a registered Professional Engineer and is a member of the Virginia Water Environment Association and the Water Environment Federation where he serves on the Collection Systems Committee. Mr. Benson is also a member of the Utility Directors Committee and the SSO Subcommittee for the Hampton Roads Planning District.

John A. Maniscalco, CPA, Director of Finance & Administration. Mr. Maniscalco graduated from Old Dominion University with a B.S.B.A. in Accounting in 1981. He is a senior financial manager with public (Big 5), private and government sector experience with diverse exposure to sanitation, education, transportation/airport and real estate. Mr. Maniscalco was employed in 1981 as an Accountant with Price Waterhouse in Norfolk and in 1982 as a Financial Manager/Controller with Virginia Beach real estate firms. He was employed as Director of Finance at Norfolk Airport Authority in 1987 and in 1995 as Director of Finance & Property Management to Capital Region Airport Commission, Richmond, Virginia. In 1996, Mr. Maniscalco was employed as Director of Finance for Portsmouth Public Schools in Portsmouth, Virginia. Mr. Maniscalco joined the District in 2000 as the Director of Finance and Administration. Strategic roles include creating, planning and implementing financial systems and creating departmental and division organization and guidelines. Mr. Maniscalco leads efforts in the District Succession Planning. Mr. Maniscalco is a member of Old Dominion University's Executive Advisory Council of the Center for Global Business & Executive Education.

Edward D. Romm, P.E., Director of Engineering. Mr. Romm graduated from the Virginia Military Institute in 1966 with a B.S. in Civil Engineering, and from the Georgia Institute of Technology in 1968 with a M.S. in Civil Engineering. He is a Registered Professional Engineer. He was employed by the Virginia Department of Highways as a Transportation Planning Engineer before serving in the U.S. Army Corps of Engineers in the Far East District as a Resident Engineer. He joined the District in 1970 as a Civil Engineer and was promoted to Assistant Director of Treatment in 1972, to Director of Treatment in 1980, and to Director of Engineering in 1987 when the department was formed.

G. David Waltrip, P.E., Director of Treatment. Mr. Waltrip graduated from Virginia Polytechnic Institute and State University in 1971 with a B.S. degree in Mechanical Engineering. In 1975, he received a MS degree in Environmental Engineering from the same university. He is a past president of the Virginia Water Environment Association and a past director for the national Water Environment Federation ("WEF"). Mr. Waltrip has authored or co-authored publications in the WEF Journal on odor control and on biological nutrient removal. He has served as an invited speaker on those and other wastewater topics at state, national, and international conferences and seminars. He was a co-author of the WEF/ASCS odor control manual (WEF Manual of Practice No. 22). He has served on the EPA Chesapeake Bay Nutrient Removal Technology task force and is a member of the WEF "Water Environmental Technology" publication Editorial Advisory Board. Mr. Waltrip joined the District in 1975. He has served the District as Treatment Engineer, Plant Manager, Assistant Director of Treatment, and since 1987 in his current position as Director of Treatment. Mr. Waltrip is a registered Professional Engineer and is a licensed Class I wastewater treatment plant operator.

Awards

Historically, the District has received a number of awards for excellence in plant operations and maintenance, permit compliance, environmental engineering and design and financial reporting. In 2002, the District's nine major treatment plants won two platinum, five gold and two silver awards from the Association of Metropolitan Sewerage Agencies.

THE SERVICE AREA

The District provides service to 733 square miles of the 3,118 square miles within the boundaries of its corporate limits. The geographical limits are shown on the map attached hereto and include the following localities:

City of Chesapeake	Gloucester County
City of Hampton	Isle of Wight County
City of Newport News	James City County
City of Norfolk	King and Queen County
City of Poquoson	King William County
City of Portsmouth	Mathews County
City of Suffolk	Middlesex County
City of Virginia Beach	York County
City of Williamsburg	

Population Growth

The area within the District has experienced rapid urban and suburban development and consequent population growth resulting in increased quantities of wastewater being treated at the District's treatment plants. The historical population and projections of future population within the District are presented below. Presently, the District contains approximately 22% of the population of the Commonwealth of Virginia.

<u>Year</u>	<u>Source</u>	<u>Population</u>	<u>Population Increase (%)</u>
1960	U.S. Census	660,338	--
1970	U. S. Census	973,247	47
1980	U.S. Census	1,085,332	12
1990	U.S. Census	1,431,000	32
2000	U.S. Census	1,551,000	8
2010	Estimate ¹	1,722,295	11

(1) Virginia Economic Development Partnership

Wastewater Flow

As the following chart indicates, during the last ten years, the District has experienced irregular growth in average daily wastewater flow. During the ten-year period, there has been population growth in the service area and growth in the number of service connections. The number of service connections has increased from 377,000 as of June 30, 1994 to 440,000 as of June 30, 2003. However, billed water consumption has remained fairly constant during such period because of conservation efforts on the part of utility customers fostered by increasing water rates, improved construction materials and the installation of low flow plumbing fixtures. In addition, the variations in average daily flow in 2000-2003 reflect relatively wet weather in 2000 and 2003 and relatively dry weather in 2001 and 2002.

Wastewater Flows Treated and Billed By The District (Million Gallons Per Day)

<u>Fiscal Year Ended June 30,</u>	<u>Average Daily Wastewater Flow</u>	<u>Total Billed Wastewater Flow⁽¹⁾</u>
1994	156	122
1995	146	125
1996	155	127
1997	162	125
1998	168	128
1999	153	128
2000	172	133
2001	157	131
2002	147	127
2003	172	126

(1) Water meters are read for billing purposes by the participating jurisdictions.

Expansion of Service Area

In most instances, the routine expansion of the service area results from the extension of the interceptor system which is performed at the request of a local government. When the interceptor system is expanded, the District requires the local government to enter into an Interest Participation Agreement with the District. An Interest Participation Agreement requires the local government to guarantee the payment of interest expense of the proposed extension. The interest payment is calculated by multiplying the total cost of construction by the current rate of interest on twenty-five year investment grade tax-exempt revenue bonds. The local government agrees to pay the District at the end of each quarterly period one-fourth of the annual interest payment as of the date of the completion of the interceptor. When the District begins the treatment of flows, the District agrees to credit against the local government's quarterly interest payment seventy percent (70%) of the revenue received from treatment service charges associated with the extension. When the revenue credit exceeds the interest payment for four consecutive quarters, the Interest Participation Agreement is terminated.

THE SYSTEM

The Wastewater System consists of nine major treatment plants (above 15 MGD capacity), four smaller plants and its interceptor system consisting of 79 major pumping stations and approximately 478 miles of interceptors ranging in diameter from 12 to 60 inches. The interceptors, which are gravity and force mains, convey wastewater from the point of delivery by municipalities, industry and other users of the Wastewater System to the District's treatment plants.

The following table identifies the location of the District's major treatment plants, their design capacities and, for the fiscal year ended June 30, 2003, their average daily flows.

**Hampton Roads Sanitation District
Treatment System Capacity & Flows
(Million Gallons Per Day)**

<u>Major Treatment Facilities</u>	<u>Average Design Capacity</u>	<u>FY 2003 Annual Average Daily Flow</u>
Atlantic Virginia Beach	36.0	30.0
Army Base Norfolk	18.0	13.1
Boat Harbor Newport News	25.0	15.6
Chesapeake-Elizabeth Virginia Beach	24.0	18.2
James River Newport News	20.0	14.7
Nansemond Suffolk	30.0	19.6
Virginia Initiative Norfolk	40.0	33.4
Williamsburg James City County	22.5	15.3
York River York County	<u>15.0</u>	<u>12.1</u>
TOTALS	230.5	172.0

The District currently operates four additional wastewater treatment plants: one each in Mathews (Mathews County), 0.1 MGD capacity with 2003 flows of 0.04 MGD; in Urbanna (Middlesex County), 0.1 MGD capacity with 2003 flows of 0.05 MGD; in West Point (King William County), 0.6 MGD capacity with 2003 flows of 0.5 MGD; and in King William (King William County), 0.025 MGD capacity with 2003 flows of 0.009 MGD.

System Improvements and Innovations

The Nansemond Treatment Plant was upgraded in 1998 to allow modular expansion up to 100 MGD capacity and expanded from 10 to 30 MGD utilizing the Virginia Initiative Plant process which removes substantial quantities of nitrogen and phosphorous from the wastewater through a biological process invented by the District and CH2M Hill. In 2002 a water reclamation facility was constructed and placed in service to furnish 0.5 MGD treated effluent to Giant Industries. The District and Giant Industries are currently evaluating other uses of the treated effluent, which would require expansion of the facility.

Three major interceptor system extensions have been completed in the last five years. The Windsor Interceptor Force Main was constructed to provide service to the Town of Windsor. The Lagomar Interceptor Force Main was completed in 2001 as part of the first phase of a southern loop that will move flow from south of

Great Bridge in Chesapeake to the Atlantic Treatment Plant. The Carolina Road Interceptor Force Main was recently completed and it extends service south of the City of Suffolk.

Odor control systems have been upgraded at five of the District's treatment plants during the last five years. All plants and most pump stations have been equipped with odor control systems. Demonstrating its commitment to the communities surrounding its treatment plants, the District has expended considerable resources in the area of odor control.

All treatment plants have had major projects designed to eliminate the use of gaseous chlorine and sulfur dioxide and to convert to the use of sodium hypochlorite as a disinfectant feed system for the effluent. The last project is in the final stages of completion, which will remove this hazardous material from all of the District's treatment plants.

Capital Improvement Program

Regulatory requirements, renewals and replacements, and increased treatment capacity are being met by the District's Capital Improvement Program (the "Capital Improvement Program"). Projects are identified each year and the program is modified as circumstances dictate. The Commission appropriates funds on an individual project basis.

The current Capital Improvement Program identifies approximately \$189 million in interceptor system and facility construction projects over the next five fiscal years ending June 30, 2008. Over \$80 million is identified for the rehabilitation and expansion of wastewater treatment plants. The rehabilitation of the Chesapeake-Elizabeth Treatment Plant, a \$33 million project, is scheduled to begin in January 2004 with a three-year construction period. A commitment for the financing of this project has been obtained from the Virginia Water Facilities Revolving Fund, through the Virginia Resources Authority, and the District will issue a Subordinate Bond to evidence the indebtedness to be incurred for such project. The expansion of the Atlantic Treatment Plant is preliminarily estimated to cost approximately \$47 million, with the projected award of the design phase in the second quarter of 2004. Preliminary discussion with the Virginia Resources Authority has begun regarding the financing of this project.

A number of interceptor projects, totaling approximately \$22 million and comprising the southern loop, are currently under construction or in the process of bid and award. The projected completion of the interceptor projects extends into 2005.

Other projects identified include a \$20 million composting facility which will provide a modern upgraded operation facility at a new location. An independent contractor currently provides composting operations. The new facility will also provide increased capacity. A new Accounts Receivable/Billing and Cashiering System is estimated to cost \$9 million. The current computer platform operating system support will end in 2006. The District bills over 440,000 customers directly, with most on a bimonthly basis.

Water reuse for irrigation and non-potable industrial uses is still a high priority of the District. The success of the reuse project at the York River Treatment Plant with Giant Industries demonstrates that reuse can pay for itself. Additional projects continue to be investigated and researched. A current study of the use of the Virginia Initiative Plant effluent for ornamental plants and turf irrigation is underway.

Regulation and Permits

The Virginia State Water Control Law (Chapter 3.1, Title 62.1, Code of Virginia, 1950, as amended) provides that the plans and specifications for wastewater facilities to be constructed be approved by the Virginia Department of Health and the Virginia Department of Environmental Quality. The Enabling Act requires any substantial change in the method used for treating wastewater and industrial wastes to prevent the pollution of any waters within the District to be approved by the Virginia Department of Health as effective and satisfactory for the purpose intended. The District operates all of its plants and interceptor systems under permits issued by the Virginia Department of Environmental Quality.

The District is not aware of any pending federal or state regulatory requirements that would require significant expenditures for additional capital improvements; however, the District cannot predict the scope or effect of future federal or state regulatory actions that could require significant expenditures for capital improvements.

James River Plant Overflow

Abnormally heavy rains, following the third wettest July in Hampton Roads in 32 years, more than doubled the normal flow of wastewater going to the James River Treatment Plant on the morning of August 7, 2003. This surge caused untreated wastewater to overflow onto the plant grounds from 11:45 A.M. until 7:00 P.M. The estimated total diluted overflow of two million gallons reached a small tributary to the Warwick River through the James River Treatment Plant's storm drains and over land, but no overflow reached the neighborhoods adjacent to the James River Treatment Plant. The James River Treatment Plant, which is rated to treat 20 million gallons during a 24-hour period, operated effectively and was able to successfully treat a total of 24 million gallons on August 7. The District has taken several steps subsequent to the event to prevent future occurrences. In addition, the District has entered into an agreement with HydroQual for the development of a computer model of the lower James River that could be utilized in the projection of the effects of this spill and future events.

Hurricane Isabel

On September 19, 2003, the effects of Hurricane Isabel were felt throughout the service area of the District. All wastewater treatment plants lost power, but remained fully functional with onsite generators. Preparations prior to Hurricane Isabel's arrival helped protect property and equipment and the District suffered minimal losses. Preliminary estimates approach \$1 million with approximately \$400,000 resulting from flood damaged seawalls at a pump station and a treatment plant. Minor roof damage, cleanup and fuel costs, among other things, are estimated at \$200,000. Hurricane condition labor costs exceeded \$300,000. The District expects insurance and FEMA reimbursements to cover the majority of these expenses.

Consulting Engineer

CH2M Hill serves as the District's consulting engineer and has provided preliminary engineering services as well as performing the duties of one of the Consultants required under the Master Indenture. CH2M Hill is one of the nation's largest consulting engineering firms specializing in the environmental field. It employs a professional and support staff of approximately 11,000 in 200 offices worldwide. CH2M Hill's services to the District are coordinated or performed by personnel located in its Newport News and Virginia Beach, Virginia offices. CH2M Hill's most recent annual report on the District was prepared in March, 2003 as required by the Master Indenture. In CH2M Hill's opinion, the Wastewater System is in good repair, working order and condition and is operated and maintained in accordance with standard industry practices. CH2M Hill is also of the opinion that the Wastewater System is sufficient to provide service for all current service area demands and is adequately staffed for such purposes. The District has the ability to undertake the necessary expansions of the Wastewater System to meet future service area demands as the need arises. CH2M Hill further advises that the District has a program to assure that necessary permits are obtained from the proper authorities and that the District is in material compliance with the permits that it holds.

FINANCIAL MANAGEMENT

General

The District conducts its financial operations in a conservative manner. Through its annual budget process, management ensures that operating revenues are sufficient to meet operating expenditures and sufficient reserves are available in the event actual billings do not meet budget estimates. The construction of new plants and extension of the interceptor system are financed by a combination of operating revenues, grant funds and debt financing.

Summary of Operations - FY 2003
(\\$000)

	<u>Amount</u>	<u>Percent of Total Revenue</u>	<u>Dollar Increase/ (Decrease) from FY2002</u>	<u>Percentage Increase/ (Decrease) from FY2002</u>
Net Operating Revenues	\$ 97,324	85.5%	\$ (444)	(0.5)%
Less: Operating Expenses	<u>101,041</u>	88.8	<u>4,132</u>	4.3
Net Operating Income	\$ (3,717)	(3.3)	\$(4,576)	(533)
Net Nonoperating Revenue	<u>9,772</u>	8.6	<u>4,912</u>	101
Excess of Revs. over Exps.	\$ 6,055	5.3	\$ 336	5.8
Capital Contribution	0	0	(2,114)	100
Special Item	<u>(6,944)</u>	<u>(6.1)</u>	<u>(6,944)</u>	<u>(100)</u>
Change in Fund Equity	\$ (889)	(0.8)	\$(8,722)	(111)

Wastewater treatment charges decreased by (0.5%) from fiscal year 2002 to \$97.324 million. This decrease was the result of constant rates over the period, while billed water consumption remained relatively flat at 127 million gallons per day. Actual wastewater treatment charges collected were 101% of the fiscal year 2003 budget. Actual facility charges were 145% of the fiscal year 2003 budget. Current expenditures were 106% of the budget authorization. Included in these expenditures was a one-time charge for the funding of the prior service costs of the post-retirement health benefit approved by the Commission. This charge was \$6.9 million. Removal of this charge results in expenditures at 95% of the budget authorization. The increase in expenses from fiscal year 2002 resulted from increases in wages, hospitalization and fuel costs.

Pension Fund. The District participates in the Virginia Retirement System ("VRS") a defined benefit plan offered by the Commonwealth of Virginia. On behalf of its employees, the District contributes monthly to the VRS. In fiscal year 2003, the District's funding requirement was 1% of annual covered payroll, plus 5%, representing the employee member contribution assumed by the District, or \$1,622,000. This funding requirement represented actuarially determined current liabilities of the District.

Post-Retirement Benefits. The Commission adopted a post-retirement health benefit for qualifying employees beginning after July 1, 2002. The program will furnish lifetime health benefits for all employees with at least 15 years of service at the District and who qualify for an unreduced retirement benefit. The prior service costs are estimated to be approximately \$7.0 million. Funding of the prior service costs was accomplished during fiscal year 2003. Ongoing annual contributions are projected to be approximately \$.5 million.

Debt Administration. Currently, the District has the Refunded Bonds and the Subordinate Bonds outstanding. The amount of outstanding debt as of June 30, 2003 was \$142,046,000 which is a reduction of \$10,832,000 from fiscal year 2002.

Cash Management. Idle cash is invested primarily in obligations of United States agencies and also in commercial paper, corporate bonds and municipal securities. For fiscal year 2003, the District's overall yield on investments was approximately 3.15%. The Commission adopted on February 28, 1995 an investment policy that gives priority to safety of principal, then liquidity and then yield.

Budgeting and Accounting

Budgetary Controls. The District adopts an annual budget based on projected cash needs and debt service coverage requirements on its revenue bonds. The budget is approved on or before June 15 of each year. The District maintains budgetary controls on a departmental basis. Unused revenue fund appropriations lapse at year end. Financial plans are adopted for capital projects for the life of the project.

Financial Statements. In accordance with generally accepted accounting principles, the District's audited general purpose financial statements have been prepared on a full accrual basis incorporating the principles of enterprise fund accounting. This approach presents the District's financial statements on a profit and loss basis,

including an annual provision for depreciation, which is comparable to private industry. The District's audited basic financial statements from the fiscal year ended June 30, 2003 are included in Appendix A.

The Government Finance Officers Association of the United States and Canada awarded a Certificate of Achievement for excellence in Financial Reporting to the District for its comprehensive annual financial reports for each of the fiscal years ended June 30, 1981 to 2002. The District will submit its report for the fiscal year ended June 30, 2003 and expects to receive another Certificate of Excellence. In order to be awarded a Certificate of Excellence, a governmental unit must publish an easily readable and efficiently organized comprehensive annual financial report, whose contents conform to program standards. Such reports must satisfy both generally accepted accounting principles and applicable legal requirements.

Rates

The District periodically reviews its rate structure and revises its charges as necessary to generate the revenues required to meet its current financial obligations. The most recent general increase in rates became effective July 1, 2003. A summary of the District's rate schedule, consisting of Wastewater Treatment Charges, Surcharges, Wastewater Treatment Facilities Charges and Equalization Charges, is included in Appendix B.

Rate Making Process

The Enabling Act provides that the Commission shall fix and revise rates, fees and charges to provide funds, which with other funds available for such purposes, will be sufficient at all times (a) to pay the cost of maintaining, repairing and operating the Wastewater System and all improvements thereto, including reserves for such purpose and for renewals and replacements and necessary extensions and additions to the Wastewater System, (b) to pay the principal of and the interest on such revenue bonds as the same shall become due and to provide reserves therefor and (c) to provide a margin of safety for making such payments.

The Enabling Act provides that before any revision of rates, fees and charges shall become effective the Commission shall publish a copy thereof for four consecutive weeks in a newspaper of general circulation within the District. If, on or before the last publication, the governing body of any city or county constituting a part of the District or five hundred or more qualified voters residing within the District shall file a petition with the Virginia State Corporation Commission complaining of the proposed revision, the State Corporation Commission may by order suspend the placing in effect of such revision for a period not exceeding sixty days from the filing of any such petition during which time it shall investigate whether such revision is just and equitable and in accordance with the provisions of the Enabling Act. If the State Corporation Commission shall not enter an order suspending, approving or disapproving such revision within sixty days from the filing of any such petition, such revision shall be deemed to be in effect. The District or the party or parties filing a petition may appeal to the Virginia Supreme Court from any such order as may be entered by the State Corporation Commission.

Collection of Unpaid Wastewater Treatment Charges

The Enabling Act provides that if any bill for wastewater treatment charges shall not be paid in full when the same shall become due, the owner, tenant or occupant of such lot or parcel of land shall, until wastewater treatment charges shall be paid, cease to dispose of wastewater or industrial wastes originating from or on such property by discharge thereof directly or indirectly into the Wastewater System, and if such owner, tenant or occupant shall not cease such discharge within two months thereafter, it shall be the duty of each public or private agency supplying water to such property, within five days after receipt of notice of such facts from the District, to cease supplying water to such property. If the water supply is not stopped, the District has the power to enter into any public or private property to shut off the property's water supply.

If any wastewater treatment charges shall not be paid within thirty (30) days after the same become due, the District may at the expiration of such thirty (30) day period proceed to recover the amount of any such delinquent sewage treatment charges by any action, suit or proceeding permitted by law or in equity.

The following table shows the District's treatment charge collection rate for the last ten fiscal years.

**Hampton Roads Sanitation District
Collection Rate**

<u>Fiscal Year Ended June 30,</u>	<u>Percentage of Wastewater Treatment Charges Collected</u>
1993	99.3
1994	99.3
1995	99.1
1996	99.2
1997	99.1
1998	99.2
1999	99.3
2000	99.5
2001	99.0
2002	99.3

Ten Largest Customers

The following table shows the District's ten largest customers on the basis of wastewater treatment fees and charges paid as of June 30, 2003.

<u>Customer</u>	<u>Type</u>	<u>Amount</u>	<u>Percentage of Total Fees and Charges</u>
Anheuser-Busch, Inc. (1)	Brewery	\$ 5,820,000	6.2%
Smithfield Foods	Meat Processor	2,021,000	2.2
U.S. Navy-Norfolk Naval Base	Military Facility	1,960,000	2.1
City of Norfolk	Municipality	954,000	1.0
U.S. Navy-Little Creek Amphibious Base	Military Facility	737,000	0.8
U.S. Air Force-Langley Air Force Base	Military Facility	626,000	0.7
Norfolk Redevelopment and Housing Authority	Housing Authority	608,000	0.6
Newport News Shipbuilding & Dry Dock Co.	Shipbuilding and Repair	388,000	0.4
City of Virginia Beach	Municipality	367,000	0.4
Norfolk Naval Shipyard	Military Ship Repair	342,000	0.4
TOTAL		\$13,283,000	14.8%

- (1) The District entered into an agreement with Anheuser-Busch, Inc, which requires a minimum payment in each of 30 years ending in July 2008. The payment is based on a minimum daily waste loading.

Operating Results

The following table shows the results of operations for the District for the indicated fiscal years ended June 30.

HAMPTON ROADS SANITATION DISTRICT RESULTS OF OPERATIONS FY 1999 - FY 2003 (,\$000)

	2003	2002	2001	2000	1999
OPERATING REVENUES					
1. Wastewater treatment charges	\$ 93,841	\$ 93,819	\$ 88,449	\$ 83,331	\$ 82,642
2. Miscellaneous	3,483	3,949	3,977	3,570	3,823
3. TOTAL OPERATING REVENUES	97,324	97,768	92,426	86,901	86,465
OPERATING EXPENSES					
4. Wastewater treatment	55,448	52,324	51,991	49,478	46,381
5. General administrative	18,118	17,659	15,789	15,604	15,456
6. Depreciation	27,475	26,926	26,312	26,455	27,402
7. TOTAL OPERATING EXPENSES	101,041	96,909	94,092	91,537	89,239
8. OPERATING INCOME (LOSS)	(3,717)	859	(1,666)	(4,636)	(2,774)
NONOPERATING REVENUES (EXPENSES)					
9. Wastewater facility charges	8,677	7,727	5,580	5,379	5,742
10. Investment earnings	3,488	4,572	5,185	4,890	5,352
11. Sale of land	4,517	-	-	-	-
12. Change in fair value of investments	(155)	(79)	1,956	(672)	(1,257)
13. Legal claim settlement	0	-	-	-	-
14. Interest expense	(6,755)	(7,360)	(7,751)	(8,100)	(8,614)
15. NET NONOPERATING REVENUES	9,772	4,860	4,970	1,497	1,223
16. INCOME (LOSS) BEFORE CONTRIBUTIONS	6,055	5,719	3,304	(3,139)	(1,551)
CAPITAL CONTRIBUTIONS					
17. Contributions from other governments	-	2,114	-	2,165	-
SPECIAL ITEM					
18. Prior service cost for post retirement health program	(6,944)	-	-	-	-
19. CHANGE IN FUND EQUITY	\$ (889)	\$ 7,833	\$ 3,304	\$ (974)	\$ (1,551)
DEBT SERVICE					
20. 1993 Senior Bonds	\$ 11,579	\$ 15,092	\$ 15,110	\$ 15,126	\$ 15,130
21. Subordinate Bonds	\$ 7,330	\$ 7,005	\$ 6,621	\$ 6,190	\$ 6,146
DEBT SERVICE COVERAGE					
22. 1993 Senior Bonds(1)	3.48	2.65	2.47	2.08	2.28
23. Total Indebtedness(2)	2.13	1.81	1.72	1.47	1.62

1. Line 16 plus lines 6 and 14 divided by line 20.

2. Line 16 plus lines 6 and 14 divided by the sum of lines 20 and 21.

LITIGATION

There is no litigation pending in any court (either state or federal) or, to the knowledge of the District, threatened against the District which in any way questions or affects the validity of or the security for the Series 2003 Bonds, or which would have a material adverse effect on the District's condition, financial or otherwise.

APPROVAL OF LEGAL PROCEEDINGS

The Series 2003 Bonds are offered subject to the approving opinion of Sidley Austin Brown & Wood LLP, New York, New York, Bond Counsel. Certain legal matters will be passed upon for the District by its General Counsel, Kellam, Pickrell, Cox & Tayloe, Norfolk, Virginia.

TAX MATTERS

Opinion of Bond Counsel

In the opinion of Sidley Austin Brown & Wood LLP, Bond Counsel, assuming compliance by the District with its covenant to comply with the requirements of the Internal Revenue Code of 1986, as amended (the "Code"), and except as provided in the following sentence, interest on the Series 2003 Bonds will not be includable in the gross income of the owners of the Series 2003 Bonds for purposes of federal income taxation under existing law. Interest on the Series 2003 Bonds will be includable in the gross income of the owners thereof retroactive to the date of issue of the Series 2003 Bonds in the event of a failure by the District to comply with applicable requirements of the Code and its covenant regarding use, expenditure and investment of the proceeds of the Series 2003 Bonds and timely payment of certain investment earnings to the United States Treasury. The opinion of Bond Counsel with respect to the exclusion from gross income of the interest on the Series 2003 Bonds for federal income tax purposes may not be relied upon to the extent that such exclusion is adversely affected as a result of any action taken in reliance upon the opinion of counsel other than Bond Counsel delivered subsequent to the issuance of the Series 2003 Bonds.

Interest on the Series 2003 Bonds will not be a specific preference item for purposes of the federal individual or corporate alternative minimum tax. The Code contains other provisions (some of which are noted below) that could result in tax consequences, as to which no opinion will be rendered by Bond Counsel, as a result of (i) ownership of the Series 2003 Bonds or (ii) the inclusion in certain computations (including, without limitation, those related to the corporate alternative minimum tax) of interest that is excluded from gross income. Interest on the Series 2003 Bonds owned by a corporation will be included in the calculation of the corporation's federal alternative minimum tax liability.

Original Issue Discount

The excess, if any, of the amount payable at maturity of any maturity of the Series 2003 Bonds over the issue price thereof constitutes original issue discount. The amount of original issue discount accrues in accordance with a constant yield method based on the compounding of interest. The amount of original issue discount that has accrued pursuant to the constant yield method described above, and is properly allocable to an owner of any maturity of the Series 2003 Bonds with original issue discount (the "Discount Bonds"), will be excluded from gross income to the same extent as interest on the Series 2003 Bonds for federal income tax purposes. In general, the issue price of a maturity of the Series 2003 Bonds is the first price at which a substantial amount of that maturity was sold (excluding sales to bond houses, brokers or similar persons acting in the capacity of underwriters or wholesalers). A purchaser's adjusted basis in a Discount Bond will be increased by the amount of such accruing discount for purposes of determining taxable gain or loss on the sale or other disposition of such Discount Bond for federal income tax purposes.

A portion of the original issue discount that accrues in each year to an owner of a Discount Bond that is a corporation will be included in the calculation of the corporation's federal alternative minimum tax liability. In

addition, original issue discount that accrues in each year to an owner of a Discount Bond is included in the calculation of the distribution requirements of certain regulated investment companies and may result in some of the collateral federal income tax consequences discussed herein. Consequently, owners of any Discount Bond should be aware that the accrual of original issue discount in each year may result in an alternative minimum tax liability, additional distribution requirements or other collateral federal income tax consequences although the owner of such Discount Bond has not received cash attributable to such original issue discount in such year.

The accrual of original issue discount and its effect on the sale or other disposition of a Discount Bond that is not purchased in the initial offering at the first price at which a substantial amount of Discount Bonds of that maturity is sold to the public may be determined according to rules that differ from those described above. Owners of Discount Bonds should consult their tax advisors with respect to the determination for federal income tax purposes of the amount of original issue discount or interest properly accruable with respect to such Discount Bonds and with respect to state and local tax consequences of owning and disposing of such Discount Bonds.

Original Issue Premium

The excess, if any, of the tax basis of the Series 2003 Bonds to a purchaser (other than a purchaser who holds such Series 2003 Bonds as inventory, stock in trade or for sale to customers in the ordinary course of business) who purchased such Series 2003 Bonds as part of the initial public offering and at the initial offering price set forth on the cover page over the amount payable at maturity is "bond premium." Bond premium is amortized over the term of such Series 2003 Bonds for federal income tax purposes (or, in the case of a bond with bond premium callable prior to its stated maturity, the amortization period and yield may be required to be determined on the basis of an earlier call date that results in the lowest yield on such bond). Owners of such Series 2003 Bonds are required to decrease their adjusted basis in such Series 2003 Bonds by the amount of amortizable bond premium attributable to each taxable year such Series 2003 Bonds are held. The amortizable bond premium on such Series 2003 Bonds attributable to a taxable year is not deductible for federal income tax purposes; however, bond premium is treated as an offset to qualified stated interest received on such Series 2003 Bonds. Owners of such Series 2003 Bonds should consult their tax advisors with respect to the determination for federal income tax purposes of the treatment of bond premium upon sale or other disposition of such Series 2003 Bonds and with respect to the state and local tax consequences of owning and disposing of such Series 2003 Bonds.

Collateral Tax Consequences

Ownership of tax-exempt obligations may result in collateral tax consequences to certain taxpayers, including, without limitation, financial institutions, property and casualty insurance companies, certain foreign corporations doing business in the United States, certain corporations with excess passive income, individual recipients of Social Security or Railroad Retirement benefits, taxpayers eligible for the earned income tax credit and taxpayers who may be deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations. Owners of the Series 2003 Bonds should consult their tax advisors as to the applicability of any such collateral consequences.

Legislation affecting municipal securities is constantly being considered by the United States Congress. There can be no assurance that legislation enacted after the date of issuance of the Series 2003 Bonds will not have an adverse effect on the tax-exempt status of the Series 2003 Bonds. Legislative or regulatory actions and proposals may also affect the economic value of the tax exemption or the market price of the Series 2003 Bonds.

Virginia Taxes

The Enabling Act provides that the Series 2003 Bonds, their transfer and the income therefrom, including any profit made on the sale thereof, shall be free and exempt from taxation by the Commonwealth of Virginia and by any political subdivision thereof.

EXPERTS

The opinions of CH2M Hill, Consulting Engineers, Newport News, Virginia, included herein have been made with their permission in reliance upon their authority as experts.

VERIFICATION OF MATHEMATICAL COMPUTATIONS

McGladrey & Pullen, LLP, independent public accountants, will verify certain mathematical computations provided by the District as to the sufficiency of the moneys and investments deposited with the Series 1993 Bond Trustee (i) to pay, when due, the interest on the Refunded Bonds from their last payment date to the date on which they are to be called for redemption and (ii) to pay the principal of, and redemption premium on the Refunded Bonds on their date of redemption. Such computations were based solely on assumptions and information supplied by the District. McGladrey & Pullen, LLP has restricted its procedures to examining the arithmetical accuracy of certain computations and has not made any study or evaluation of the assumptions and information on which the computations are based and, accordingly, has not expressed an opinion on the data used, the reasonableness of the assumptions, or the achievability of future events.

RATINGS

The Series 2003 Bonds have been assigned ratings of "Aa3" and "AA" by Moody's Investors Service, Inc. and Standard & Poor's Ratings Services, respectively. Such ratings reflect only the view of such organizations and a fuller explanation of the significance of such ratings may be obtained from the rating agencies. The District furnished to such rating agencies certain information regarding its policies, practices and finances, including information that is not included in this Official Statement. There is no assurance that such policies, practices and finances or such ratings will continue for any given period of time or that such ratings will not be revised downward or withdrawn entirely by such rating agencies. Any such downward revision or withdrawal could have an adverse effect on the market price of the Series 2003 Bonds.

FUTURE FINANCIAL INFORMATION

On November 10, 1994, the Securities and Exchange Commission adopted in final form certain amendments (the "Amendments") to Rule 15c2-12 under the Securities Exchange Act of 1934, as amended. In general, the Amendments prohibit an underwriter from purchasing or selling municipal securities sold on or after July 3, 1995, such as the Series 2003 Bonds, unless it has determined that the issuer of such securities and/or other persons deemed to be material "obligated persons" have committed to provide (i) on an annual basis, certain financial information and operating data ("Annual Reports"), and, if available, audited financial statements, to each Nationally Recognized Municipal Securities Information Repository (a "NRMSIR") and the relevant state information depository (if any) and (ii) notice of various events described in the Amendments, if material ("Event Notices"), to each NRMSIR or the Municipal Securities Rulemaking Board ("MSRB") and to any such state information depository.

The District will covenant in the Continuing Disclosure Agreement (the form of which appears in Appendix E) for the benefit of the holders of the Series 2003 Bonds to provide to each NRMSIR and to any Virginia information depository that has been formed, annually, not later than December 31 of each year, commencing December 31, 2004, Annual Reports with respect to itself, as issuer. Similarly, the District will provide Event Notices with respect to the Series 2003 Bonds to each such NRMSIR, the MSRB and to any Virginia information depository. This is the District's first continuing disclosure undertaking pursuant to the Amendments.

SALE BY COMPETITIVE BIDDING

The Series 2003 Bonds were awarded pursuant to electronic competitive bidding held via Parity on November 18, 2003 to Legg Mason Wood Walker, Incorporated (the "Underwriter") at a price to the District that results in an underwriter's discount of \$137,758 from the initial public offering prices derived from the yields shown on the cover page. The Underwriter has supplied the information as to the initial public offering yields shown on the cover page. The Underwriter may offer to sell the Series 2003 Bonds to certain dealers and others at prices lower than the initial public offering prices derived from the yields shown on the cover page.

MISCELLANEOUS

All of the foregoing summaries or descriptions of the provisions of the Enabling Act, the Series 2003 Bonds, the Master Indenture, Supplement No. 2 and the Trust Agreement are made subject to all of the detailed provisions thereof to which reference is made for further information. The foregoing summaries do not purport to be complete statements of any or all of the provisions thereof. Copies of the Trust Agreement and the Master Indenture are available upon request to the District at the following address: 1436 Air Rail Road, Virginia Beach, Virginia 23455: Phone (804) 460-2261.

Capitalized terms used but not defined herein shall have the meanings given to such terms in the Master Indenture and Trust Agreement. (See also, Appendix C, "Definitions of Certain Terms"). Brief descriptions and summaries of certain provisions of the Series 2003 Bonds, the Master Indenture and the Trust Agreement are included in Appendix C.

Any statement in this Official Statement involving matters of opinion whether or not expressly so stated are intended as such and not as representations of fact. The execution and delivery of this Official Statement has been duly authorized by the District.

/s/ William H. Pierce

Chairman

Hampton Roads Sanitation District Commission

/s/ D.R. Wheeler

General Manager

Hampton Roads Sanitation District

APPENDIX A

**Basic Financial Statements and
Related Auditor's Report for the fiscal year ended
June 30, 2003 as rendered by KPMG LLP**

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2100 Dominion Tower
999 Waterside Drive
Norfolk, VA 23510

Independent Auditors' Report

The Commissioners
Hampton Roads Sanitation District:

We have audited the accompanying financial statements of the Hampton Roads Sanitation District (HRSD), a component unit of the Commonwealth of Virginia, as of and for the years ended June 30, 2003 and 2002, as listed in the accompanying table of contents. These financial statements are the responsibility of HRSD's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of HRSD as of June 30, 2003 and 2002, and its operations, changes in fund equity and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in note 2, HRSD adopted the provisions of Governmental Accounting Standards Board (GASB) Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, as of July 1, 2001.

The accompanying management's discussion and analysis on pages 14 through 17 and the schedule of funding progress in note 7 are not required parts of the basic financial statements but are supplementary information required by the GASB. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods and measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

The introductory and statistical sections as listed in the accompanying table of contents are presented for purposes of additional analysis and are not required parts of the basic financial statements. The information included in the introductory and statistical sections has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

KPMG LLP

August 29, 2003



KPMG LLP, KPMG LLP a U.S. limited liability partnership, is
a member of KPMG International, a Swiss association.

MANAGEMENT'S DISCUSSION AND ANALYSIS

This discussion and analysis of Hampton Roads Sanitation District's financial performance provides an overview of HRSD's financial activities for the fiscal year ended June 30, 2003. Please read it in conjunction with the transmittal letter on page 1 and the financial statements, which begin on page 18.

HIGHLIGHTS

Financial highlights

- HRSD's fund equity decreased by \$0.9 million, or 0.3%, as a result of this year's operations.
- Revenues increased to \$114 million or more than 3.6% in 2003, while operating expenses increased 4.3%.
- \$6.9 million was placed in trust to fully fund the prior service cost of the post retirement health care program.
- Just over 20 acres of surplus property was sold for \$4.5 million.
- HRSD's investment in capital assets, net of related debt increased 3.1% to \$250 million at the end of FY-03.

HRSD highlights

- Design of the Chesapeake-Elizabeth Treatment Plant rehabilitation and improvements nears completion.
- The water reuse facility at the York River Plant operated successfully in its first year providing reuse water to Giant Industries.
- Completion of the 30" directionally drilled Elizabeth River crossing interceptor force main.
- Operations center phase V, providing new automotive and electrical shops and training facilities, was completed.
- HRSD held the line on wastewater and surcharge rates but adjusted facility charge rates by 2.9% effective July 1, 2002.

USING THIS ANNUAL REPORT

The Financial Section of the Annual Report consists of three parts; Management's Discussion and Analysis (MD&A), Financial Statements, and unaudited Supplementary Information. The Financial Statements also include notes that explain in more detail some of the information in the financial statements.

MD&A serves as an introduction to the basic Financial Statements and supplementary information along with management's examination and analysis of the financial condition and performance. Summary financial statement data, key financial and operational indicators contained in HRSD's budgets, commission resolutions and other management tools were used for this analysis.

The Financial Statements of HRSD report information about HRSD using accounting methods similar to those used by private sector companies. These statements offer both short and long range financial information about its activities. The Balance Sheet includes the nature and amounts of investments in resources (assets) and obligations to creditors (liabilities). It also provides the basis for computing the rate of return, evaluation of the capital structure, and assessing the liquidity and financial flexibility of HRSD. The Statement of Operations and Changes in Fund Equity contains all of the current year's revenue and expenses. This statement measures the success of HRSD operations over the past year and can be used to determine whether HRSD has successfully recovered all its costs through its user fees and other charges, profitability, and credit worthiness. The final required financial statement is the Statement of Cash Flows. The primary purpose of this statement is to provide information about the cash receipts and cash payments made by HRSD during the reporting period. The statement reports cash receipts, cash payments, and net changes in cash resulting from operations, investing, and capital and non-capital financing activities, without consideration of the earnings event, when an obligation arises, or depreciation of capital assets. The Notes to the Financial Statements provide required disclosures and other information that are essential to a full understanding of material data provided in the statements. The notes present information about HRSD's accounting policies, significant account balances and activities, material risks, obligations, commitments, contingencies and subsequent events, if any.

FINANCIAL ANALYSIS

One of the most important questions asked about HRSD's finances is "is HRSD better off or worse off as a result of this year's activities?" The Balance Sheet and the Statement of Operations and Changes in Fund Equity report information about HRSD's activities in a way that will help answer this question. These two statements report the fund equity of HRSD and changes to it. The difference between assets and liabilities, fund equity, is one way to measure financial health or financial position. Over time, increases or decreases in HRSD fund equity are one indicator of whether its financial health is improving or deteriorating. However, you will need to also consider other non-financial factors such as changes in economic conditions, population and service area growth, and new or changed legislation.

HRSD's total fund equity decreased from last year by \$0.9 million. Our analysis below focuses on the change in fund equity and the resulting changes in asset and liabilities. The 4.9% decrease in long-term liabilities results from the unique structure of the debt service payments on refunded debt in the 1993 revenue bonds issue. Current assets and investments were utilized to pay down current and long-term liabilities.

(in thousands)	2003	2002	Dollars	Change
Capital assets	\$392,387	\$396,812	\$ (4,425)	(1.1%)
Current assets and investments	111,375	118,535	(7,160)	(6.0%)
Total assets	<u>\$503,762</u>	<u>\$515,347</u>	<u>\$(11,585)</u>	(2.3%)
Long-term liabilities	\$134,376	\$141,326	\$ (6,950)	(4.9%)
Current liabilities	22,317	26,063	(3,746)	(14.4%)
Total liabilities	<u>\$156,693</u>	<u>\$167,389</u>	<u>\$(10,696)</u>	(6.4%)
Fund equity:				
Investment in capital assets, net of debt	\$250,043	\$242,427	\$ 7,616	3.1%
Restricted	7,062	10,243	(3,181)	(31.1%)
Unrestricted	89,964	95,288	(5,324)	(5.6%)
Total fund equity	<u>\$347,069</u>	<u>\$347,958</u>	<u>\$ (889)</u>	(0.3%)

The changes in HRSD's fund equity can be determined by reviewing the following condensed Statement of Operations and Changes in Fund Equity for the year.

(in thousands)	2003	2002	Dollars	Change
Net operating revenues	\$ 97,324	\$ 97,768	\$ (444)	(0.5%)
Facility charges	8,677	7,727	950	12.3%
Sale of land	4,517	-	4,517	100%
Investment income, net	3,333	4,493	(1,160)	(25.8%)
Total revenues	<u>\$113,851</u>	<u>\$109,988</u>	<u>\$ 3,863</u>	3.5%
Operating expenses	101,041	96,909	4,132	4.3%
Interest expense	6,755	7,360	(605)	(8.2%)
Total expenses	<u>107,796</u>	<u>104,269</u>	<u>3,527</u>	3.4%
Excess of revenues over expenses	6,055	5,719	336	5.9%
Contributions	-	2,114	2,114	100%
Special Item	(6,944)	-	(6,944)	(100%)
Changes in fund equity	(889)	7,833	(8,722)	(111%)
Beginning fund equity	<u>347,958</u>	<u>340,125</u>	<u>7,833</u>	2.3%
Ending fund equity	<u>\$347,069</u>	<u>\$347,958</u>	<u>\$ (889)</u>	0.3%

Operating revenue declined by (0.5%) in 2003 compared to 2002 which was the result of constant rates over the period, while billed water consumption remained relatively flat at 127 million gallons per day. Total revenue increased by 3.5% resulting from the sale of land, and increases in the facility charge. Facility charges were up due to a 2.9% rate adjustment on July 1, 2002 and increased construction in the service area. The investment income change was due to the general reduction in interest rates over the period. A special item of \$6.9 million in 2003 was the funding of prior service costs associated with the post retirement health program adopted by the HRSD Commission in July 2002.

Operating expenses grew 4.3% from 2002 to 2003 due primarily to increased human resource costs, utilities, and increased medical insurance premiums. Actual operating expenses, excluding debt service and the special item, were 5.4% below budget for the fiscal year ended June 30, 2003. Interest expense continued to decline with the retirement of existing debt, a rate reduction on three VRA loans and new borrowings at lower rates.

HRSD'S FUNDS

HRSD has operated as a single enterprise fund since the new trust indenture became effective in December 1993. In 1993 all HRSD outstanding bonds were refinanced and the 1962-trust indenture was retired.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital assets

At the end of 2003, HRSD had \$392.4 million invested in a broad range of capital assets, including wastewater treatment plants, interceptor mains and pump stations, automotive, administrative and maintenance building, and office and computer equipment. This amount represents a net decrease (including additions and deductions) of \$4.4 million over last year or (1.1%).

The following table summarizes HRSD's capital assets, net of accumulated depreciation, as of June 30, 2003 and 2002 (in thousands).

	<u>2003</u>	<u>2002</u>
Land	\$ 4,421	\$ 3,672
Treatment plants	212,814	226,146
Interceptor systems	135,892	132,819
Small community facilities	3,544	3,778
Buildings	11,241	9,582
Office equipment	1,845	2,231
Automotive	1,315	1,595
Other equipment	<u>1,006</u>	<u>1,206</u>
	372,078	381,029
Construction in progress	<u>20,309</u>	<u>15,783</u>
Net property, plant, and equipment	<u>\$392,387</u>	<u>\$396,812</u>

The following table summarizes the changes in capital assets. These changes are presented in a more detailed schedule in note 5.

(in thousands)	<u>2003</u>	<u>2002</u>
Balance at beginning of year	\$396,812	\$404,322
Additions	18,539	22,353
Retirements	(83)	(542)
Depreciation	(27,475)	(26,926)
Accumulated depreciation retired	68	539
Increase (decrease) in construction in progress	<u>4,526</u>	<u>(2,934)</u>
Balance at end of year	<u>\$392,387</u>	<u>\$396,812</u>

This year's major additions to plant, property, and equipment included:

Monticello interceptor force main sections A,B,C	\$ 3.1 million
York River reclamation facilities	\$ 3.0 million
Army Base, Williamsburg, and Chesapeake-Elizabeth off gas improvements	\$ 2.4 million
Elizabeth River crossing interceptor force main	\$ 2.4 million
Operations Center building	\$ 2.3 million
Lamberts Point & North Trunk interceptor force mains	\$ 1.3 million

HRSD's FY-04 to FY-08 five-year capital program identifies \$159.9 million in capital projects, including these major projects:

Atlantic Treatment Plant expansion	\$47.5 million
Chesapeake-Elizabeth Treatment Plant improvements	\$32.7 million
Lake Ridge interceptor force main	\$13.0 million
Biosolids processing facility	\$19.8 million
Elbow Road interceptor force main	\$ 6.7 million

These projects will be funded from cash reserves, non-operating revenue, and additional debt. HRSD has requested financing of the Chesapeake-Elizabeth Treatment Plant improvements with the Virginia Resource Authority (VRA).

Debt

At year-end, HRSD had a total of \$142.0 million in bonds outstanding versus \$153.0 million last year, a decrease of (7.2%) (in thousands).

	<u>2003</u>	<u>2002</u>
Primary sewer revenue bonds	\$ 64,445	\$ 75,850
Secondary VRA bonds	<u>77,601</u>	<u>77,128</u>
Total outstanding debt	<u>\$142,046</u>	<u>\$152,978</u>

HRSD's primary sewer revenue bond rating is Aa3 from Moody's and AA from Standard & Poors rating services. This high rating allows HRSD to borrow at very favorable interest rates. Since December 1993, HRSD has not issued any primary sewer revenue bonds, but has elected to participate in the Virginia Resource Authority program that allows us to borrow at 1% below the projected market rate for double A bonds.

Bond closing results after the award of the construction contract when projected costs of the project are better known. During construction, periodic draws are made against the bonds. During FY-03 HRSD completed the draw down phase on five bonds with the Virginia Resource Authority. As of June 30, 2003 HRSD had drawn down \$5.9 million on these bonds. More detailed information about HRSD's debt is presented in Note 8 to the financial statements.

ECONOMIC FACTORS AND NEXT YEAR BUDGETS AND RATES

Billed consumption has remained fairly level since FY-1998 at approximately 128 million gallons per day even though the number of accounts served continues to grow. This phenomenon is primarily the result of water conservation throughout the region. HRSD reviews rates annually to implement small adjustments as necessary and to avoid large adjustments as much as possible. The 2004 Annual Budget increased 2.3% as compared to the 2003 Annual Budget, which resulted in a rate adjustment on July 1, 2003. The increase in the Annual Budget was a result of increases in personnel services, health care costs, utilities, and property and casualty insurance, offset by a reduction in debt service of \$1.4 million. A rate review will be made in conjunction with the preparation of the 2005 Annual budget next spring.

A 4.8% adjustment to the facility charge rates on July 1, 2003 was implemented due to increased construction costs.

CONTACTING HRSD'S FINANCIAL MANAGEMENT

This financial report is designed to provide our customers and creditors with a general overview of HRSD's finances and to demonstrate HRSD's accountability for the money it receives. If you have questions about this report or need additional financial information regarding HRSD, contact either the Chief of Accounting and Finance or the Director of Finance and Administration at 1440 Air Rail Avenue, Va. Beach, VA 23455.

HAMPTON ROADS SANITATION DISTRICT
BALANCE SHEETS
As of JUNE 30, 2003 and 2002

ASSETS

(In thousands)

	<u>2003</u>	<u>2002</u>
CURRENT ASSETS		
Cash and cash equivalents	\$ 13,074	\$ 38,583
Investments	20,595	13,708
Accounts receivable, net	14,807	15,118
Accrued interest	262	556
Other current assets	2,495	1,883
TOTAL CURRENT ASSETS	<u>51,233</u>	<u>69,848</u>
RESTRICTED ASSETS		
Cash and cash equivalents	<u>7,062</u>	<u>10,243</u>
INVESTMENTS	<u>53,080</u>	<u>38,444</u>
PROPERTY, PLANT, AND EQUIPMENT		
Land	4,421	3,672
Treatment plants	558,410	551,124
Interceptor systems	206,319	199,426
Small community facilities	4,797	4,599
Buildings	18,891	16,577
Office equipment	9,978	9,413
Automotive	8,027	7,792
Other equipment	6,810	6,594
	<u>817,653</u>	<u>799,197</u>
Less: Accumulated depreciation	<u>445,575</u>	<u>418,168</u>
	<u>372,078</u>	<u>381,029</u>
Construction in progress	<u>20,309</u>	<u>15,783</u>
NET PROPERTY, PLANT, AND EQUIPMENT	<u>392,387</u>	<u>396,812</u>
TOTAL ASSETS	<u><u>\$ 503,762</u></u>	<u><u>\$ 515,347</u></u>

LIABILITIES & FUND EQUITY

(In thousands)

	<u>2003</u>	<u>2002</u>
CURRENT LIABILITIES		
Trade and contracts payable	\$ 4,888	\$ 4,408
Contract retention	555	524
Accrued salaries and wages	741	612
Current portion long-term debt	11,454	15,121
Current portion compensated absences	2,745	2,531
Debt interest payable	1,164	1,299
Other liabilities	769	1,568
TOTAL CURRENT LIABILITIES	<u>22,316</u>	<u>26,063</u>
 LONG-TERM LIABILITIES		
Compensated absences	2,685	2,619
Other liabilities	1,100	850
Bonds payable	130,592	137,857
TOTAL LONG-TERM LIABILITIES	<u>134,377</u>	<u>141,326</u>
 TOTAL LIABILITIES	<u>156,693</u>	<u>167,389</u>
 FUND EQUITY		
Investment in capital assets, net of related debt	250,043	242,427
Fund equity restricted for debt service	7,062	10,243
Fund equity unrestricted	89,964	95,288
TOTAL FUND EQUITY	<u>347,069</u>	<u>347,958</u>
 TOTAL LIABILITIES AND FUND EQUITY	<u>\$ 503,762</u>	<u>\$ 515,347</u>

See Accompanying Notes to Financial Statements

HAMPTON ROADS SANITATION DISTRICT
STATEMENTS OF OPERATIONS AND CHANGES IN FUND EQUITY
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 and 2002

(In thousands)

	<u>2003</u>	<u>2002</u>
OPERATING REVENUES		
Wastewater treatment charges	\$ 93,841	\$ 93,819
Miscellaneous	3,483	3,949
TOTAL OPERATING REVENUES	<u>97,324</u>	<u>97,768</u>
 OPERATING EXPENSES		
Wastewater treatment	55,448	52,324
General and administrative	18,118	17,659
Depreciation	27,475	26,926
TOTAL OPERATING EXPENSES	<u>101,041</u>	<u>96,909</u>
 OPERATING INCOME (LOSS)	<u>(3,717)</u>	<u>859</u>
 NONOPERATING REVENUES (EXPENSES)		
Wastewater facility charges	8,677	7,727
Investment income	3,488	4,572
Gain on sale of land	4,517	-
Change in fair value of investments	(155)	(79)
Interest expense	(6,755)	(7,360)
NET NONOPERATING REVENUES	<u>9,772</u>	<u>4,860</u>
 INCOME BEFORE CONTRIBUTIONS & SPECIAL ITEM	6,055	5,719
Capital contributions from other governments	-	2,114
Special Item		
Prior service cost for post retirement health program	(6,944)	-
CHANGE IN FUND EQUITY	<u>(889)</u>	<u>7,833</u>
 TOTAL FUND EQUITY - Beginning	<u>347,958</u>	<u>340,125</u>
 TOTAL FUND EQUITY - Ending	<u><u>\$ 347,069</u></u>	<u><u>\$ 347,958</u></u>

See Accompanying Notes to Financial Statements

HAMPTON ROADS SANITATION DISTRICT
STATEMENTS OF CASH FLOWS
FOR THE FISCAL YEARS ENDED JUNE 30, 2003 and 2002

Increase (Decrease) in Cash and Cash Equivalents

(In thousands)

	<u>2003</u>	<u>2002</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash received from customers	\$ 94,152	\$ 92,756
Other operating revenues	3,483	3,949
Cash payments to suppliers for goods and services	(44,712)	(39,974)
Cash payments to employees for services	(29,126)	(28,435)
Net cash provided by operating activities	<u>23,797</u>	<u>28,296</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Wastewater facility charges	8,677	7,727
Acquisition and construction of property, plant, and equipment	(23,019)	(19,332)
Capital contributions from other governments	-	2,114
Bond proceeds	4,263	5,854
Proceeds from sale of land	4,517	-
Prior service cost for post retirement health program	(6,944)	-
Principal paid on debt	(15,195)	(14,346)
Interest paid on bonds	(6,890)	(7,451)
Net cash used for capital and related financing activities	<u>(34,591)</u>	<u>(25,434)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Purchases of investments	(272,749)	(106,049)
Sales and maturities of investments	251,071	134,455
Interest and dividends on investments	3,782	5,116
Net cash provided by (used in) investing activities	<u>(17,896)</u>	<u>33,522</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(28,690)	36,384
CASH AND CASH EQUIVALENTS, AT BEGINNING OF YEAR	48,826	12,442
CASH AND CASH EQUIVALENTS, AT END OF YEAR	<u>\$ 20,136</u>	<u>\$ 48,826</u>

Reconciliation of Operating Income (Loss) to Net Cash Provided by Operating Activities

Operating income (loss)	\$ (3,717)	\$ 859
Adjustments to reconcile operating income (loss) to net cash provided by operating activities		
Depreciation	27,475	26,926
(Increase) decrease in operating assets		
Accounts receivable	311	(1,063)
Net change in other current assets	(612)	106
Increase (decrease) in operating liabilities		
Trade and contracts payable	480	479
Accrued salaries and wages	129	30
Compensated absences	280	910
Net change in other liabilities	(549)	49
NET CASH PROVIDED BY OPERATING ACTIVITIES	<u>\$ 23,797</u>	<u>\$ 28,296</u>

See Accompanying Notes to Financial Statements

**HAMPTON ROADS SANITATION DISTRICT
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2003 and 2002**

NOTE 1-GENERAL INFORMATION

Organization and Administration

The Hampton Roads Sanitation District (HRSD) was created by the Virginia General Assembly in 1940, as a political subdivision of the Commonwealth of Virginia (the Commonwealth), to construct, maintain, and operate a wastewater treatment system in the Hampton Roads area. The Hampton Roads Sanitation District Commission (the Commission) is constituted as HRSD's governing body and consists of eight members, appointed by the Governor. The Commission's functions were updated by Chapter 66 of the Acts of the Assembly of Virginia of 1960, as amended. The administration of HRSD is under the control of a general manager, supported by five departmental directors.

Regulatory Oversight

HRSD's operations are subject to regulations established by the United States Environmental Protection Agency and the Virginia Department of Environmental Quality. HRSD currently meets all of its permit requirements. Changes in these regulations could require HRSD to modify its treatment processes and require additional capital expenditures.

Purpose of HRSD

HRSD was created for the specific purpose of abating pollution in the Hampton Roads area through the interception of existing wastewater outfalls, installation of interception service into new areas as necessary, and providing treatment facilities. HRSD provides points of interception throughout the area. The responsibility of providing lateral sewers and subtrunk facilities to carry sewage from industries, residences, and businesses is primarily the responsibility of the local municipal governments.

Corporate Limits of HRSD

The geographical limits of HRSD include:

City of Chesapeake	City of Suffolk	King and Queen County
City of Hampton	City of Virginia Beach	King William County
City of Newport News	City of Williamsburg	Mathews County
City of Norfolk	Gloucester County	Middlesex County
City of Poquoson	Isle of Wight County	York County
City of Portsmouth	James City County	

NOTE 2-SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

HRSD is a political subdivision of the Commonwealth and a government instrumentality. The Commission, which is the governing board of HRSD, was granted corporate powers by the General Assembly. The Governor appoints the Commission members, who serve at his pleasure, thereby making HRSD a reportable component unit of the Commonwealth. The Commonwealth is not obligated by the debt of the Commission. The Commission is for the benefit of the inhabitants of the HRSD geographical area. HRSD derives its revenue primarily from charges for wastewater treatment services. HRSD has no property assessment authority. The Commission has no influence in the selection of the governing authority or management personnel of the jurisdictions it serves, nor does it have any influence in their operations or financial matters. Accordingly, the accompanying financial statements present only the accounts of HRSD.

Basis of Accounting

The accompanying financial statements report the financial position and results of operations of HRSD in accordance with generally accepted accounting principles. Because HRSD is a political subdivision of the Commonwealth, the preparation of HRSD's financial statements are governed by the pronouncements of the Governmental Accounting Standards Board (GASB). These statements are prepared on an enterprise fund basis and present HRSD's operating revenues and expenses in a manner similar to a private business, where the costs, including depreciation, of providing services to the general public on a continuing basis are financed or recovered primarily through user charges.

An enterprise fund, a proprietary fund type, is accounted for on an economic resources measurement focus. All assets and liabilities, whether current or noncurrent, associated with its activities are included on its balance sheet. Proprietary fund type operating statements present increases (revenues) and decreases (expenses) in fund equity. The financial statements are presented using the accrual basis of accounting, whereby revenues are recognized when earned and expenses are recognized when incurred.

Budget

HRSD operates in accordance with an annual budget, prepared on a modified accrual basis, which is adopted by the Commission for each fiscal year. Budgetary control is at the departmental level. Any amendments to the budget require Commission approval. All operating budget appropriations lapse at the end of the fiscal year.

Cash Equivalents

All short-term investments that are highly liquid are considered to be cash equivalents. Cash equivalents are readily convertible to known amounts of cash, and at the day of purchase, have a maturity date of no longer than three months.

Investments

Investments, which consist primarily of U.S. government obligations including agencies, are stated at fair value when the original maturity is greater than a year. Investments with an original maturity of one year or less are stated at cost, net of any unamortized premium or discount.

Allowance for Uncollectible Accounts

HRSD provides an allowance for estimated uncollectible accounts receivable based on bad debt experience. The balance in the allowance for uncollectible accounts is considered by management to be sufficient to cover anticipated losses on reported receivable balances.

Property, Plant, and Equipment

Property, plant, and equipment purchased or constructed are stated at cost, including interest cost on funds borrowed to finance the construction of major capital additions. The capitalization threshold is \$5,000. Donated assets are stated at market value. Property, plant, and equipment are depreciated using the straight-line method over the following estimated useful lives:

Treatment plants and buildings	30 years
Interceptor systems	50 years
Office furniture and equipment	5-10 years
Automotive	5 years
Other equipment	5 years

Depreciation recognized on property, plant, and equipment is charged as an expense against operations.

Revenue Recognition

Wastewater treatment charges are computed based on water consumption. These charges are recognized as revenue when billed. Unbilled revenues through June 30 of each fiscal year are accrued at year-end.

Wastewater facility charges are computed based on the water meter size and are received and recognized as revenue in advance of a building permit being issued.

Operating and Nonoperating Revenue and Expenses Recognition

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses result from providing services and producing and delivering goods in connection with HRSD principal service of providing wastewater treatment. The majority of operating revenues is from wastewater treatment, but other associated miscellaneous services and charges are also included. Revenues and expenses not meeting the operating definition are reported as nonoperating. These consist mainly of wastewater facility charges, interest income and interest expense.

Employee Benefits

All permanent employees earn annual leave upon starting a full-time position. The amount of leave earned is based upon the employee's years of service and is expensed as employees earn the right to these benefits. The maximum annual leave an employee may accumulate at year-end varies by the years of service with the maximum being 54 days. An employee has a vested right to the full amount of annual leave earned.

All permanent employees earn eight hours per month of sick leave regardless of the years of service. The amount of sick leave that may be accumulated is unlimited. An employee has vested rights to 35% of accumulated sick leave to a maximum of \$10,000 after five years of service with HRSD.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions. These estimates affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from management's estimates.

Proprietary Activity Accounting and Financial Reporting

In accordance with GASB Statement No. 20, "Accounting and Financial Reporting for Proprietary Funds and other Governmental Entities that use Proprietary Fund Accounting," HRSD applies all applicable GASB pronouncements, and has elected to apply only those FASB Statements and Interpretations, APB Opinions, and Accounting Research Bulletins, issued on or before November 30, 1989, that do not conflict with or contradict GASB Pronouncements.

Disclosure Requirements

The Governmental Accounting Standards Board has issued GASB Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*, which establishes financial reporting standards for state and local governments, including states, cities, towns, villages, and special-purpose governments such as school districts and public utilities. It establishes that the basic financial statements and required supplementary information for general-purpose governments should consist of management's discussion and analysis, basic financial statements, and required supplementary information. HRSD has adopted the provisions of GASB 34 effective July 1, 2001.

NOTE 3- DEPOSITS AND INVESTMENTS

Deposits

Custodial Credit Risk. Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. At year-end, the carrying value of HRSD's deposits was \$1,315,000 and the bank balance was \$2,025,000. Of the bank balance, \$1,977,000 was covered by federal depository insurance or collateralized in accordance with the Virginia Security for Public Deposits Act, except for the fact that the State Treasury Board notified the HRSD that Bank of America was not properly collateralized in accordance with the Act. Under the Act, banks holding public deposits in excess of the amounts insured by the Federal Deposit Insurance Corporation (FDIC) must pledge collateral in the amount of 50% of excess deposits to a collateral pool in the name of the State Treasury Board. If any member financial institution, whose public deposits are collateralized in accordance with the requirements of the Act, fails, the entire market value of the collateral pool becomes available to satisfy the claims of governmental entities. If the value of the pool's collateral were inadequate to cover a loss, additional amounts would be assessed on a pro rata basis to the members of the pool. The State Treasury Board is responsible for monitoring compliance with the collateralization and reporting requirements of the Act and for notifying local governments of compliance by banks.

Credit Risk. HRSD invests overnight in money market accounts that are invested in government securities and the Commonwealth of Virginia Local Government Investment Pool (LGIP). As of June 30, 2003, HRSD's had deposits in Merrill Lynch's Government Fund that was rated AAA by Standard & Poor's. The Treasury Board of Virginia provides LGIP oversight.

Concentration of Credit Risk. The \$12,087,000 invested in the LGIP and the \$4,763,000 invested in Merrill Lynch's Government Fund (SEC registered) are not classified by risk categories because they are not evidenced by securities that exist in physical or book entry form as defined by GASB Statement No. 3. Both funds share price valuations use a constant \$1.00 net asset value. HRSD Investment Policy allows 25% each in deposits in money market funds and LGIP.

Investments

As of June 30, 2003, HRSD had the following investments and maturities. (Amounts are in thousands)

<u>Investment Type</u>	<u>Fair Value</u>	<u>Investment Maturities (In Years)</u>		
		<u>Less Than 1</u>	<u>1-3</u>	<u>4-6</u>
U.S. Agencies	\$65,124	\$ 2,994	\$12,919	\$49,211
Commercial Paper	4,000	4,000	--	--
Corporate Bonds	3,016	3,016	--	--
Municipal Securities	1,535	1,535	--	--
Total	<u>\$73,675</u>	<u>\$11,545</u>	<u>\$12,919</u>	<u>\$49,211</u>

Interest Rate Risk. HRSD's Investment Policy does not limit maturities as a means of managing its exposure to fair value losses arising from increasing interest rates. Most of the U.S. Agencies have a call provision on a monthly or quarterly schedule, and we expect most to be exercised before maturity. Subsequent to year-end, \$13 million were called that were classified in the 4 to 6 year table above.

Custodial Credit Risk. For an investment, custodial credit risk is the risk that, the event of the failure of the counterparty, HRSD will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. HRSD utilizes its Trustee, The Bank of New York, as recipient of all investment transactions on a delivery versus pay basis. At year-end, the Trust Department of the Bank of New York held all \$73,675,000 in investments in the Trustee name for HRSD.

Credit Risk. HRSD's Trust Agreement requires HRSD to invest and reinvest in investment obligations that are approved by the Commonwealth of Virginia. State law limits investments in commercial paper to the top two ratings issued by nationally recognized statistical rating organizations (NRSROs). HRSD's Investment Policy limits its investments, in this investment type to the top rating issued by NRSROs. As of June 30, 2003, HRSD's

investments in commercial paper were rated A-1 by Standard & Poor's, and P-1 by Moody's Investors Service. HRSD's investment in Federal Home Loan Banks securities were rated AAA by Standard & Poor's and Aaa by Moody's Investors Service.

Concentration of Credit Risk. HRSD's Investment Policy includes a 5% maximum for each issuer of Banker's Acceptance, Certificates of Deposit, Municipal Securities, Commercial Paper, and Corporate Notes. More than 5 percent of HRSD investments are in Federal Home Loan Banks securities. HRSD's Investment Policy requires a minimum of 30% in government paper. At June 30, 2003 HRSD portfolio contained 80% government paper.

The change in fair value is calculated as follows (in thousands):

	2003	2002
Fair value of investments, end of year	\$ 73,675	\$ 52,152
Add: Proceeds of investments during the year	251,071	134,455
Less: Cost of investments purchased during the year	272,749	106,049
Less: Fair value of investments, beginning of year	52,152	80,637
Change in fair value of investments	<u>\$ (155)</u>	<u>\$ (79)</u>

NOTE 4-ALLOWANCE FOR UNCOLLECTABLE ACCOUNTS

An analysis of the allowance for uncollectable accounts at June 30 is as follows (in thousands):

	2003	2002
Balance, beginning of year	\$ 900	\$ 575
Add: Current provision for uncollectable accounts	465	1,173
Less: Charge-off of uncollectable accounts	665	848
Balance, end of year	<u>\$ 700</u>	<u>\$ 900</u>

NOTE 5-PROPERTY, PLANT, AND EQUIPMENT

Property, plant, and equipment activity for the year ended June 30 was as follows (in thousands):

	Balance at 6/30/01			Balance at 6/30/02			Balance at 6/30/03
	Balance	Additions	Retirements	Balance	Additions	Retirements	Balance
Non-Depreciable Capital Assets							
Land	\$ 3,558	\$ 114	\$ -	\$ 3,672	\$ 749	\$ -	\$ 4,421
Construction in Progress	18,717	9,607	(12,541)	15,783	12,055	(7,529)	20,309
Depreciable Capital Assets							
Treatment plants	537,870	13,254	-	551,124	7,286	-	558,410
Interceptor systems	194,389	5,037	-	199,426	6,893	-	206,319
Small community facilities	2,513	2,086	-	4,599	198	-	4,797
Buildings	16,916	12	(351)	16,577	2,314	-	18,891
Office equipment	8,781	632	-	9,413	565	-	9,978
Automotive	7,313	670	(191)	7,792	318	(83)	8,027
Other equipment	6,046	548	-	6,594	216	-	6,810
Total	796,103	31,960	(13,083)	814,980	30,594	(7,612)	837,962
Less accumulated depreciation:							
Treatment plants	(305,153)	(19,825)	-	(324,978)	(20,618)	-	(345,596)
Interceptor systems	(62,890)	(3,717)	-	(66,607)	(3,820)	-	(70,427)
Small community facilities	(126)	(695)	-	(821)	(432)	-	(1,253)
Buildings	(6,726)	(617)	348	(6,995)	(655)	-	(7,650)
Office equipment	(6,127)	(1,055)	-	(7,182)	(951)	-	(8,133)
Automotive	(5,843)	(546)	191	(6,198)	(582)	68	(6,712)
Other equipment	(4,916)	(471)	-	(5,387)	(417)	-	(5,804)
Total accumulated depreciation	(391,781)	(26,926)	539	(418,168)	(27,475)	68	(445,575)
Net property, plant, and equipment	<u>\$404,322</u>	<u>\$ 5,034</u>	<u>\$ (12,544)</u>	<u>\$396,812</u>	<u>\$ 3,119</u>	<u>\$ (7,544)</u>	<u>\$392,387</u>

NOTE 6-COMPENSATED ABSENCES

The liability for vested annual, sick, and compensatory leave at June 30 is as follows (in thousands):

	<u>2003</u>	<u>2002</u>
Annual leave	\$ 2,707	\$ 2,491
Sick leave	2,685	2,619
Compensatory leave	38	40
Total	<u>\$ 5,430</u>	<u>\$ 5,150</u>

NOTE 7-EMPLOYEE BENEFITS

Post Retirement Health Benefit Plan

HRSD's Commission adopted a post-retirement health benefit for qualifying employees beginning after July 1, 2002. The program furnishes health and dental benefits for life for all employees with at least 15 years of service at HRSD and who also qualify for an unreduced retirement benefit through the Virginia Retirement System. The program allows the retiree at their expense to cover their spouse and dependent under HRSD's health care provider. HRSD funded the estimated prior service cost of approximately \$7,000,000 in a separate trust established for this purpose from the sale of land and additional designated revenue. For the year ended June 30, 2003 the estimated ongoing annual required contribution is approximately \$500,000, and is funded through operations.

Defined Benefit Pension Plan

Plan Description:

HRSD contributes to the Virginia Retirement System (VRS), an agent and cost-sharing multiple-employer defined benefit pension plan, which acts as a common investment and administrative agent for political subdivisions in the Commonwealth of Virginia. All full-time permanent employees of HRSD are covered by VRS. Benefits vest after 5 years of service. Employees are eligible for an unreduced retirement benefit at age 65 with 5 years of service and at age 55 with 30 years of service. Employees who retire with an unreduced benefit are entitled to an annual retirement benefit payable monthly for life in an amount equal to 1.7 percent of their average final salary (AFS) for each year of credited service. AFS is defined as the highest consecutive 36 months of salary. In addition, retirees qualify for annual cost-of-living increases beginning in their second year of retirement. The cost of living adjustment is limited to 5% per year. Benefits are actuarially reduced for retirees who retire prior to becoming eligible for full retirement benefits. The VRS also provides death and disability benefits. Title 51.1 of the Code of Virginia (1950), as amended, assigns the authority to establish and amend benefit provisions to the General Assembly of Virginia.

VRS issues a publicly available comprehensive annual financial report that includes financial statements and required supplemental information for VRS. A copy of that report may be obtained by writing to VRS at P.O. Box 2500, Richmond, VA, 23218-2500.

At June 30, 2002, the date of the most recent valuation, the plan contained 642 active, 212 inactive and 168 retired employees from HRSD. The information presented in the required supplemental schedules was determined as part of the actuarial valuations at the dates indicated. Additional information as of the latest actuarial valuation follows:

Actuarial cost method	Entry Age Normal
Amortization cost method	Level percent, Open
Payroll growth rate	3%
Remaining amortization period	18 Years
Asset valuation method	Modified Market
Actuarial assumptions:	
Investment rate of return ¹	8%
Projected salary increases ¹	4.25% to 6.10%
Cost-of-living adjustments	3%

¹ includes inflation at 3%

There were no significant changes in actuarial assumptions or employee pension benefit provisions between those used in the 2002 valuation and those used in the prior evaluation that would significantly affect the valuation.

Funding Policy:

Employees are required by Title 51.1 of the Code of Virginia (1950), as amended, to contribute 5% of their annual salary to the VRS. This 5% member contribution has been assumed by HRSD. In addition, HRSD is required to contribute the remaining amounts necessary to fund its participation in the VRS using the actuarial basis specified by the statute and approved by the VRS Board of Trustees. The HRSD contribution rate for the fiscal year ended June 30, 2003 was 1.0% of annual covered payroll. The payroll for employees covered by VRS for the years ended June 30, 2003 and 2002 was \$27,033,000 and \$26,485,000, which was 91.5% and 90.2% of total payrolls of \$29,535,000 and \$29,375,000, respectively. Actual contributions by HRSD totaled \$1,622,000, \$1,591,000, and \$1,556,000, which is 100% of the Annual Required Contribution (ARC) for 2003, 2002, and 2001 respectively. HRSD has no Net Pension Obligation at June 30, 2003.

Trend Information:

Historical trend information gives an indication of the progress made in accumulating sufficient assets to pay benefits when due. Summarized information provided by the VRS for actuarial valuations of HRSD employees are presented below as required supplementary information.

		Schedule of Funding Progress (unaudited)							
(in thousands)									
Valuation Date	June 30,	(1)	2002	2001	2000	1999	1998	1996	1994
Actuarial Value of Assets (AVA)		(2)	\$85,897	\$82,998	\$75,301	\$64,655	\$55,539	\$39,392	\$30,291
Actuarial Accrued Liability (AAL)		(3)	\$70,586	\$63,006	\$56,985	\$57,205	\$49,580	\$39,645	\$27,001
Unfunded Actuarial Accrued Liability (UAAL) (3)-(2)		(4)	(\$15,311)	(\$19,992)	(\$18,316)	(\$7,450)	(\$5,959)	\$253	(\$3,290)
Funded Ratio (2)/(3)		(5)	122%	132%	132%	113%	112%	99%	112%
Annual Covered Payroll		(6)	\$26,634	\$25,459	\$23,947	\$22,991	\$23,399	\$22,271	\$20,327
UAAL as a % of Payroll (4)/(6)		(7)	(57.5%)	(78.5%)	(76.5%)	(32.4%)	(25.5%)	1.1%	(16.2%)

NOTE 8-BONDS PAYABLE

All bonds are secured by the revenues of HRSD and are payable serially over the duration of each issue. A summary of activity for the year ended June 30 was as follows:

	Balance at 6/30/01	Additions	Deductions	Balance at 6/30/02	Additions	Deductions	Balance at 6/30/03
Series-1993	\$ 86,790	\$ -	\$ 10,940	\$ 75,850	\$ -	\$ 11,405	\$ 64,445
Virginia Resource Authority	<u>74,680</u>	<u>5,854</u>	<u>3,406</u>	<u>77,128</u>	<u>4,263</u>	<u>3,790</u>	<u>77,601</u>
Total Bonds Outstanding	<u>\$161,470</u>	<u>\$5,854</u>	<u>\$14,346</u>	<u>\$152,978</u>	<u>\$4,263</u>	<u>\$15,195</u>	<u>\$142,046</u>

A summary of the primary bonds outstanding at June 30, 2003 is as follows:

PRIMARY	(in thousands)				Original Interest Cost	Duration of Issue	Final Maturity October 1,
	Total Amount	Principal Outstanding Current	Principal Outstanding Long-Term	Interest to Maturity			
Series-1993	\$64,445	\$7,240	\$57,205	\$26,674	4.98%	30 years	2023

Maturities of primary bond principal and interest are as follows (in thousands):

<u>June 30,</u>	<u>Principal</u>	<u>Interest</u>
2004	\$ 7,240	\$ 3,003
2005	6,185	2,691
2006	6,350	2,395
2007	6,630	2,082
2008	3,045	1,843
2009-2013	13,635	6,967
2014-2018	2,625	4,749
2019-2023	15,220	2,856
2024	3,515	88
	<u>\$64,445</u>	<u>\$26,674</u>

HRSD is indebted to the Virginia Water Facilities Revolving Fund from the issuance of several bonds with interest rates ranging from 2.5% to 4.75%. One loan is still in the draw down stage of the bond agreement, as indicated in the table below. The final amounts for principal borrowed cannot be determined until the loan is completed, the interest to maturity was determined assuming the full loan is drawn. A summary of the secondary bonds outstanding at June 30, 2003 is as follows:

SECONDARY

SECONDARY	(in thousands)			Interest to Maturity	Original Interest Cost	Duration of Issue	Final Maturity	
	Maximum Draw Down Available	Principal Outstanding						
		Total	Current					Long-term
Smithfield		\$11,938	\$ 793	\$11,145	\$ 3,210	4.00%	20 years	June 1, 2015
Nansemond I		31,596	1,806	29,790	9,602	4.00%	20 years	Dec 1, 2016
Nansemond II		12,323	704	11,619	3,745	4.00%	20 years	Dec 1, 2016
CE/AB		4,378	227	4,151	1,665	4.75%	20 years	June 1, 2017
Disinfection		5,882	258	5,624	1,972	3.50%	20 years	Mar 1, 2020
Middle Peninsula		388	15	373	187	4.75%	20 years	Dec 1, 2020
AT/BH Generator		3,643	140	3,503	1,543	4.10%	20 years	June 1, 2021
BH Odor Control		2,263	89	2,174	830	3.50%	20 years	Sep 1, 2021
York River Reuse		2,476	100	2,376	668	2.50%	20 years	Sep 1, 2022
AB Aeration		1,759	63	1,696	736	3.75%	20 years	Oct 1, 2022
Ches-Eliz Off Gas	\$ 1,070	955	19	936	482	3.75%	20 years	Mar 1, 2023
Total	\$ 1,070	\$77,601	\$4,214	\$73,387	\$24,640			

Maturities of secondary bond principal and interest are as follows (in thousands):

<u>June 30,</u>	<u>Principal</u>	<u>Interest</u>
2004	\$ 4,214	\$ 3,036
2005	4,400	2,853
2006	4,576	2,677
2007	4,761	2,494
2008	4,951	2,303
2009-2013	27,895	8,374
2014-2018	23,049	2,630
2019-2023	3,755	273
	<u>\$77,601</u>	<u>\$24,640</u>

NOTE 9-FUND EQUITY

Restricted for Debt Service

In addition to a general pledge of its revenues as security for its bondholders, HRSD's Master Trust Indenture requires HRSD to designate sinking funds on a monthly basis. HRSD was in compliance with these requirements during the fiscal years ended June 30, 2003 and 2002.

Reserved for Improvement

HRSD's Master Trust Indenture requires a reserve for improvements. There is no specific funding mechanism established by the Trust agreement; the balance in the account at June 30, 2003 and 2002 is \$10,779,000 and \$9,359,000 and is contained in the Fund Equity Unrestricted. HRSD was in compliance with all funding requirements of this reserve during the fiscal years ended June 30, 2003 and 2002.

Reserved for Construction

A reserve for the construction program is based on funds designated by HRSD's Commission for such purposes. At June 30, 2003 and 2002, \$39,006,000 and \$50,372,000 were contained in the Fund Equity Unrestricted.

NOTE 10-RISK MANAGEMENT

HRSD is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; employee dishonesty; injuries to employees; and natural disasters. HRSD purchases commercial insurance for specific types of coverage including property, liability, auto, health, crime, public officials, and worker's compensation. There were no significant reductions in insurance coverage from the prior year. Claim settlements and judgments not covered by commercial insurance are covered by operating resources. The amount of settlements did not exceed insurance coverage for each of the past three years. Claim expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated.

APPENDIX B

Schedule of Rates and Charges

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**HAMPTON ROADS SANITATION DISTRICT
RATE SCHEDULE
[Excerpted]**

For Wastewater and Associated Charges Effective
July 1, 2003

I. WASTEWATER TREATMENT CHARGE

A. METERED PUBLIC (OR NON-GOVERNMENT UTILITY WATER SUPPLY)

	<u>Per 100 Cubic Feet</u>
For the first 30 CCF* per 30 day period	\$1.39
In excess of 30 CCF* per 30 day period	\$1.24
	<u>Per 30 day Period</u>
Minimum charge for 2 CCF* or less	\$3.96
*CCF=100 Cub Feet (Approx. 748 gallons)	

B. PRIVATE WATER SUPPLY

1. Resident, Non-metered (Based on number of toilets)

	<u>Per 30 day Period</u>
First toilet	\$6.27
Second toilet	\$4.18
Each additional toilet	\$2.09

2. Residential, Metered

- a. At the customer's opinion, in lieu of charges based on the number of toilets, a meter may be purchased, permanently installed and maintained at the customer's expense.
- b. The customer is required to provide to HRSD a meter reading by the tenth day of each month. Charges will be based on the schedule in Section A. In the event a valid meter reading is not received by the tenth day of the month, HRSD will bill the customer based upon the schedule in Section I.B.1. Refunds or adjustments on billings where customers were at fault in not properly supplying the meter reading will not be authorized.
- c. All meters installed are subject to periodic inspection and reading by HRSD personnel to ensure the accuracy of billings. Meters may be required, at customer's expense, to be certified as accurate to manufacturer's specifications. A copy of the certification, if required, must be provided to HRSD. Meters installed after July 1, 1992 must be installed in such a manner to provide one person access as defined in HRSD's confined space entry program.

3. Non-Residential, Metered

- a. Meters must be purchased, permanently installed and maintained at the customer's expense.
- b. The customer is required to provide HRSD a meter reading by the tenth day of each month. Charges will be based on the schedules in Section I.A. & D. In the event the meter reading is not received by the tenth day of the month, HRSD will bill estimated wastewater Treatment charges (and applicable surcharges) based upon a consumption as determined appropriate by HRSD. In the event the customer fails to provide a meter

reading for a third consecutive month, HRSD will read the meter and calculate wastewater treatment charges (and applicable surcharges) based on consumption since the last actual meter reading less consumption on the estimated billings. A meter reading charge will be assessed.

- c. All meters installed are subject to periodic inspection and reading by HRSD personnel to ensure the accuracy of billings. Meters may be required, at customer's expense, to be certified as accurate to manufacturer's specifications. A copy of the certification, if required, must be provided to HRSD. Meters installed after July 1, 1992 must be installed in such a manner to provide one person access as defined in HRSD's confined space entry program.
- d. Defective meters must be repaired or replaced. Billing in the interim will be based on an estimate by HRSD and the appropriate adjustment will be made based on six months of metered consumption using repaired or replaced meters.

* * *

D. **SURCHARGES**

1. <u>High Strength or Unusual Waste</u>	<u>Per Hundred Pounds</u>
a. Biochemical Oxygen Demand (BOD) In Excess of 250 milligrams/liter	\$ 22.22
b. Total Suspended Solids (TSS) In excess of 250 milligrams/liter	\$ 19.13
c. Phosphorus (PO ₄ P) In excess of 6 milligrams/liter	\$ 167.00
d. Total Kjeldahl Nitrogen (TKN) In excess of 35 milligrams/liter	\$ 22.90
e. Unusual wastes not covered by this rate schedule will be considered separately and may be assigned a special rate.	

2. Survey

HRSD may make an initial wastewater monitoring survey of the discharge to determine the applicability of the surcharge. Based on survey results HRSD may institute the surcharge and/or require the customer to provide such tests and equipment as will provide adequate basis for the surcharge to be made. Where the wastewater discharge is subject to surcharge, the surcharge may be based on the normal characteristics of waste from such operations as determined from industrial, or chemical, or engineering tests, or other appropriate reference or wastewater surveys of discharges from other similar operations.

3. Pretreatment

Wastewater discharge limitations may be imposed by HRSD to protect transmission and treatment structures or processes and to insure compliance with Federal and State effluent limitation guidelines. Pretreatment before discharge or elimination of the discharge may be required to meet limitations of toxic or other guidelines or to remove any type of waste/alter and manner of discharge determined by HRSD to be detrimental to either transmission and treatment structures or process.

4. Damage to Facilities

In the event that either transmission or treatment structures or processes are damaged, or the flow through said structures or processes is hampered by a customer's wastewater discharge, HRSD may make or require to be made, at the customer's expense, such

repairs as are necessary to restore transmission or treatment structures or processes to normal system operation.

* * *

II. WASTEWATER FACILITY CHARGE (FACILITY CHARGE)

A. TABLE OF CHARGES

The wastewater facility charge covers the cost of treatment capacity expansion as well as line extensions and pump stations. A facility charge is applied to residential, commercial, or industrial new connections to any sewer or sewer system discharging into HRSD facilities or if an existing connection is increased. If septic tank is converted to existing sanitary sewer or sewer system, the appropriate facility charge will be abated for comparable service.

<u>Water Meter Size</u>	<u>Facility Charge</u>
5/8 Inch	\$ 1,300
¾ Inch	\$ 1,975
1 Inch	\$ 3,680
1 ½ Inch	\$ 8,935
2 Inch	\$ 16,735
3 Inch	\$ 40,525
4 Inch	\$ 75,970
6 Inch	\$ 184,120
8 Inch	\$ 344,940
10 Inch	\$ 561,460

B. HIGH STRENGTH OR VOLUME WASTE

In addition to the above charge, when a new user's high strength or high volume wastewater impacts HRSD facilities to such an extent that special modification and/or expansion is required, an additional Facility Charge may be assessed. This additional Facility Charge shall be calculated based on those capital expenditures required to provide service to the affected user.

C. WHEN PAYABLE

The Facility Charge shall be due and payable prior to the issuance of a building permit/sewer permit by the local jurisdiction. The Facility Charge shall also be due and payable prior to the renewal and/or re-issuance of a building permit, except in cases where the applicable Facility Charge was paid when the building permit was originally issued.

* * *

V. **TEMPORARY EQUALIZATION CHARGE**

A. **BACKGROUND**

HRSD's billing is based on water usage because this is the most convenient way to allocate costs, but it is not truly representative of the actual costs incurred to treat the waste materials in the water. For instance, with a water usage of 75% of normal, the treatment costs are decreased by only about 6% since fixed charges and the costs to treat the same amount of waste materials in the water are not decreased; however, the customer's payments are lowered by 25%. This results in an inequity because the customer on water rationing is no longer paying for the full value of services received. The equalization charge would increase the bill for a customer on 75% water rationing by 19% to 94% of their normal bill. The remaining 6% would reflect the reduced cost of treatment a smaller quantity of water.

B. **EQUALIZATION CHARGE**

To offset the inequity caused by water rationing, a temporary equalization charge will be added to that portion of the Wastewater Treatment Service Charge applicable to flow for all customers who are on water rationing. The equalization charge will be lifted when water service is restored to normal. The charge is based on the water rationing allocation percentage as follows (other allocations prepared accordingly):

<u>% Water Rationing Allocation</u>	<u>HRSD Charge Increased by</u>	<u>% of Normal HRSD Bill</u>
75%	19%	94%
70%	23%	93%
65%	27%	92%
60%	31%	91%
55%	35%	90%
50%	39%	89%

The following categories of accounts are exempt:

1. Private well water accounts
2. Any accounts that are in a water rationing exempt status by the cities

In the event that a customer is fined by the City for excessive consumption, the customer may request an adjustment to the equalization charge. An administrative fee will be charged to cover the cost of processing this adjustment.

For other adjustments an "Adjustment Review Panel" is appointed consisting of one member from the Commission, one member from HRSD's Staff and the third member from HRSD's consulting engineers. This Panel will render a final decision on any matter brought to it.

**HAMPTON ROADS SANITATION DISTRICT
RATE SCHEDULE - TOWN OF URBANNA**

For All Wastewater and Associated Charges Effective November 1, 2003

*Minimum set at 6,000 gallons bi-month water usage
Total Wastewater Rate
Minimum Bill

Per 1000 Gallons
\$ 7.94
\$47.64

**HAMPTON ROADS SANITATION DISTRICT
RATE SCHEDULE - TOWN OF WEST POINT**

For All Wastewater and Associated Charges Effective November 1, 2003

*Minimum set at 6,000 gallons bi-month water usage	Per 1000 Gallons
Total Wastewater Rate	\$ 6.36
Minimum Bill	\$38.16

HAMPTON ROADS SANITATION DISTRICT

RATE SCHEDULE - MATHEWS COUNTY

For All Wastewater and Associated Charges Effective November 1, 2003

Unit Cost	\$6.29/1000 gallons
*ERU Usage	12,000 gallons/quarter
ERU Rate	\$75.48/quarter

The amount charged Mathews residential customers is a flat rate based on an equivalent residential water usage (ERU) of 12,000 gallons per quarter. All others, including commercial, government and professional customers, are charged based on a schedule of fractions or multiples of the ERU as appropriate for each customer category. This schedule is derived from information supplied by the Mathews Courthouse Sanitary District and may be subject to verification or revision.

**Hampton Roads Sanitation District
Rate Schedule
Wastewater Treatment Charges
Last Ten Years**

	<u>2003</u>	<u>2001</u>	<u>2000</u>	<u>1999</u>	<u>1997</u>	<u>1996</u>	<u>1995</u>	<u>1994</u>
Residential-metered								
First 3,000 cubic feet per month or 9,000 cubic feet per quarter	\$1.36	\$1.32	\$1.26	1.22	\$1.20	\$1.17	\$1.10	\$1.05
In excess of 3,000 cubic feet per month, in excess of 9,000 cubic feet per quarter,	1.22	1.17	1.11	1.09	1.08	1.05	1.00	0.97
Minimum charges*								
Less than 200 cubic feet, billed monthly	3.86	3.75	3.60	3.50	3.45	3.35	3.15	3.00
Less than 500 cubic feet, billed bimonthly	7.72	7.50	7.20	7.00	6.90	6.70	6.30	6.00
Less than 800 cubic feet, billed quarterly	11.58	11.25	10.80	10.50	10.35	10.05	9.45	9.00
Residential-unmetered								
First toilet								
Billed bimonthly	12.24	11.88	11.34	10.98	10.80	10.50	9.80	9.40
Billed quarterly	18.36	17.82	17.01	16.47	16.20	15.75	14.70	14.05
Second toilet								
Billed bimonthly	8.16	7.92	7.56	7.32	7.20	7.00	6.60	6.35
Billed quarterly	12.24	11.88	11.34	10.98	10.80	10.50	9.90	9.45
Additional each								
Billed bimonthly	4.08	3.96	3.78	3.66	3.60	3.50	3.30	3.10
Billed quarterly	6.12	5.94	5.67	5.49	5.40	5.25	4.95	4.65
Non-residential Special Category								
Biochemical Oxygen Demand (BOD)								
Excess over 250 mg/1 (per 100 pounds)	22.67	22.43	22.88	23.00	23.50	22.90	22.50	22.50
Suspended solids								
Excess over 250 mg/1 (per 100 pounds)	18.88	18.16	17.50	18.25	19.95	19.50	20.50	21.43
Phosphorus								
Excess over 6 mg/1 (per 100 pounds)	147.11	139.00	129.00	120.00	107.50	105.00	109.00	114.00
Total Kjeldahl Nitrogen								
Excess over 35 mg/1 (per 100 pounds)	22.50	20.90	20.36	20.13	42.50	42.50	42.50	31.13
Unusual wastes not covered								
Septic Tank Waste								
Per each 500 gallons or part thereof	22.64	23.00	22.50	23.20	23.15	22.55	21.25	20.25

**Hampton Roads Sanitation District
Rate Schedule
Wastewater Facility Charges
Last Ten Years**

	<u>2003</u>	<u>2002</u>	<u>1999</u>	<u>1997</u>	<u>1996</u>	<u>1993</u>
Residential	\$ 1,240	\$ 1,205	\$ 720	\$ 720	\$ 720	\$ 705
Commercial/Industrial						
5/8" Meter	1,240	1,205	720	720	705	665
3/4" Meter	1,880	1,860	1,110	1,440	1,410	1,330
1" Meter	3,550	3,415	2,040	3,600	3,525	3,325
1-1/2" Meter	8,495	8,285	4,950	10,800	10,575	9,975
2" Meter	15,915	15,515	9,270	20,880	20,445	19,285
3" Meter	38,545	37,575	22,450	52,560	51,465	48,545
4" Meter	72,255	70,410	42,070	108,000	105,750	99,750
6" Meter	175,110	170,640	101,960	241,920	236,880	223,440
8" Meter	328,065	319,810	191,090	403,200	394,800	372,400
10" Meter	533,990	520,360	310,920	590,400	578,100	545,300

Note one charge per connection

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APPENDIX C

Definitions of Certain Terms and Summaries of Documents

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DEFINITIONS OF CERTAIN TERMS

The following is a summary of the definitions of certain terms contained in the Trust Agreement or the Master Indenture and used in this Official Statement:

“Additional Indebtedness” means any Indebtedness incurred by the District subsequent to the issuance of the initial Obligation under the Master Indenture or incurred by any other Member of the Obligated Group subsequent to or contemporaneously with its becoming a Member of the Obligated Group.

“Audited Financial Statements” means financial statements of the Designated Units of the District. Audited Financial Statements of the District shall also include, in an additional information section, unaudited combining financial statements for the same twelve-month period from which the accounts of any affiliate or subsidiary of the District which is not a Member of the Obligated Group have been eliminated and to which the accounts of any Member of the Obligated Group which is not an affiliate or a subsidiary have been added; provided, however, that for purposes of adding the accounts of a Member of the Obligated Group which is not an affiliate or subsidiary of the District, the balances of such accounts shall be extracted from audited financial statements of such Member of the Obligated Group and its affiliates or subsidiaries, if any.

“Average Annual Debt Service” means, at any given time of determination, average annual Principal and Interest Requirements for the Series 2003 Bonds until their final maturity.

“Balloon Long-Term Indebtedness” means Long-Term Indebtedness 25% or more of the principal payments of which are due in a single year, which portion of the principal is not required by the documents pursuant to which such Indebtedness is issued to be amortized by redemption prior to such date.

“Bond Fund” means the Hampton Roads Sanitation District, Virginia Wastewater Refunding Revenue Bonds, Series 2003 Bond Fund created and so designated by the Trust Agreement.

“Bond Registrar” means the Bond Registrar at the time serving as such under the Trust Agreement whether the original or a successor bond registrar.

“Bond Trustee” means the Bond Trustee at the time serving as such under the Trust Agreement, whether the original or successor Trustee, which shall initially be The Bank of New York, New York, New York and its successors in the trusts created under the Trust Agreement.

“Bond Year” means the period commencing on October 1 of any year and ending on September 30 of the following year.

“Business Day” means any day on which banks in the city in which the principal corporate trust office of the Bond Trustee is located and in New York, New York are open for commercial banking purposes,

“Closing” means the date on which the Trust Agreement becomes legally effective, the same being the date on which the Series 2003 Bonds are delivered against payment therefor.

“Code” means the Internal Revenue Code of 1986, as amended.

“Commission” means the Hampton Roads Sanitation District Commission, which is the governing body of the District.

“Completion Indebtedness” means any Long-Term Indebtedness incurred by any Member of the Obligated Group for the purpose of financing the completion of facilities for the acquisition, construction or equipping of which Long-Term Indebtedness has theretofore been incurred in accordance with the provisions of the Master Indenture, to the extent necessary to provide a completed and equipped facility of the type and scope contemplated at the time that such Long-Term Indebtedness theretofore incurred was originally incurred, and, to the extent the

same shall be applicable, in accordance with the general plans and specifications for such facility as originally prepared with only such changes as have been made in conformance with the documents pursuant to which such Long-Term Indebtedness theretofore incurred was originally incurred.

"Consultant" means a firm or firms which are not, and no member, stockholder, director, officer, trustee or employee of which is, an officer, director, trustee or employee of any Member of the Obligated Group, and which is a professional management or engineering consultant of national repute for having the skill and experience necessary to render the particular report required by the provision of the Master Indenture in which such requirement appears.

"Contracted Services" means services rendered or facilities provided to a Member of the Obligated Group for the performance for or on behalf of such Member of the Obligated Group of functions similar to those performed by such Member of the Obligated Group from a specific project, projects or systems, pursuant to a contract, whether a financing lease, a service agreement or another arrangement.

"Credit Facility" means a line of credit, letter of credit, standby bond purchase agreement or similar credit enhancement or liquidity facility established to provide credit or liquidity support for indebtedness.

"Crossover Date" means, with respect to Cross-over Refunding Indebtedness, the date on which the principal portion of the related Cross-over Refunded Indebtedness is to be paid or redeemed from the proceeds of such Cross-over Refunding Indebtedness.

"Crossover Refunded Indebtedness" means Indebtedness refunded by Cross-over Refunding Indebtedness.

"Crossover Refunding Indebtedness" means Indebtedness issued for the purpose of refunding other Indebtedness if the proceeds of such refunding Indebtedness are irrevocably deposited in escrow to secure the payment on the applicable redemption date or maturity date of the refunded Indebtedness, and the earnings on such escrow deposit (i) are required to be applied to pay interest on such Refunding Indebtedness until the Cross-over Date and (ii) shall not be used directly or indirectly to pay interest on the Refunded Indebtedness.

"Debt Service Component of Contracted Services" means that part of the payment for Contracted Services for which a Member of the Obligated Group is obligated to pay that the chief financial officer of such Member of the Obligated Group shall have determined in writing in an Officer's Certificate at the time such Member of the Obligated Group commits to receive such Contracted Services to be for the purpose of paying a fixed charge or the principal of and interest on obligations, directly or indirectly associated with rendering the Contracted Services, of the person providing the Contracted Services.

"Debt Service Reserve Fund" means the Hampton Roads Sanitation District, Virginia Wastewater Refunding Revenue Bonds, Series 2003 Debt Service Reserve Fund created and so designated by the Trust Agreement.

"Debt Service Reserve Fund Requirement" means (i) at the Closing, zero (0) and (ii) during any Reserve Funding Period or at such other time as the District may elect to fund the Debt Service Reserve Fund, the least of (A) one hundred percent (100%) of Maximum Annual Debt Service on the Bonds; (B) one hundred twenty-five percent (125%) of Average Annual Debt Service and (C) ten percent (10%) of the proceeds of the Series 2003 Bonds determined on the basis of the initial offering prices to the public; provided, however, that if the Series 2003 Bonds have original issue discount or premium that exceeds two percent (2%) of the stated redemption price at maturity, the initial offering prices to the public will be used in lieu of the stated principal amount for purposes of the ten percent (10%) limitation.

"Defaulted Interest" means any interest on any Series 2003 Bond which is payable, but is not punctually paid or duly provided for, on any Interest Payment Date.

"Defeasance Obligations" means (i) noncallable Government Obligations, (ii) evidences of ownership of a proportionate interest in specified Government Obligations, which Government Obligations are held by a bank or

trust company organized and existing under the laws of the United States of America or any state thereof in the capacity of custodian, (iii) obligations issued pursuant to Section 21B(d)(3) of the Federal Home Loan Bank Act, as amended by Section 511(a) of the Financial Institutions Reform, Recovery and Enforcement Act of 1989, and commonly known as "interest strips" of the Resolution Funding Corporation, (iv) Defeased Municipal Obligations and (v) evidences of ownership of a proportionate interest in specified Defeased Municipal Obligations, which Defeased Municipal Obligations are held by a bank or trust company organized and existing under the laws of the United States of America or any state thereof in the capacity as custodian.

"Defeased Municipal Obligations" means obligations of state or local government municipal bond issuers which are rated the highest rating by Moody's and Standard & Poor's, respectively, provision for the payment of the principal of and interest on which shall have been made by deposit with a trustee or escrow agent of (i) Government Obligations or (ii) evidences of ownership of a proportionate interest in specified Government Obligations, which Government Obligations are held by a bank or trust company organized and existing under the laws of the United States of America or any state thereof in the capacity as custodian, the maturing principal of and interest on such Government Obligations or evidences of ownership, when due and payable, shall provide sufficient money to pay the principal of, redemption premium, if any, and interest on such obligations of state or local government municipal bond issuers.

"Defeased Obligations" means Obligations issued under a Supplement that have been discharged, or provision for the discharge of which has been made, pursuant to its terms.

"Derivative Indebtedness" means Indebtedness or any portion thereof with respect to which a Member of the Obligated Group shall have entered into a Derivative Agreement.

"Derivative Agreement" means, without limitation, (i) any contract known as or referred to or which performs the function of an interest rate swap agreement, forward payment conversion agreement or futures contract; (ii) any contract providing for payments based on levels of, or changes or differences in, interest rates or other indices; (iii) any contract to exchange cash flows or payments or series of payments; (iv) any type of contract called, or designed to perform the function of, interest rate floors or caps, options, puts or calls, to hedge or minimize any type of financial risk, including, without limitation, payment, rate or other financial risk; and (v) any other type of contract or arrangement that a Member of the Obligated Group determines is to be used, or is intended to be used, to manage or reduce the cost of Indebtedness, to convert any element of Indebtedness from one form to another or to protect against any type of financial risk or uncertainty.

"Derivative Agreement Counterparty" means, with respect to a Derivative Agreement, the Person that is identified in such agreement as the counterparty to, or contracting party with, a Member of the Obligated Group.

"Designated Unit" means (i) the Wastewater System and (ii) any Operating Unit which a Member of the Obligated Group that is a Governmental Entity causes to become a Designated Unit in accordance with the provisions of the Master Indenture.

"District" means the Hampton Roads Sanitation District, a political subdivision of the Commonwealth of Virginia.

"District Representative" means each of the persons at the time designated to act on behalf of the District in a written certificate furnished to the Bond Trustee, which certificate shall contain the specimen signature(s) of such person(s) and shall be signed on behalf of the Commission by its Chairman or Vice Chairman.

"Enabling Act" means Chapter 66 of the Acts of Assembly of Virginia of 1960, as amended.

"Financial Statements" means the unaudited combining financial statements of the Obligated Group derived from the Audited Financial Statements included, in an additional information section, in the Audited Financial Statements and covering the same twelve-month period as the Audited Financial Statements to which the accounts of any Member of the Obligated Group other than the District have been added; provided, however, that for purposes of adding the accounts of a Member of the Obligated Group other than the District, the balances of such

accounts shall be extracted from audited financial statements of such Member of the Obligated Group and its affiliates, if any.

"Fiscal Year" means the fiscal year of each Member of the Obligated Group, which shall be the period commencing on the first day of July of any year and ending on the last day of June of the following year unless the Master Trustee is notified in writing by the Obligated Group Representative of a change in such period, in which case the Fiscal Year shall be the period set forth in such notice.

"Governing Body" means, when used with respect to the District, the Commission and, when used with respect to any other Member of the Obligated Group, its board of directors, board of trustees, or other board or group of individuals in which the powers of such Member of the Obligated Group are vested.

"Government Obligations" means direct obligations of, or obligations the timely payment of the principal of and interest on which are fully and unconditionally guaranteed by, the United States of America.

"Governmental Entity" means the Commonwealth of Virginia or any contiguous state or the District of Columbia or any municipal corporation or political subdivision formed under the laws thereof or any constituted authority or agency or instrumentality of any of the foregoing.

"Governmental Member of the Obligated Group" means a Member of the Obligated Group which is a Governmental Entity.

"Gross Receipts" means all revenues, income, receipts and money (other than proceeds of borrowing) received in any period by or on behalf of any Member of the Obligated Group, including, but without limiting the generality of the foregoing, (a) revenues derived from its operations, (b) gifts, grants, bequests, donations and contributions and the income therefrom, exclusive of any gifts, grants, bequests, donations and contributions to the extent specifically restricted by the donor to a particular purpose inconsistent with their use for the payment of Obligations, (c) proceeds derived from: (i) insurance, except to the extent otherwise required by the Master Indenture, (ii) accounts, (iii) securities and other investments, (iv) inventory and other tangible and intangible property and (v) contract rights and other rights and assets now or hereafter owned, held, or possessed by any Member of the Obligated Group, and (d) rentals received from the leasing of real or tangible personal property.

"Guaranty" means any obligation of any Member of the Obligated Group guaranteeing in any manner, directly or indirectly, any obligation of any Person that is not a Member of the Obligated Group which obligation of such other Person would, if such obligation were the obligation of a Member of the Obligated Group, constitute Indebtedness under the Master Indenture. For the purposes of the Master Indenture, the aggregate annual principal and interest payments on any Indebtedness in respect of which any Member of the Obligated Group shall have executed and delivered its Guaranty shall, so long as no payments are required to be made thereunder and so long as such Guaranty constitutes a contingent liability under generally accepted accounting principles, be deemed to be equal to twenty percent (20%), provided that if there shall have occurred a payment by any Member of the Obligated Group on such Guaranty, then, during the period commencing on the date of such payment and ending on the day which is 180 days after such other Person resumes making all payments on such guaranteed obligation, (i) with respect to a historical computation, 100% of the amount actually paid by a Member of the Obligated Group for principal and interest on such guaranteed indebtedness during the period for which the computation is being made shall be taken into account and (ii) with respect to a computation of projected debt service coverage, 100% of the amount payable for principal and interest on such guaranteed indebtedness during the period for which the computation is being made shall be taken into account.

"Holder" means, with respect to the Master Indenture, an owner of any Obligation issued in other than bearer form and, with respect to the Trust Agreement, a person in whose name a Series 2003 Bond is registered in the registration books maintained by the Bond Registrar.

"Income Available for Debt Service" means, with respect to the Obligated Group, as to any period of 12 consecutive calendar months, its excess of revenues over expenses before depreciation, amortization and interest expense on Long-Term Indebtedness, as determined in accordance with generally accepted accounting principles

consistently applied; provided, however, that (1) no determination thereof shall take into account any gain or loss resulting from either the extinguishment of Indebtedness or the sale, exchange or other disposition of capital assets not made in the ordinary course of business, (2) revenues shall include all wastewater facility charges and (3) revenues shall not include income from the investment of Qualified Escrow Funds to the extent that such income is applied to the payment of principal or interest on Long-Term Indebtedness which is excluded from the determination of Long-Term Debt Service Requirement or Related Bonds secured by such Long-Term Indebtedness.

"Indebtedness" means (i) all indebtedness of Members of the Obligated Group for borrowed money, (ii) all installment sales, conditional sales and capital lease obligations incurred or assumed by any Member of the Obligated Group, (iii) all Guaranties (other than any Guaranty by any Member of the Obligated Group of Indebtedness of any other Member of the Obligated Group), whether constituting Long-Term Indebtedness or Short-Term Indebtedness and (iv) the Debt Service Component of Contracted Services. Indebtedness shall not include obligations of any Member of the Obligated Group to another Member of the Obligated Group.

"Insurance Consultant" means a firm or Person selected by the District which is not, and no member, stockholder, director, trustee, officer or employee of which is, an officer, director, trustee or employee of any Member of the Obligated Group, which is qualified to survey risks and to recommend insurance coverage for wastewater treatment systems and organizations engaged in such operations and which is selected by the District.

"Interest Payment Date" means April 1, 2004 and each April 1 and October 1 thereafter, to and including October 1, 2015.

"Interest Requirements" for any Bond Year means the amount that is required to pay interest on all Outstanding Series 2003 Bonds on April 1 in such Bond Year and on October 1 of the following Bond Year.

"Investment Obligations" means any and all investment obligations authorized by (i) the Investment of Public Funds Act, being Section 2.2-4500 et seq., Code of Virginia, 1950, as amended, (ii) the Government Non-Arbitrage Investment Act, being Section 2.2-4700 et seq., Code of Virginia, 1950, as amended, and (iii) successor statutes as the same shall be from time to time amended.

"Lien" means any mortgage, deed of trust or pledge of, security interest in or encumbrance on any Property of any Member of the Obligated Group which secures any indebtedness or any other obligation of any Member of the Obligated Group or which secures any obligation of any Person, other than an obligation to any Member of the Obligated Group.

"Liquidity Ratio" means the ratio determined by dividing (i) the sum of all cash, cash equivalents and marketable securities that do not constitute Restricted Funds held by each Member of the Obligated Group for its various purposes but not including cash, cash equivalents or securities which constitute proceeds of Indebtedness issued to finance capital improvements or funds held in the Bond Fund (or any similar sinking fund held by a trustee for the payment of Indebtedness) by (ii) Maximum Annual Debt Service. For the purposes of the preceding sentence, "Restricted Funds" means funds or other assets of a Member of the Obligated Group the use of which is restricted or limited in such a way that such funds or other assets are not available for general purposes of such Member of the Obligated Group, but shall not include funds or assets designated, restricted or limited by a Member of the Obligated Group for specific purposes where such designation, restriction or limitation may be changed at the discretion of such Member.

"Long-Term Debt Service Coverage Ratio" means for any period of time the ratio determined by dividing the Income Available for Debt Service by Maximum Annual Debt Service;

"Long-Term Debt Service Requirement" means, for any period of twelve (12) consecutive calendar months for which such determination is made, the aggregate of the payments to be made in respect of principal and interest (whether or not separately stated) on Outstanding Long-Term Indebtedness of the Obligated Group during such period, also taking into account:

(i) with respect to Balloon Long-Term Indebtedness which is not amortized by the terms thereof (a) the amount of principal which would be payable in such period if such principal were amortized from the date of incurrence thereof over a period of thirty (30) years on a level debt service basis at an interest rate equal to the current market rate for a 30-year obligation set forth in an opinion of a banking institution or an investment banking institution knowledgeable in wastewater treatment system finance delivered to the Master Trustee as the interest rate at which the Obligated Group could reasonably expect to borrow the same by issuing an Obligation with the same term as assumed above; provided, however, that if the date of calculation is within twelve (12) calendar months of the actual maturity of such Indebtedness, the full amount of principal payable at maturity shall be included in such calculation or (b) principal payments or deposits with respect to Indebtedness secured by an irrevocable letter of credit issued by, or an irrevocable line of credit with, a bank having a combined capital and surplus of at least seventy-five million dollars (\$75,000,000), or insured by an insurance policy issued by any insurance company rated at least "A" by Alfred M. Best Company or its successors in Best's Insurance Reports or its successor publication, nominally due in the last Fiscal Year in which such Indebtedness matures may, at the option of the Member of the Obligated Group which issued such Indebtedness, be treated as if such principal payments or deposits were due as specified in any credit agreement issued in connection with such letter of credit, line of credit or insurance policy or pursuant to the repayment provisions of such letter of credit, line of credit or insurance policy, and interest on such Indebtedness after such Fiscal Year shall be assumed to be payable pursuant to the terms of such credit agreement or repayment provisions;

(ii) with respect to Long-Term Indebtedness which is Variable Rate Indebtedness, the interest on such Indebtedness shall be calculated at the rate which is equal to the average of the actual interest rates which were in effect (weighted according to the length of the period during which each such interest rate was in effect) for the most recent twelve-month period immediately preceding the date of calculation for which such information is available (or shorter period if such information is not available for a twelve-month period), except that with respect to new Variable Rate Indebtedness the interest rate for such Indebtedness for the initial interest rate period shall be the initial rate at which such Indebtedness is issued and thereafter shall be calculated as set forth above;

(iii) with respect to any Credit Facility, to the extent that such Credit Facility has not been used or drawn upon, the principal and interest relating to such Credit Facility shall not be included in the Long-Term Debt Service Requirement; and

(iv) with respect to Derivative Indebtedness, (i) for any historical computation, the interest on such Indebtedness shall be calculated by adding (A) the amount of interest payable by a Member of the Obligated Group on such Derivative Indebtedness pursuant to its terms and (B) the amount of regularly scheduled payments made by a Member of the Obligated Group pursuant to the Derivative Agreement and subtracting (C) the amount of regularly scheduled payments made by the Derivative Agreement Counterparty pursuant to the Derivative Agreement; (ii) for any historical pro forma or forecasted computation, if the Derivative Agreement Counterparty has a long-term credit rating of at least "A" (without regard to any rating refinement or gradation by numerical modifier or otherwise) assigned to it by at least one nationally recognized rating agency then rating the Obligations or the Related Bonds and does not have a long-term rating of less than "A" (without regard to any rating refinement or gradation by numerical modifier or otherwise) from any other nationally recognized rating agency then rating the Obligations or the Related Bonds and has not defaulted on its payment obligations thereunder as of the date of computation, the interest on such Derivative Indebtedness shall be calculated by adding (A) the amount of interest payable by a Member of the Obligated Group on such Derivative Indebtedness pursuant to its terms and (B) the amount of regularly scheduled payments payable by such Member of the Obligated Group pursuant to the Derivative Agreement and subtracting (C) the amount of regularly scheduled payments payable by the Derivative Agreement Counterparty pursuant to the Derivative Agreement; and (iii) in all other instances, the amount of interest payable by a Member of the Obligated Group on such Derivative Indebtedness shall be calculated as if such Derivative Agreement had not been executed; provided, however, that, for any historical pro forma or forecasted computation, any floating payment rate specified in the Derivative Agreement shall be calculated (a) at the rate which is equal to the weighted average of the floating payment rates (1) which were in effect during the five-year period ending as close as possible to the date of computation or (2) if such Derivative Agreement was entered into less than five

years prior to the date of computation or such Derivative Indebtedness has not yet been incurred, which would have been in effect during such five-year period if such Derivative Agreement had been in effect for such period and the rate can be determined based on the variables provided in the Derivative Agreement and (b) in all other instances, (1) at the rate which is equal to the weighted average of the floating payment rates which were in effect from the date the Derivative Agreement became effective to as close as possible to the date of computation, provided that such period is not less than one year, or (2) if the rate cannot be determined under clause (b)(1), at the rate set forth in an opinion of a commercial or investment banking institution knowledgeable in municipal finance delivered to the Master Trustee as the floating payment rate which such institution reasonably expects to be in effect during the projected computation period; and provided, further, that, in lieu of relying on an opinion pursuant to clause (b)(2) of the preceding proviso, the Obligated Group may elect, as evidenced by an Officer's Certificate of an Obligated Group Representative, to determine the amount of interest payable by a Member of the Obligated Group on such Derivative Indebtedness as if such Derivative Agreement had not been executed;

provided, however, that interest shall be excluded from the determination of Long-Term Debt Service Requirement to the extent the same is provided from the proceeds of the Long-Term Indebtedness and provided further, however, notwithstanding the foregoing, the aggregate of the payments to be made with respect to principal and interest on Outstanding Long-Term Indebtedness shall not include principal and interest payable from Qualified Escrow Funds.

"Long-Term Indebtedness" means all obligations having a maturity of a term longer than one year for borrowed money incurred or assumed by any Member of the Obligated Group, including (a) Guaranties, except Guaranties of obligations of any Member of the Obligated Group by another Member of the Obligated Group, (b) Short-Term Indebtedness if a commitment by an institutional lender exists to provide financing to retire such Short-Term Indebtedness and such commitment provides for the repayment of principal on terms which would, if such commitment were implemented, constitute Long-Term Indebtedness, and (c) the current portion of Long-Term Indebtedness, for any of the following:

- (i) money borrowed for an original term, or renewable at the option of the borrower for a period from the date originally incurred, longer than one year;

- (ii) leases which are required to be capitalized in accordance with generally accepted accounting principles having an original term, or renewable at the option of the lessee for a period from the date originally incurred, longer than one year;

- (iii) installment sale or conditional sale contracts having an original term in excess of one year; and

- (iv) the Debt Service Component of Contracted Services in connection with Contracted Services rendered or provided pursuant to a contract having an original term of more than one year.

"Master Indenture" means the Master Trust Indenture, dated as of December 1, 1993, as amended, by and between the District and The Bank of New York, as Master Trustee, including any further amendments or supplements thereto.

"Master Trustee" means The Bank of New York, New York, New York, and its successors in the trusts created under the Master Indenture.

"Maximum Annual Debt Service" means the highest Long-Term Debt Service Requirement for any succeeding Fiscal Year.

"Maximum Annual Debt Service on the Bonds" means, at any given time of determination, the maximum Principal and Interest Requirements for the Series 2003 Bonds for the then current or any succeeding Bond Year.

"Member of the Obligated Group" means the District and any other Person becoming a Member of the Obligated Group pursuant to the Master Indenture.

"Moody's" means Moody's Investors Service, Inc., a corporation organized and existing under the laws of the State of Delaware, its successors and their assigns, and, if such corporation shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, "Moody's" shall be deemed to refer to any other nationally recognized securities rating agency designated by the District by notice to the Bond Trustee.

"Net Book Value" when used in connection with Property, Plant and Equipment or other Property of any Person, means the value of such property, net of accumulated depreciation, as it is carried on the books of such Person in conformity with generally accepted accounting principles, and when used in connection with Property, Plant and Equipment or other Property of the Obligated Group, means the aggregate of the values so determined with respect to such Property, Plant and Equipment or other Property of the Obligated Group determined in such a manner that no portion of such value of Property, Plant and Equipment or other Property is included more than once.

"Net Revenues" means all revenues derived by a Governmental Member of the Obligated Group from its Designated Units except such part thereof as may be required to pay the cost of maintaining, repairing and operating such Designated Units.

"Obligated Group" means, collectively, the Members of the Obligated Group.

"Obligated Group Representative" means each of the Person(s) at the time designated to act on behalf of the Obligated Group in a written certificate furnished to the Master Trustee, which certificate shall contain the specimen signature(s) of such Person(s) and shall be signed on behalf of the Obligated Group by the Chairman of the Commission or his designee.

Each certificate of an Obligated Group Representative presented pursuant to the Master Indenture shall state that it is being delivered pursuant to (and shall identify the section or subsection of), and shall incorporate by reference and use in all appropriate instances all terms defined in the Master Indenture. Each certificate of an Obligated Group Representative shall state (i) whether the terms thereof are in compliance with the requirements of the section or subsection pursuant to which such certificate is delivered or shall state in reasonable detail the nature of any non-compliance and the steps being taken to remedy such non-compliance and (ii) that it is being delivered together with any opinions, schedules, statements or other documents required in connection therewith.

"Obligation" means the evidence of particular Indebtedness issued under the provisions of the Master Indenture.

"Obligation No. 2" means the obligation so designated and issued under the Master Indenture and delivered to the Bond Trustee as security for the payment of the Series 2003 Bonds.

"Officer's Certificate" means a certificate signed by the chairman of the Governing Body, or the general manager, or the president or chief executive officer, or the chief financial officer, or the chairman of the finance committee of the Governing Body of such Member of the Obligated Group as the context requires.

Each Officer's Certificate presented pursuant to the Master Indenture shall state that it is being delivered pursuant to (and shall identify the section or subsection of), and shall incorporate by reference and use in all appropriate instances all terms defined in, the Master Indenture. Each Officer's Certificate shall state (i) that the terms thereof are in compliance with the requirements of the section or subsection pursuant to which such Officer's Certificate is delivered or shall state in reasonable detail the nature of any non-compliance and the steps being taken to remedy such non-compliance and (ii) that it is being delivered together with any opinions, schedules, statements or other documents required in connection therewith.

"Operating Assets" means any or all land, leasehold interests, buildings, machinery, equipment, hardware, and inventory owned or operated by each Member of the Obligated Group and used in its respective trade or business, whether separately or together with other such assets, but not including cash, investment securities and other Property held for investment purposes.

"Operating Unit" means any enterprise owned and operated by a Governmental Entity the activities of which are recorded in financial statements which (i) relate only to such enterprise, (ii) have been prepared in accordance with generally accepted accounting principles, and (iii) have been audited and reported upon by independent certified public accountants; provided, however, that such financial statements may relate to more than one enterprise if all of the enterprises covered by such financial statements are Designated Units.

"Opinion of Bond Counsel" means an opinion in writing signed by an attorney or firm of attorneys acceptable to the Master Trustee and experienced in the field of municipal bonds whose opinions are generally accepted by purchasers of municipal bonds.

"Opinion of Counsel" means an opinion in writing signed by an attorney or firm of attorneys, acceptable to the Master Trustee or Bond Trustee, as applicable, who may be counsel for the District or any Member of the Obligated Group or other counsel acceptable to the Master Trustee or Bond Trustee, as applicable.

"Outstanding" when used with reference to Series 2003 Bonds means, as of a particular date, all Series 2003 Bonds theretofore issued under the Trust Agreement, except:

(1) Series 2003 Bonds theretofore cancelled by the Bond Registrar or delivered to the Bond Registrar for cancellation;

(2) Series 2003 Bonds for the payment of which money, Defeasance Obligations, or a combination of both, sufficient to pay, on the date when such Series 2003 Bonds are to be paid, the principal amount of, and the interest accruing to such date on, the Series 2003 Bonds to be paid, has been deposited with the Bond Trustee or the Bond Registrar in trust for the Holders of such Bonds; Defeasance Obligations shall be deemed to be sufficient to pay Series 2003 Bonds on a specified date if the principal of and the interest on such Defeasance Obligations, when due, will be sufficient to pay on such date the principal of, and the interest accruing on, such Bonds to such date;

(3) Series 2003 Bonds in exchange for or in lieu of which other Series 2003 Bonds have been issued; and

(4) Series 2003 Bonds deemed to have been paid in accordance with the provisions of the Trust Agreement;

provided, however, Series 2003 Bonds owned or held by or for the account of the District or any affiliate or any subsidiary or controlled affiliate of the District shall not be deemed Outstanding Bonds for the purpose of any consent or other action or any calculation of Outstanding Bonds provided for in the Articles in the Trust Agreement entitled "Events of Default and Remedies", "Supplemental Trust Agreements" and "Defeasance" and neither the District nor any affiliate, subsidiary or controlled affiliate of the District as registered owners of such Bonds shall be entitled to consent or take any other action provided for in the above-mentioned provisions of the Trust Agreement.

"Outstanding" when used with reference to Indebtedness means, as of any date of determination, all Indebtedness theretofore issued or incurred and not paid and discharged other than (i) Obligations cancelled by the Master Trustee or delivered to the Master Trustee for cancellation, (ii) Indebtedness deemed paid and no longer Outstanding under the documents pursuant to which such Indebtedness was incurred, (iii) Defeased Obligations and (iv) Obligations in lieu of which other Obligations have been authenticated and delivered or have been paid pursuant to the provisions of the Supplement regarding mutilated, destroyed, lost or stolen Obligations unless proof satisfactory to the Master Trustee has been received that any such Obligation is held by a bona fide purchaser; provided, however, that for purposes of determining whether the Holders of the requisite principal amount of Obligations have concurred in any demands, direction, request, notice, consent, waiver or other action under the Master Indenture, Obligations or Related Bonds that are owned by any Member of the Obligated Group or by any person directly or indirectly controlling or controlled by or under direct or indirect common control with such Member shall be deemed not to be Outstanding, provided further, however, that for the purposes of determining whether the Master Trustee shall be protected in relying on any such direction, consent, or waiver, only such

Obligations or Related Bonds which the Trustee has actual notice or knowledge are so owned shall be deemed to be not Outstanding.

"Permitted Liens" shall be as described under the caption "SUMMARY OF THE MASTER INDENTURE – Limitation on Creation of Liens" herein.

"Person" includes an individual, association, unincorporated organization, corporation, partnership, joint venture, business trust or any other nongovernmental entity or any Governmental Entity.

"Principal and Interest Requirements" means, for any Bond Year, the sum of the Principal Requirements and Interest Requirements for such Bond Year.

"Principal Requirements" means, for any Bond Year, the amount required to pay the principal of all Outstanding Series 2003 Bonds coming due on October 1 of the following Bond Year.

"Property" means any and all rights, title and interests in and to any and all property whether real or personal, tangible or intangible and wherever situated.

"Property, Plant and Equipment" means all Property of the Members of the Obligated Group which is property, plant and equipment under generally accepted accounting principles.

"Qualified Escrow Funds" means amounts deposited in a segregated escrow fund or other similar fund or account in connection with the issuance of Long-Term Indebtedness or Related Bonds secured by such Long-Term Indebtedness which fund or account is required by the documents establishing such fund to be applied toward the Obligated Group's payment obligations with respect to principal or interest on (a) the Long-Term Indebtedness or Related Bonds secured thereby which are issued under the documents establishing such fund or (b) Long-Term Indebtedness or Related Bonds secured thereby which are issued prior to the establishment of such fund.

"Qualified Reserve Fund Substitute" means (i) an irrevocable letter of credit, naming the Bond Trustee as beneficiary, issued by any domestic or foreign bank, or any branch or agency thereof, whose long-term debt obligations are rated in one of the two highest rating categories by Moody's, if rated by Moody's, and Standard & Poor's, if rated by Standard & Poor's, respectively, or (ii) a policy of reserve fund insurance naming the Bond Trustee as beneficiary, issued by an insurance company whose claims paying ability is rated in one of the two highest rating categories by Moody's, if rated by Moody's, and Standard & Poor's, if rated by Standard & Poor's, respectively, in either case (A) in an amount not less than the Debt Service Reserve Fund Requirement, (B) the terms of which allow the Bond Trustee to make the draws provided for in the section of the Trust Agreement entitled "Application of Money in Debt Service Reserve Fund; Qualified Reserve Fund Substitute" and (C) provides that the issuer of which shall not have been given a lien on any portion of the property of the District unless such lien also secures the Series 2003 Bonds on a parity basis.

"Related Bond Indenture" means any indenture, bond resolution or other comparable instrument pursuant to which a series of Related Bonds is issued.

"Related Bond Issuer" means the issuer of any issue of Related Bonds.

"Related Bonds" means:

(i) the revenue bonds or other obligations issued by the District or any other Member of the Obligated Group that is a Governmental Entity pursuant to a single Related Bond Indenture, the proceeds of which are made available to the District or such other Member of the Obligated Group in consideration of the execution, authentication and delivery of an Obligation to secure such revenue bonds or other obligations; and

(ii) the revenue bonds or other obligations issued pursuant to a single Related Bond Indenture by a Governmental Entity the proceeds of which are made available to (A) a Member of the Obligated Group

in consideration of the execution, authentication and delivery of an Obligation to or for the order of such Governmental Entity, or (B) any Person other than a Member of the Obligated Group in consideration of the issuance to such Governmental Entity (1) by such Person of any indebtedness or other obligation of such Person, and (2) by a Member of the Obligated Group of a Guaranty in respect of such indebtedness or other obligation, which Guaranty is represented by an Obligation.

“Related Bond Trustee” means the trustee and its successors in the trusts created under any Related Bond Indenture.

“Reserve Funding Period” means the period beginning at such time, if any, when the District is required to fund the Debt Service Reserve Fund in accordance with the provisions of the Trust Agreement and ending at such time, if any, when the Liquidity Ratio for each of the past two Fiscal Years, as computed based on the Financial Statements as of the end of each Fiscal Year, is equal to or greater than 1.35 and the Long-Term Debt Service Coverage Ratio for each of the past two Fiscal Years, as calculated pursuant to the provisions of the Master Indenture, is equal to or greater than 1.35.

“Securities Depository” means The Depository Trust Company, New York, New York or other recognized securities depository selected by the District, which maintains a book-entry system in respect of the Series 2003 Bonds, and shall include any substitute for or successor to the securities depository initially acting as Securities Depository.

“Securities Depository Nominee” means, as to any Securities Depository, such Securities Depository or the nominee of such Securities Depository in whose name there shall be registered on the registration books maintained by the Bond Registrar the bond certificates to be delivered to and immobilized at such Securities Depository during the continuation with such Securities Depository of participation in its book-entry system.

“Series 2003 Bonds” means the Hampton Roads Sanitation District, Virginia Wastewater Refunding Revenue Bonds, Series 2003, issued under the Trust Agreement.

“Short-Term Indebtedness” means all obligations for borrowed money, other than any Guaranty of an obligation of a Person which is a Member of the Obligated Group and the current portion of Long-Term Indebtedness, incurred or assumed by one or more Members of the Obligated Group, for any of the following:

- (i) money borrowed for an original term, or renewable at the option of the borrower for a period from the date originally incurred, of one year or less;

- (ii) leases which are capitalized in accordance with generally accepted accounting principles having an original term, or renewable at the option of the lessee for a period from the date originally incurred, of one year or less; and

- (iii) installment purchase or conditional sale contracts having an original term of one year or less.

“Special Record Date” for the payment of any Defaulted Interest on Series 2003 Bonds means a date fixed by the Bond Trustee pursuant to the Trust Agreement.

“Standard & Poor’s” means Standard & Poor’s Ratings Services, a division of The McGraw-Hill Companies, Inc., a corporation organized and existing under the laws of the State of New York, its successors and their assigns, and, if such corporation shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, “Standard & Poor’s” shall be deemed to refer to any other nationally recognized securities rating agency designated by the District by notice to the Bond Trustee.

“Subordinated Indebtedness” means Indebtedness of a Member of the Obligated Group the terms of which shall provide that it shall be subordinate and junior in right of payment to the prior payment in full of the Obligations to the extent and in the manner set forth below:

In the event (a) of any insolvency or bankruptcy proceedings, and any receivership, liquidation, reorganization, arrangement or other similar proceedings in connection therewith, relative to such Member of the Obligated Group or to its property, or in the event of any proceedings for voluntary liquidation, dissolution or other winding-up of such Member of the Obligated Group whether or not involving insolvency or bankruptcy, (b) any Subordinated Indebtedness is declared or otherwise becomes due and payable before its expressed maturity because of the occurrence of an event of default occurring under the documents pursuant to which such Subordinated Indebtedness is issued; and such declaration has not been rescinded and annulled, or (c) any Event of Default under the Master Indenture shall occur and be continuing with respect to Obligations and (1) written notice of such default shall have been given to such Member of the Obligated Group and (2) judicial proceedings shall be commenced in respect of such Event of Default within 180 days in the case of a default in payment of principal or interest on Obligations and within 90 days in the case of any other default after the giving of such notice, then the Holders of Obligations shall be entitled to receive payment in full of all principal, premium and interest on all Obligations before the Holders of the Subordinated Indebtedness are entitled to receive any payment on account of principal or interest upon the Subordinated Indebtedness, and to that end the Holders of Obligations shall be entitled to receive for application in payment thereof any payment or distribution of any kind or character, whether in cash or property or securities, which may be payable or deliverable in any such proceedings in respect of the Subordinated Indebtedness after giving effect to any concurrent payment or distribution in respect of such Obligations.

"Supplement" means an indenture supplemental to, and authorized and executed pursuant to the terms of, the Master Indenture.

"Supplement No. 2" means Supplemental Indenture for Obligation No. 2, dated as of December 1, 2003, by and between the District and the Master Trustee.

"Tax Certificate" means the Tax Certificate and Agreement, dated as of the Closing, executed and delivered by the District in connection with the issuance of the Series 2003 Bonds.

"Total Operating Revenues" means, with respect to the Obligated Group, as to any period of time, total operating revenues as determined in accordance with generally accepted accounting principles consistently applied.

"Transfer" means any act or occurrence the result of which is to dispossess any Person of any asset or interest therein, including specifically, but without limitation, the forgiveness of any debt or the lease of any such asset.

"Trust Agreement" means the Trust Agreement securing the Series 2003 Bonds, dated as of December 1, 2003, by and between the District and The Bank of New York, New York, New York, as trustee, including any trust agreement amendatory thereof or supplemental thereto.

"Variable Rate Indebtedness" means any portion of Indebtedness the interest rate on which is not established at the time of incurrence at a fixed or constant rate until maturity.

"Wastewater System" means the wastewater treatment enterprise of the District the activities of which are recorded in financial statements which (i) relate only to such enterprise, (ii) have been prepared in accordance with generally accepted accounting principles, and (iii) have been audited and reported upon by independent certified public accountants.

SUMMARY OF THE MASTER INDENTURE

Application of Definitions and Covenants to Designated Units

Unless otherwise expressly so provided in the Master Indenture, with respect to any Governmental Member of the Obligated Group, any determination required to be made thereunder as to the existence, character or amount of any asset, liability or item of income or expense for the purpose of any test, limitations, ratios or defined terms

thereunder shall be based upon or determined from the Financial Statements of the Designated Units and not from the Financial Statements of the Governmental Member of the Obligated Group taken as a whole.

Unless otherwise expressly so provided in the Master Indenture, with respect to any Governmental Member of the Obligated Group, any actions, payments, covenants, obligations or other things to be done or performed shall be based upon the use of the Property of the Designated Units and not the Property of the Governmental Member of the Obligated Group generally. (Sec. 1.02)

Indebtedness, Authorization, Issuance and Terms of Obligations

There is no limit on the principal amount or number of Obligations that may be issued under the Master Indenture or the principal amount of Indebtedness that may be created under other documents except as limited by the provisions of the Master Indenture or of any Supplement, but no Obligations may be issued unless the provisions of the Master Indenture are followed. Each Member of the Obligated Group is jointly and severally liable for each and every Obligation. (Sec. 2.01)

Any Member of the Obligated Group and the Master Trustee may from time to time enter into a Supplement in order to create Indebtedness under the Master Indenture. Such Supplement shall, with respect to an Obligation evidencing Indebtedness created thereby, set forth the date thereof, and the date or dates on which the principal of, redemption premium, if any, and interest on such Obligation shall be payable, and the form of such Obligation and such other terms and provisions as shall conform with the provisions and conditions of the Master Indenture. (Sec. 2.04)

Particular Covenants

Security; Restrictions on Encumbering Net Revenues and Gross Receipts; Payment of Principal and Interest

(a) Any Obligation issued pursuant to the Master Indenture shall be a special obligation payable solely from (i) Net Revenues in the case of Governmental Members of the Obligated Group and (ii) Gross Receipts in the case of any other Member of the Obligated Group.

To secure prompt payment of the principal of, redemption premium, if any, and the interest on the Obligations, and the performance by each Member of the Obligated Group of its other obligations under the Master Indenture, (i) each Governmental Member of the Obligated Group pledges to the Master Trustee its Net Revenues and (ii) each Member of the Obligated Group that is not a Governmental Entity grants to the Master Trustee a security interest in its Gross Receipts.

(b) Each Member of the Obligated Group covenants that it will not pledge or grant a security interest in (except as provided in (a) above and as may be otherwise provided in the Master Indenture) any of its Property.

(c) Each Obligation shall be a joint and several special obligation of each Member of the Obligated Group payable from (i) Net Revenues in the case of Governmental Members of the Obligated Group and (ii) Gross Receipts in the case of Members of the Obligated Group that are not Governmental Entities. Each Member of the Obligated Group covenants to promptly pay or cause to be paid the principal of, premium, if any, and interest on each Obligation issued under the Master Indenture at the place, on the dates and in the manner provided in the Master Indenture and in said Obligation according to the terms thereof whether at maturity, upon proceedings for redemption, by acceleration or otherwise.

(d) Each Member of the Obligated Group covenants that, if an Event of Default under the Master Indenture shall have occurred and be continuing, it will, upon request of the Master Trustee, deliver or direct to be delivered to the Master Trustee all Net Revenues in the case of Governmental Members of the Obligated Group and all Gross Receipts in the case of Members of the Obligated Group that are not Governmental Entities until such Event of Default has been cured. (Sec. 3.01)

Covenants as to Existence, Maintenance of Properties, Etc.

Each Member of the Obligated Group covenants:

(a) Except as otherwise expressly provided in the Master Indenture, to preserve its corporate or other legal existence and all its rights and licenses to the extent necessary or desirable in the operation of its business and affairs and be qualified to do business in each jurisdiction where its ownership of Property or the conduct of its business requires such qualifications; provided, however, that nothing contained in the Master Indenture shall be construed to obligate it to retain or preserve any of its rights or licenses, no longer used or, in the judgment of its Governing Body, useful in the conduct of its business.

(b) At all times to cause its Property to be maintained, preserved and kept in good repair, working order and condition and all needed and proper repairs, renewals and replacements thereof to be made; provided, however, that nothing contained in the Master Indenture shall be construed to (i) prevent it from ceasing to operate any portion of its Property, if in its judgment (evidenced, in the case of such a cessation other than in the ordinary course of business by an opinion or certificate of a Consultant) it is advisable not to operate the same, or if it intends to sell or otherwise dispose of the same and within a reasonable time endeavors to effect such sale or other disposition, or (ii) obligate it to retain, preserve, repair, renew or replace any Property, leases, rights, privileges or licenses no longer used or, in the judgment of its Governing Body, useful in the conduct of its business.

(c) To do all things reasonably necessary to conduct its affairs and carry on its business and operations in such manner as to comply with any and all applicable laws of the United States and the several states thereof and duly observe and conform to all valid orders, regulations or requirements of any governmental authority relative to the conduct of its business and the ownership of its Properties; provided, nevertheless, that nothing contained in the Master Indenture shall require it to comply with, observe and conform to any such law, order, regulation or requirement of any governmental authority so long as the validity thereof or the applicability thereof to it shall be contested in good faith.

(d) To pay promptly all lawful taxes, governmental charges and assessments at any time levied or assessed upon or against it or its Property; provided, however, that it shall have the right to contest in good faith any such taxes, charges or assessments or the collection of any such sums and pending such contest may delay or defer payment thereof.

(e) To pay promptly or otherwise satisfy and discharge all of its Indebtedness and all demands and claims against it as and when the same become due and payable, other than any thereof (exclusive of the Indebtedness created and Outstanding under the Master Indenture) whose validity, amount or collectibility is being contested in good faith.

(f) At all times to comply with all terms, covenants and provisions of any Liens at such time existing upon its Property or any part thereof or securing any of its Indebtedness.

(g) To procure and maintain all necessary licenses and permits for the operation of its wastewater treatment facilities; provided, however, that it need not comply with this covenant if and to the extent that its Governing Body shall have determined in good faith, evidenced by a resolution of the Governing Body, that such compliance is not in its best interests and that lack of such compliance would not materially impair its ability to pay its Indebtedness when due. (Sec. 3.02)

Insurance

Each Member of the Obligated Group agrees that it will maintain, or cause to be maintained, the following types of insurance (including one or more self-insurance programs considered to be adequate by the Insurance Consultant) in such amounts as, in its judgment, are adequate to protect it and its Property and operations: (i) comprehensive general public liability insurance, including automobile insurance including owned and hired automobiles (excluding collision and comprehensive coverage thereon), (ii) fire, lightning, windstorm, hail,

explosion, riot, riot attending a strike, civil commotion, damage from aircraft, smoke and uniform standard coverage and vandalism and malicious mischief endorsements and (iii) workers' compensation insurance.

The District shall employ an Insurance Consultant to review the insurance requirements of the Members of the Obligated Group from time to time (but not less frequently than biennially). If the Insurance Consultant makes recommendations for the increase of any coverage, the Obligated Group shall incense or cause to be increased such coverage in accordance with such recommendations, subject to a good faith determination of the Commission that such recommendations, in whole or in part, are in the best interests of the Obligated Group. If the Insurance Consultant makes recommendations for the decrease or elimination of any coverage, the Obligated Group may decrease or eliminate such coverage in accordance with such recommendations, subject to a good faith determination of the Commission that such recommendations, in whole or in part, are in the best interests of the Obligated Group. Notwithstanding the foregoing, each Member of the Obligated Group shall have the right, without giving rise to an Event of Default solely on such account, (i) to maintain insurance coverage below that most recently recommended by the Insurance Consultant, if the Obligated Group furnishes the Master Trustee a report of the Insurance Consultant to the effect that the insurance so provided affords the greatest amount of coverage available for the risk being insured against at rates which in the judgment of the Insurance Consultant are reasonable in connection with reasonable and appropriate risk management or (ii) to adopt alternative risk management programs which the Insurance Consultant determines to be reasonable, including, without limitation, to self-insure in whole or in part individually or in connection with other institutions, to participate in programs of captive insurance companies, to participate with other wastewater treatment systems in mutual or other cooperative insurance or other risk management programs or to participate in state or federal insurance programs; all as may be approved by the Insurance Consultant as reasonable and appropriate risk management by the Obligated Group. If any Member of the Obligated Group shall be self-insured for any coverage, the report of the Insurance Consultant mentioned above shall state whether the anticipated funding of any self-insurance fund is actuarially sound, and, if not, the required funding to produce such result, and such coverage shall be reviewed by such Consultant not less frequently than annually. If the Insurance Consultant determines that the anticipated funding of any self-insurance fund is not actuarially sound, the Obligated Group covenants that it will fund such self-insurance fund in the manner recommended by the Insurance Consultant. (Sec. 3.03)

Insurance and Condemnation Proceeds

Amounts that do not exceed twenty percent (20%) of the Net Book Value of the Property, Plant and Equipment of the Obligated Group received by any Member of the Obligated Group for casualty losses or condemnation may be used as the recipient determines, including, without limitation, the application of such moneys to the partial payment or prepayment of any Indebtedness in accordance with the terms thereof and of any pertinent Supplement. However, amounts that exceed twenty percent (20%) of the Net Book Value of the Property, Plant and Equipment of the Obligated Group received by any Member of the Obligated Group for casualty losses or condemnation may be used in such manner as the recipient may determine if the recipient notifies the Master Trustee and, within 12 months after the casualty loss or taking, delivers to the Master Trustee (i) an Officer's Certificate certifying the expected Long-Term Debt Service Coverage Ratio for each of the two periods of 12 full consecutive calendar months following the expected date of application of such funds is not less than 1.50, as shown by pro forma financial statements for each such period and a written report of a Consultant confirming such certification; or (ii) a written Consultant's report stating recommendations, including recommendations as to the use of such proceeds or awards, to cause the Long-Term Debt Service Coverage Ratio for each of such periods to be not less than 1.20, or, if in the opinion of the Consultant the attainment of such level is impracticable, at the highest practicable level. (Sec. 3.04)

Limitation on Creation of Liens

(a) Each Member of the Obligated Group agrees that it will not create or suffer to be created or permit the existence of any Lien on Property now owned or hereafter acquired by it or upon (i) Net Revenues in the case of Governmental Members of the Obligated Group or (ii) Gross Receipts in the case of Members of the Obligated Group that are not Governmental Entities other than Permitted Liens.

(b) Permitted Liens shall consist of the following:

(i) Liens arising by reason of good faith deposits with any Member of the Obligated Group in connection with leases of real estate, bids or contracts (other than contracts for the payment of money), deposits by any Member of the Obligated Group to secure public or statutory obligations, or to secure, or in lieu of, surety, stay or appeal bonds, and deposits as security for the payment of taxes or assessments or other similar charges;

(ii) Any Lien arising by reason of deposits with, or the giving of any form of security to, any governmental agency or any body created or approved by law or governmental regulation for any purpose at any time as required by law or governmental regulation as a condition to the transaction of any business or the exercise of any privilege or license, or to enable any Member of the Obligated Group to maintain self-insurance or to participate in any funds established to cover any insurance risks or in connection with workers' compensation, unemployment insurance, pension or profit sharing plans or other social security, or to share in the privileges or benefit required for companies participating in such arrangements;

(iii) Any judgment lien against any Member of the Obligated Group so long as such judgment is being contested in good faith and execution thereon is stayed;

(iv) (A) Rights reserved to or vested in any municipality or public authority by the terms of any right, power, franchise, grant, license, permit or provision of law, affecting any Property; (B) any liens on any Property for taxes, assessments, levies, fees, water and sewer rents, and other governmental and similar charges and any liens of mechanics, materialmen, laborers, suppliers or vendors for work or services performed or materials furnished in connection with such Property, which are not due and payable or which are not delinquent or which, or the amount or validity of which, are being contested and execution thereon is stayed or, with respect to liens of mechanics, materialmen, laborers, suppliers or vendors have been due for less than 90 days; (C) easements, rights-of-way, servitudes, restrictions, oil, gas or other mineral reservations and other minor defects, encumbrances, and irregularities in the title to any property which do not materially impair the use of such Property or materially and adversely affect the value thereof; (D) to the extent that it affects title to any Property, the Master Indenture; and (E) landlord's liens;

(v) Any Lien which is existing on the date of authentication and delivery of the initial Obligation issued under the Master Indenture provided that no such Lien may be increased, extended, renewed or modified to apply to any Property of any Member of the Obligated Group not subject to such Lien on such date or to secure Indebtedness not Outstanding as of the date of the Master Indenture, unless such Lien as so extended, renewed or modified otherwise qualifies as a Permitted Lien under the Master Indenture;

(vi) Any Lien on pledges, gifts or grants to be received in the future including any income derived from the investment thereof;

(vii) Any Lien securing all Obligations on a parity basis;

(viii) Liens on Property received by any Member of the Obligated Group through gifts, grants or bequests, such Liens being due to restrictions on such gifts, grants or bequests of Property or the income thereon;

(ix) Any Lien on moveable equipment securing Indebtedness incurred to purchase such moveable equipment, provided that the total of such Indebtedness does not exceed fifteen percent (15%) of the Net Book Value of the Property of the Obligated Group as shown on the Financial Statements of the prior Fiscal Year; and

(x) Any Lien on (i) Net Revenues securing Subordinated Indebtedness in the case of a Governmental Member of the Obligated Group or (ii) Gross Receipts securing Subordinated Indebtedness in the case of a Member of the Obligated Group that is not a Governmental Entity; provided that such Lien is expressly subordinate and junior to the Lien on Net Revenues or Gross Receipts described in paragraph

(a) above under "Security; Restrictions on Encumbering Net Revenues and Gross Receipts; Payment of Principal and Interest". (Sec. 3.05)

Limitations on Indebtedness

Each Member of the Obligated Group agrees that it will not incur any Additional Indebtedness if, after giving effect to all other Indebtedness incurred by the Obligated Group, such Indebtedness could not be incurred pursuant to paragraphs (a) through (e), inclusive, below. Any Indebtedness may be incurred only in the manner and pursuant to the terms set forth in the Master Indenture in (a) through (e) below.

(a) Long-Term Indebtedness may be incurred if prior to incurrence of the Long-Term Indebtedness there is delivered to the Master Trustee:

(i) an Officer's Certificate of an Obligated Group Representative certifying that the Long-Term Debt Service Coverage Ratio for the most recent period of twelve (12) full consecutive calendar months preceding the date of delivery of the certificate of the Obligated Group Representative for which there are Financial Statements available adjusted for revenues resulting from anticipated new customers and any planned program of rate increases that has been approved by the Governing Body of the applicable Member of the Obligated Group, taking all Long-Term Indebtedness incurred after such period and the proposed Long-Term Indebtedness into account as if such Long-Term Indebtedness had been incurred at the beginning of such period, is not less than 1.20; or

(ii) An Officer's Certificate of an Obligated Group Representative certifying (A) that the Long-Term Debt Service Coverage Ratio for the period mentioned in paragraph (a)(i) above was at least 1.20; and (B) that the projected Long-Term Debt Service Coverage Ratio is not less than 1.30 for (x) in the case of Long-Term Indebtedness (other than a Guaranty) to finance capital improvements, each of the first two full Fiscal Years succeeding the earlier of (1) the date on which such capital improvements are expected to be in operation or (2) the last day of the last Fiscal Year in which the entire Long-Term Debt Service Requirement with respect thereto has been funded from proceeds of such Long-Term Indebtedness or (y) in the case of Long-Term Indebtedness not financing capital improvements or in the case of a Guaranty, each of the two full Fiscal Years succeeding the date on which the Indebtedness is incurred, as shown by pro forma financial statements for the Obligated Group for each such period, accompanied by a statement of the relevant assumptions upon which such pro forma financial statements for the Obligated Group are based including but not limited to adjustments to revenues resulting from anticipated new customers and any planned program of rate increases that has been approved by the Governing Body of the applicable Member of the Obligated Group.

(b) Long-Term Indebtedness may be incurred for the purpose of refunding any Outstanding Long-Term Indebtedness if, prior to the incurrence of such Long-Term Indebtedness, (i) either (A) the Master Trustee receives an Officer's Certificate stating that, taking into account the Long-Term Indebtedness proposed to be incurred, the existing Long-Term Indebtedness to remain Outstanding after the refunding and the refunding of the existing Long-Term Indebtedness to be refunded, Maximum Annual Debt Service will not be increased by more than fifteen percent (15%), or (B) the conditions described in paragraphs (a)(i) or (a)(ii) above are met with respect to such proposed Long-Term Indebtedness, taking into account the existing Long-Term Indebtedness to remain Outstanding after the refunding and the refunding of the existing Long-Term Indebtedness to be refunded and (ii) the Master Trustee receives an Opinion of Counsel stating that upon the incurrence of such proposed Long-Term Indebtedness and application of the proceeds thereof (on the Crossover Date, in the case of Crossover Refunding Indebtedness), the Outstanding Long-Term Indebtedness to be refunded thereby will no longer be Outstanding.

(c) Short-Term Indebtedness may be incurred in the ordinary course of business subject to the limitation that the aggregate of all Short-Term Indebtedness shall not at any time exceed twenty-five percent (25%) of Total Operating Revenues as reflected in the Financial Statements of the Obligated Group for the most recent period of twelve consecutive months for which Financial Statements are available; provided, however, that there shall be a period of at least twenty (20) consecutive calendar days during each such period of twelve consecutive calendar months for which Financial Statements are available during which Short-Term Indebtedness shall not exceed three percent (3%) of Total Operating Revenues.

(d) Completion Indebtedness may be incurred without limitation; provided, however, that prior to the incurrence of Completion Indebtedness, the Obligated Group Representative shall furnish to the Master Trustee the following: a certificate of a Consultant estimating the costs of completing the facilities for which Completion Indebtedness is to be incurred; an Officer's Certificate of the chief financial officer of the Member of the Obligated Group for which Completion Indebtedness is to be incurred certifying that the amount of Completion Indebtedness to be incurred will be sufficient, together with other funds, if applicable, to complete construction of the facilities with respect to which Completion Indebtedness is to be incurred; and a certificate from a Consultant to the effect that the Long-Term Indebtedness originally incurred to finance the costs of the construction of the facilities in respect of which Completion Indebtedness is to be incurred was estimated prior to the date of incurrence of the original Long-Term Indebtedness to be sufficient, together with other funds, if applicable, to complete the construction of such facilities, but due to certain factors enumerated in the certificate the costs of constructing such facilities exceeded the amount of the original Indebtedness plus other funds, if applicable.

(e) Subordinated Indebtedness may be incurred without limitation.

Notwithstanding the foregoing provisions, nothing contained in the Master Indenture shall preclude a Member of the Obligated Group from incurring any obligation under a Credit Facility. (Sec.3.06)

Long-Term Debt Service Coverage Ratio

(a) Each Member of the Obligated Group covenants to set rates and charges for its facilities, services and products such that the Income Available for Debt Service for the Obligated Group, calculated at the end of each Fiscal Year, will not be less than the greater of (i) one hundred twenty percent (120%) of the Long-Term Debt Service Requirement for all Indebtedness except Subordinated Indebtedness for such Fiscal Year and (ii) one hundred percent (100%) of the Long-Term Debt Service Requirement for all Indebtedness including Subordinated Indebtedness for such Fiscal Year; provided, however, that in any case where Long-Term Indebtedness has been incurred to acquire or construct capital improvements, the Long-Term Debt Service Requirement with respect thereto shall not be taken into account in making the foregoing calculation until the first Fiscal Year commencing after the occupation or utilization of such capital improvements to the extent the Long-Term Debt Service Requirement with respect thereto is required to be paid from sources other than the proceeds of such Long-Term Indebtedness prior to such Fiscal Year.

(b) If at any time the Long-Term Debt Service Coverage Ratio required by clause (a) above, as derived from the most recent Financial Statements for the most recent Fiscal Year, is not met, the Obligated Group covenants to retain a Consultant within 30 days to make recommendations to increase such Long-Term Debt Service Coverage Ratio in the following Fiscal Year to the level required or, if in the opinion of the Consultant the attainment of such level is impracticable, to the highest level attainable. Any Consultant so retained shall be required to submit such recommendations within 45 days after being so retained. Each Member of the Obligated Group agrees that it will, to the extent permitted by law, follow the recommendations of the Consultant. So long as a Consultant shall be retained and each Member of the Obligated Group shall follow such Consultant's recommendations to the extent permitted by law, these provisions shall be deemed to have been complied with even if the Long-Term Debt Service Coverage Ratio for the following Fiscal Year is below the required level; provided, however, that the revenues of the Obligated Group shall not be less than the amount required to pay when due the total operating expenses of the Obligated Group and to pay when due the debt service on all Indebtedness of the Obligated Group for such Fiscal Year and further provided, however, that the Obligated Group shall not be required to retain a Consultant to make recommendations pursuant to the provisions of the Master Indenture described in this clause (b) more frequently than biennially. (Sec. 3.07)

Sale, Lease or Other Disposition of Operating Assets; Disposition of Cash and Investments

(a) Each Member of the Obligated Group agrees that it will not transfer in any Fiscal Year Operating Assets except for Transfers:

(i) To any Person of Operating Assets (A) the disposition of which is permitted by the provisions of the Master Indenture relating to Property that is no longer useful and (B) the Net Book Value

of which does not exceed five percent (5%) of the unrestricted fund balance (plus, in the case of Members of the Obligated Group that are stock corporations, the excess of assets over liabilities, if applicable) of the Obligated Group, as shown on the Financial Statements for the most recent period of 12 full consecutive calendar months for which such Financial Statements are available.

(ii) To any Person if prior to the sale, lease or other disposition the Master Trustee receives an Officer's Certificate of an Obligated Group Representative stating that such Operating Assets have become inadequate, obsolete, worn out, unsuitable, unprofitable, undesirable or unnecessary and the sale, lease, removal or other disposition thereof will not impair the structural soundness, efficiency or economic value of the remaining Operating Assets or adversely affect the amount of Total Operating Revenues of the Obligated Group; provided, however, that no Officer's Certificate shall be required to be delivered to the Master Trustee with respect to the Transfer of any such Operating Assets having an aggregate Net Book Value of less than the greater of (A) \$1,000,000 per year and (B) five percent (5%) of all Property, Plant and Equipment of the Obligated Group.

(iii) To another Member of the Obligated Group without limit.

(iv) To any Person provided that there shall be delivered to the Master Trustee prior to such Transfer either:

(A) an Officer's Certificate (accompanied by the Financial Statements mentioned below) certifying the Long-Term Debt Service Coverage Ratio, adjusted to exclude the revenues and expenses derived from the Operating Assets proposed to be disposed of, for the most recent period of 12 full consecutive calendar months preceding the date of delivery of the Officer's Certificate for which the Financial Statements are available and such Long-Term Debt Service Coverage Ratio is not less than 1.30 and not less than sixty-five percent (65%) of what it would have been were such Transfer not to take place; or

(B) the report of a Consultant to the effect that the forecasted Long-Term Debt Service Coverage Ratio, taking such Transfer into account, for each of the two periods of 12 full consecutive calendar months succeeding the date on which such Transfer is expected to occur, and the Long-Term Debt Service Coverage Ratio for each such period is not less than 1.30 and not less than sixty-five percent (65%) of what it would have been were such Transfer not to take place, accompanied by a statement of the relevant assumptions upon which such forecasts are based.

(v) To any Person provided that the Member of the Obligated Group proposing to make such Transfer shall receive, as consideration for such Transfer, cash, services or Property equal to the fair market value of the asset so transferred (fair market value of real property shall be evidenced by a written report of an independent appraiser who is a Member of the Appraisal Institute (MAI) which report shall state the fair market value of a date not more than two years prior to the date as of which such fair market value is being determined).

Each Member of the Obligated Group covenants to maintain records adequate to enable the Master Trustee to ascertain that the provisions of the Master Indenture described in paragraph (v) above have been complied with and to make such records available to the Master Trustee upon written request.

(b) Each Member of the Obligated Group agrees that it will not transfer cash or securities except for Transfers:

(i) To another Member of the Obligated Group without limit.

(ii) To any Person if there shall be filed with the Master Trustee an Officer's Certificate of the Obligated Group Representative, accompanied by and based upon Financial Statements for the most recent period of 12 full consecutive calendar months for which Financial Statements are available, demonstrating that the Long-Term Debt Service Coverage Ratio, for such 12-month period, would not be reduced below

1.10 if the amount of the proposed Transfer were deducted from Income Available for Debt Service for such period.

(c) Notwithstanding the foregoing provisions, nothing in the foregoing provisions shall be construed as limiting the ability of any Member of the Obligated Group to purchase or to sell Property (other than Operating Assets) in the ordinary course of business or to transfer cash, securities and other investment properties in connection with ordinary investment transactions where such purchases, sales and transfers are for substantially equivalent value. (Sec. 3.08)

Consolidation, Merger, Sale or Conveyance

(a) Each Member of the Obligated Group covenants that it will not merge or consolidate with or sell or convey all or substantially all of its assets to any Person that is not a Member of the Obligated Group, unless:

(i) Either a Member of the Obligated Group will be the successor Person, or if the successor Person is not a Member of the Obligated Group, such successor Person shall execute and deliver to the Master Trustee an appropriate instrument, satisfactory to the Master Trustee, containing the agreement of such successor Person to assume the due and punctual payment of the principal of, premium, if any, and interest on all Outstanding Obligations issued under the Master Indenture according to their tenor and the due and punctual performance and observance of all the covenants and conditions of the Master Indenture and any Supplement to the Master Indenture and (A) pledging to the Master Trustee the Net Revenues of such successor Person if such successor Person is a Governmental Member of the Obligated Group or (B) granting the Master Trustee a security interest in the Gross Receipts of such successor Person if such successor Person is not a Governmental Member of the Obligated Group; and

(ii) No Member of the Obligated Group immediately after such merger or consolidation, or sale or conveyance would be in default in the performance or observance of any covenant or condition of the Master Indenture; and

(iii) If all amounts due or to become due on any Related Bond have not been fully paid to the holder thereof, the Master Trustee shall also receive an Opinion of Bond Counsel that under then existing law, the consummation of such merger or consolidation or sale or conveyance, whether or not contemplated on any date of the delivery of such Related Bond, would not adversely affect the tax status of interest payable on any such Related Bond for purposes of federal income taxation; and

(iv) There is delivered to the Master Trustee an Officer's Certificate of an Obligated Group Representative demonstrating that the conditions described in paragraph (a)(ii) above under "Limitations on Indebtedness" have been satisfied for the issuance of an additional one dollar (\$1.00) of Additional Indebtedness, assuming such merger, consolidation or sale of assets had occurred at the beginning of the most recent period of 12 full consecutive calendar months for which Financial Statements are available, and there is also delivered to the Master Trustee either (A) an Officer's Certificate of an Obligated Group Representative demonstrating that if such merger, consolidation, sale or conveyance of assets had occurred at the beginning of the most recent period of 12 full consecutive calendar months for which Financial Statements are available, the Long-Term Debt Service Coverage Ratio for such period would not have been reduced by more than thirty-five percent (35%) and would not have been reduced to less than 1.20 or (B)(1) a written report of a Consultant indicating that the expected average Long-Term Debt Service Coverage Ratio for the two periods of 12 full consecutive calendar months succeeding the proposed date of such merger, or consolidation, or sale or conveyance of assets is greater than 1.30; provided, however, that compliance with the test set forth in this clause (B)(1) may be evidenced by an Officer's Certificate of an Obligated Group Representative in lieu of a Consultant's report where the Long-Term Debt Service Coverage Ratio for each of the two most recent periods of twelve consecutive calendar months for which Financial Statements are available preceding the proposed date of such merger or consolidation, or sale or conveyance of assets is greater than 2.00 and for the most recent period of twelve full consecutive calendar months for which Financial Statements are available it would not have been reduced by more than thirty-five percent (35%) if such merger or consolidation, or sale or conveyance of assets had occurred at the beginning of such period and (2) an Officer's Certificate of an Obligated Group Representative

demonstrating that the unrestricted fund balance (or excess of assets over liabilities, as the case may be) of the successor, resulting or acquiring Person, after giving effect to said merger or consolidation, or sale or conveyance of assets is not less than ninety percent (90%) of the unrestricted fund balance (or excess of assets over liabilities, as the case may be) of the Member of the Obligated Group which was merged into, consolidated with or whose assets were acquired by, such successor Person as reflected in the most recent Financial Statements; provided, however, that the requirements in clause (B)(2) need not be met if there is delivered to the Master Trustee an Officer's Certificate of an Obligated Group Representative demonstrating that the Long-Term Debt Service Coverage Ratio, assuming such merger or consolidation, or sale or conveyance of assets had occurred at the beginning of the most recent period of twelve full consecutive calendar months for which Financial Statements are available would have been greater than the Long-Term Debt Service Coverage Ratio for such period as reflected in the Financial Statements of the Obligated Group for such period.

(b) In case of any such consolidation or merger, or sale or conveyance and upon any assumption by the successor Person, such successor Person shall succeed to and be substituted for its predecessor, with the same effect as if it had been named in the Master Indenture as such predecessor or had become a Member of the Obligated Group pursuant to the Master Indenture. Such successor Person thereupon may cause to be signed, and may issue in its own name Obligations issuable under the Master Indenture; and upon the order of such successor Person and subject to all the terms, conditions and limitations in the Master Indenture prescribed, the Master Trustee shall authenticate and shall deliver Obligations that such successor Person shall have caused to be signed and delivered to the Master Trustee. All Outstanding Obligations so issued by such successor Person under the Master Indenture shall in all respects have the same security position and benefit under the Master Indenture as Outstanding Obligations theretofore or thereafter issued in accordance with the terms of the Master Indenture as though all of such Obligations had been issued under the Master Indenture without any such consolidation or merger, or sale or conveyance having occurred.

(c) In case of any such consolidation or merger, or sale or conveyance such changes in phraseology and form (but not in substance) may be made in Obligations thereafter to be issued under the Master Indenture as may be appropriate.

(d) The Master Trustee may accept an Opinion of Counsel (not an employee of a Member of the Obligated Group in this case) as conclusive evidence that any such consolidation or merger, or sale or conveyance, and any such assumption, complies with the provisions of the Master Indenture and that it is proper for the Master Trustee, under the provisions of the Master Indenture, to join in the execution of any instrument required to be executed and delivered by the Master Indenture. (Sec. 3.09)

Filing of Financial Statements, Certificate of No Default, Other Information

The Obligated Group covenants that it will:

(a) Within 30 days after receipt of the audit report mentioned below but in no event later than one hundred fifty (150) days after the end of each fiscal reporting period for which the Audited Financial Statements are reported upon by independent certified public accountants, file with the Master Trustee and with each Holder who may have so requested of the District in writing, a copy of the Audited Financial Statements as of the end of such fiscal reporting period accompanied by the opinion of independent certified public accountants. Such Audited Financial Statements shall be prepared in accordance with generally accepted accounting principles and shall include such statements necessary for a fair presentation of unrestricted fund financial position, results of operations and changes in unrestricted fund balance and financial position as of the end of such fiscal reporting period.

(b) Within 30 days after the receipt of the audit report, but in no event later than 150 days after the end of the fiscal reporting period, file with the Master Trustee and with each Holder who may have so requested or on whose behalf the Master Trustee may have so requested, an Officer's Certificate and a report of independent certified public accountants stating the Long-Term Debt Service Coverage Ratio for such fiscal reporting period and stating, to the best knowledge of the signers, whether any Member of the Obligated Group is in default in the performance of any covenant contained in the Master Indenture and, if so, specifying each such default of which the signers may have knowledge and whether each such default has been corrected.

(c) If an Event of Default shall have occurred and be continuing, (i) file with the Master Trustee such other financial statements and information concerning its operations and financial affairs as the Master Trustee may from time to time reasonably request, excluding specifically personnel records and (ii) provide access to its facilities for the purpose of inspection by the Master Trustee during regular business hours or at such other times as the Master Trustee may reasonably request.

(d) Within 30 days after its receipt thereof, file with the Master Trustee a copy of each report which any provision of the Master Indenture requires to be prepared by a Consultant or an Insurance Consultant. (Sec. 3.10)

Inspection of Treatment and Interceptor System

The Obligated Group covenants that it will cause a Consultant to make inspection of a representative portion of the treatment and interceptor system operated by the Obligated Group at least once in each Fiscal Year and to submit to the Commission a report setting forth (a) its findings whether the portion of the system so inspected has been maintained in good repair, working order and condition and (b) its recommendations as to the proper maintenance, repair and operation of the treatment and interceptor system operated by the Obligated Group during the ensuing fiscal year and an estimate of the amount of money necessary for such purposes.

Promptly after the receipt of such report by the Obligated Group, copies thereof shall be filed with the Master Trustee.

The Obligated Group further covenants that, if any such report of the Consultant shall set forth that the treatment and interceptor system has not been maintained in good repair, working order and condition, it will promptly restore the treatment and interceptor system to good repair, working order and condition with all expedition practicable in accordance with the recommendations of the Consultant. (Sec. 3.11)

Annual Budget

Each Member of the Obligated Group covenants that on or before the first (1st) day of June in each Fiscal Year the Governing Body of such Member of the Obligated Group will finally adopt a budget of operating and nonoperating revenues and expenses for the ensuing Fiscal Year. On or before the 30th day of June in such Fiscal Year copies of such annual budget shall be filed with the Master Trustee and with each Holder who may have so requested of the District in writing. (Sec. 3.12)

Renewal and Replacement Reserve

The District covenants that it will establish a reserve to finance anticipated renewals, replacements, extensions, additions and extraordinary repairs of the Wastewater System and that it will reserve in retained earnings and credit to such reserve Net Revenues to the extent needed to finance such anticipated renewals, replacements, extensions, additions and extraordinary repairs. (Sec. 3.13)

Parties Becoming Members of the Obligated Group

To the extent permitted by law, Persons which are not Members of the Obligated Group may, with the written prior consent of the District, become Members of the Obligated Group, if:

(a) The Person which is becoming a Member of the Obligated Group shall execute and deliver to the Master Trustee an appropriate instrument, satisfactory to the Master Trustee, containing the agreement of such Person (i) to become a Member of the Obligated Group under the Master Indenture and any Supplements and thereby become subject to compliance with all provisions of the Master Indenture and any Supplements pertaining to a Member of the Obligated Group (such agreement being limited, in the case of a Governmental Entity, to any Operating Units which are designated in accordance with the provisions of the Master Indenture described in paragraph (f) below) including the pledge provided for and the performance and observance of all covenants and obligations of a Member of the Obligated Group under the Master Indenture, (ii) to adopt the same Fiscal Year as that of the District, and (iii) unconditionally and irrevocably to guarantee to the Master Trustee and each other

Member of the Obligated Group that all Obligations issued and then Outstanding or to be issued and Outstanding under the Master Indenture will be paid in accordance with the terms thereof and of the Master Indenture when due; and

(b) Each instrument executed and delivered to the Master Trustee in accordance with paragraph (a) above shall be accompanied by an Opinion of Counsel, addressed to and satisfactory to the Master Trustee, to the effect that such instrument has been duly authorized, executed and delivered by such Person and constitutes a valid and binding obligation enforceable in accordance with its terms, except as enforceability may be limited by bankruptcy laws, insolvency laws, other laws affecting creditors' rights generally, equity principles and laws dealing with fraudulent conveyances; and

(c) There shall be filed with the Master Trustee an Officer's Certificate of an Obligated Group Representative demonstrating that the conditions described in paragraph (a)(ii) under "Limitations on Indebtedness" above have been satisfied for the incurrence of an additional \$1.00 of Additional Indebtedness, assuming such admission actually occurred at the beginning of the most recent period of 12 full consecutive calendar months for which Financial Statements are available, and there is also delivered to the Master Trustee either (i) an Officer's Certificate of an Obligated Group Representative demonstrating that the Long-Term Debt Service Coverage Ratio for the most recent period of 12 full consecutive calendar months for which Financial Statements are available (A) would not have been reduced by more than thirty-five percent (35%) and would not have been reduced to less than 1.20 or (B) would be greater than in the absence of such Person becoming a Member of the Obligated Group; or (ii) the written report of a Consultant demonstrating that the expected average Long-Term Debt Service Coverage Ratio for the two periods of 12 full consecutive calendar months succeeding the proposed date of such admission is greater than 1.30; provided, however, that compliance with the tests set forth in clause (ii) may be evidenced by an Officer's Certificate of an Obligated Group Representative in lieu of a Consultant's report where the Long-Term Debt Service Coverage Ratio for each of the two most recent periods of twelve consecutive calendar months for which Financial Statements are available preceding the proposed date of such admission is greater than 2.00 and that for the most recent period of twelve full consecutive calendar months for which Financial Statements are available it would not have been reduced by more than thirty-five percent (35%) if such admission had occurred at the beginning of such period; and

(d) If all amounts due or to become due on any Related Bond have not been paid to the holders thereof, there shall be filed with the Master Trustee, an Opinion of Bond Counsel, in form and substance satisfactory to the Master Trustee, to the effect that the consummation of such transaction would not adversely affect the tax status of interest payable on any such Related Bond for purposes of federal income taxation; and

(e) The Obligated Group Representative shall have delivered to the Master Trustee an Opinion of Counsel to the effect that the addition of such Person to the Obligated Group will not necessitate the registration of any Obligations under the Securities Act of 1933, as amended, or cause the qualification of the Master Indenture or any Supplement under the Trust Indenture Act of 1939, as amended, to be required, or, if such registration or qualification is required, that all applicable registration and qualification provisions of said acts have been complied with; and

(f) If the Person that is becoming a Member of the Obligated Group is a Governmental Entity it shall designate which Operating Units of such Governmental Entity are to become subject to compliance with the provisions of the Master Indenture and any Supplements pertaining to a Member of the Obligated Group, including the pledge provided for in the Master Indenture and the performance and observance of all covenants and obligations of a Member of the Obligated Group thereunder.

The Obligated Group Representative shall give any rating agency which then has a rating in effect for any series of Related Bonds written notice not later than thirty (30) days prior to the addition of a Member of the Obligated Group. (Sec. 3.14)

Operating Units Becoming Designated Units

To the extent permitted by law, Operating Units which are not Designated Units may become Designated Units, if:

(a) The Governmental Member of the Obligated Group shall execute and deliver to the Master Trustee an appropriate instrument, satisfactory to the Master Trustee, containing the agreement of the Governmental Member of the Obligated Group to cause such Unit to become a Designated Unit under the Master Indenture and thereby subject the Governmental Member of the Obligated Group to compliance with all provisions of the Master Indenture pertaining to the Governmental Member of the Obligated Group with respect to such Designated Unit, including the performance and observance of all covenants and obligations of the Governmental Member of the Obligated Group.

(b) The Governmental Member of the Obligated group shall file with the Master Trustee Financial Statements for such Unit for the most recent Fiscal Year.

(c) The conditions set forth in paragraphs (c) and (d) under "Parties Becoming Members of the Obligated Group" above shall be satisfied with respect to such Unit becoming a Designated Unit. (Sec. 3.15).

Withdrawal from the Obligated Group; Cessation of Status as Designated Unit

(a) The District may not withdraw from the Obligated Group and the Wastewater System may not cease to be a Designated Unit under any circumstances. Any Member of the Obligated Group other than the District may withdraw from the Obligated Group and any Designated Unit other than the Wastewater System may cease to be a Designated Unit with the prior written consent of the District if, prior to the taking of such action, there is delivered to the Master Trustee:

(i) An Officer's Certificate of an Obligated Group Representative demonstrating that (A) all Obligations issued by such Member of the Obligated Group or for such Designated Unit are no longer Outstanding, or (B) an amount of cash or securities sufficient to accomplish the requirements of clause (A) of this paragraph has been paid by such Member to the Master Trustee, provided that if all amounts due on any Related Bonds which bear interest which is not includable in the gross income of the recipient thereof under the Code have not been paid to the holders thereof, there shall be delivered to the Master Trustee an Opinion of Bond Counsel, in form and substance satisfactory to the Master Trustee, to the effect that under then existing law such Member's withdrawal from the Obligated Group or such Designated Unit's ceasing to be a Designated Unit, whether or not contemplated on any date of delivery of any Related Bond, would not affect the tax status of interest payable on such Related Bond for purposes of federal income taxation; and

(ii) An Officer's Certificate of an Obligated Group Representative demonstrating that the conditions described in paragraph (a)(ii) under "Limitations on Indebtedness" above have been satisfied for the incurrence of an additional \$1.00 of Additional Indebtedness, assuming such action to have occurred at the beginning of the most recent period of 12 full consecutive calendar months for which Financial Statements are available, and either (A) a certificate of an Obligated Group Representative demonstrating that the Long-Term Debt Service Coverage Ratio for the most recent period of 12 full consecutive calendar months for which Financial Statements are available (1) would not, if such action had occurred at the beginning of such period, be reduced by more than thirty-five percent (35%) and would not be reduced to less than 1.20 or (2) would be greater than in the absence of such action; or (B) a written report of a Consultant demonstrating that the expected average Long-Term Debt Service Coverage Ratio for the two periods of 12 full consecutive calendar months succeeding the proposed date of such action is greater than 1.30; provided, however, that compliance with the test set forth in clause (B) above may be evidenced by an Officer's Certificate of an Obligated Group Representative in lieu of a Consultant's report where the Long-Term Debt Service Coverage Ratio for each of the two periods of twelve full consecutive calendar months succeeding the proposed date of such action is greater than 2.00 and not less than sixty-five percent (65%) of what it would have been were such action not to take place, assuming such action had occurred on the first day of the most recent 12 month period for which Financial Statements of the Obligated Group are available.

(b) If any Member withdraws from the Obligated Group or any Designated Unit ceases to be a Designated Unit pursuant to clause (a) above, any guaranty or other obligation assumed by such Member or such Designated Unit pursuant to the provisions of the Master Indenture shall be released and discharged in full and all liability of

such Member of the Obligated Group or such Designated Unit with respect to all Obligations Outstanding under the Master Indenture shall cease. (Sec. 3.16)

Defaults and Remedies

Events of Default

An Event of Default under the Master Indenture is any of the following events: (a) the failure by the Members of the Obligated Group to make any payment of the principal of, the redemption premium, if any, or interest on any Obligations when due and payable, whether at maturity, by proceedings for redemption, by acceleration or otherwise in accordance with the terms thereof, of the Master Indenture or any Supplement; (b) the failure by any Member of the Obligated Group to perform, observe or comply with any covenant or agreement under the Master Indenture and such failure continues for a period of 30 days after written notice of such failure, requiring the same to be remedied, shall have been given to the Members of the Obligated Group by the Master Trustee, or to the Members of the Obligated Group and the Master Trustee by the Holders of not less than a majority in aggregate principal amount of Obligations then Outstanding; provided, however, that if said failure is such that it cannot be corrected within such 30-day period, no Event of Default will exist if corrective action is instituted within such 30-day period and diligently pursued until the Event of Default is corrected; (c) an Event of Default under a Related Bond Indenture or upon a Related Bond; (d) failure by any Member of the Obligated Group to make any required payment of any Indebtedness (other than Obligations issued and Outstanding under the Master Indenture), whether such Indebtedness now exists or shall hereafter be created, and any applicable grace period shall have expired, or an event of default as defined in any mortgage, indenture or instrument under which there may be issued, secured or evidenced any Indebtedness, whether such Indebtedness now exists or shall hereafter be created, shall occur, which event of default shall not have been waived by the holder of such mortgage, indenture or instrument, and as a result of such failure to pay or other event of default such Indebtedness shall have been accelerated; provided, however, that such default shall not constitute an Event of Default if within 30 days (i) written notice is delivered to the Master Trustee that such Member of the Obligated Group is contesting the payment of such Indebtedness and the amount of such Indebtedness is less than one-half of one percent (0.50%) of Income Available for Debt Service of the immediately preceding Fiscal Year or (ii) if such Indebtedness is equal to or greater than one-half of one percent (0.5%) of Income Available for Debt Service, within the time allowed for service of a responsive pleading if a proceeding to enforce payment of the Indebtedness is commenced, any Member of the Obligated Group in good faith shall commence proceedings to contest the obligation to pay or alleges the nonexistence or payment of such Indebtedness; (e) the entry of a decree or order by a court having jurisdiction in the premises for an order for relief against any Member of the Obligated Group, or approving as properly filed a petition seeking reorganization, arrangement, adjustment or composition of or in respect of such Member under the United States Bankruptcy Code or any other applicable federal or state law, or appointing a receiver, liquidator, custodian assignee or sequestrator (or other similar official) of such Member or of any substantial part of its Property, or ordering the winding up or liquidation of its affairs, and the continuance of any such decree or order unstayed and in effect for a period of 90 consecutive days; and (f) the institution by any Member of the Obligated Group of proceedings for an order for relief, or the consent by it to an order for relief against it, or the filing by it of a petition or answer or consent seeking reorganization, arrangement, adjustment, composition or relief under the United States Bankruptcy Code or any other similar applicable federal or state law, or the consent by it to the filing of any such petition or to the appointment of a receiver, liquidator, custodian, assignee, trustee or sequestrator (or other similar official) of such Member of the Obligated Group or of any substantial part of its Property, or the making by it of an assignment for the benefit of creditors, or the admission by it in writing of its inability to pay its debts generally as they become due. (Sec. 4.01)

Acceleration; Annulment of Acceleration

Upon the occurrence and during the continuation of any Event of Default under the Master Indenture, the Master Trustee may and, upon the written request of (i) the Holders of not less than a majority in aggregate principal amount of Obligations Outstanding or (ii) any Person properly exercising the right given to such Person under any Supplement to require acceleration of the Obligations issued pursuant to such Supplement, shall, by notice to the Members of the Obligated Group, declare all Obligations Outstanding immediately due and payable, whereupon such Obligations shall become and be immediately due and payable, anything in the Obligations or in the Master Indenture to the contrary notwithstanding; provided, however, that if the terms of any Supplement give a Person the

right to consent to acceleration of the Obligations issued pursuant to said Supplement, the Obligations issued pursuant to such Supplement may not be accelerated by the Master Trustee unless such consent is properly obtained pursuant to the terms of such Supplement. In the event Obligations are accelerated, there shall be due and payable on such Obligations an amount equal to the total principal amount of all such Obligations, plus all interest accrued thereon to the date of acceleration and, to the extent permitted by applicable law; which accrues to the date of payment.

If, at any time after the principal of the Obligations has been so declared due and payable and before the entry of final judgment or decree in any proceeding relating thereto, (i) the Obligated Group has paid or caused to be paid or deposited with the Master Trustee moneys or Defeasance Obligations sufficient to pay all matured installments of interest and interest on installments of principal and interest and principal or redemption prices then due (other than the principal then due only because of such declaration) of all Obligations Outstanding; (ii) the Obligated Group has paid or caused to be paid or deposited with the Master Trustee moneys sufficient to pay the charges, compensation, expenses, disbursements, advances, fees and liabilities of the Master Trustee; (iii) all other amounts then payable by the Obligated Group under the Master Indenture shall have been paid or a sum sufficient to pay the same shall have been deposited with the Master Trustee; and (iv) every Event of Default (other than a default in the payment of the principal of such Obligations then due only because of such declaration) shall have been remedied, then the Master Trustee may, and upon the written request of Holders of not less than a majority in aggregate principal amount of the Obligations Outstanding shall, annul such declaration and its consequences with respect to any Obligations or portions thereof not then due by their terms. No such annulment shall extend to or affect any subsequent Event of Default or impair any right consequent thereon. (Sec. 4.02)

Additional Remedies and Enforcement of Remedies

Upon the occurrence and continuance of any Event of Default, the Master Trustee may, and upon the written request of the Holders of not less than a majority in aggregate principal amount of the Obligations Outstanding, together with indemnification of the Master Trustee to its satisfaction, shall, proceed forthwith to protect and enforce its rights and the rights of such the Holders by such suits, actions or proceedings as the Master Trustee being advised by counsel shall deem expedient.

Regardless of the happening of an Event of Default, the Master Trustee, if requested in writing by the Holders of not less than a majority in aggregate principal amount of the Obligations then Outstanding, shall, when indemnified to its satisfaction, institute and maintain such suits and proceedings necessary or expedient to prevent any impairment of security by any acts which may be unlawful or in violation of the Master Indenture, or to preserve or protect the interests of the Holders, provided that such request and action to be taken by the Master Trustee are not in conflict with any applicable law or the Master Indenture and, in the Master Trustee's sole judgment, are not unduly prejudicial to the interest of the Holders not making such request. (Sec. 4.03)

Application of Gross Receipts and Other Moneys After Default

During the continuance of an Event of Default all Net Revenues of Governmental Members of the Obligated Group and all Gross Receipts of Members of the Obligated Group that are not Governmental Entities and other moneys received by the Master Trustee, after payment of (i) the costs and expenses of the proceedings resulting in the collection of such moneys and of the expenses and advances incurred or made by the Master Trustee with respect thereto and all other fees and expenses of the Master Trustee under the Master Indenture and (ii) with respect to Gross Receipts of a Member of the Obligated Group that is not a Governmental Entity the payment of the expenses of operating such Member of the Obligated Group, shall be applied as follows:

(a) Unless the principal of all Outstanding Obligations shall have become or have been declared due and payable: First: to the payment of the Persons entitled thereto of all installments of interest then due on Obligations in the order of the maturity of such installments, and, if the amount available shall not be sufficient to pay in full all installments maturing on the same date, then ratably, according to the amounts due, without discrimination or preference; and Second: to the payment of the Persons entitled thereto of the unpaid principal installments of any Obligations then due, whether at maturity or by call for redemption, in the order of their due dates, and if amounts available shall not be sufficient to pay in full all Obligations due on any date, then to the payment thereof ratably, according to the amounts of principal installments due on such date, without discrimination or preference.

(b) If the principal of all Outstanding Obligations shall then be or have been declared to be due and payable, to the payment of the principal and interest then due and unpaid 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 Obligation over any other Obligation, ratably, according to the amounts due respectively for principal and interest, to the Persons entitled thereto, without discrimination or preference.

(c) If the principal of all Outstanding Obligations shall have been declared due and payable, and if such declaration shall thereafter have been rescinded and annulled under the provisions of the Master Indenture, then, subject to the provisions of paragraph (b) above in the event that the principal of all Outstanding Obligations shall later become due or be declared due and payable, the moneys shall be applied in accordance with the provisions of paragraph (a) above.

Moneys to be applied by the Master Trustee during a continuance of an Event of Default shall be applied as the Master Trustee shall determine, having due regard for the amount available and the likelihood of additional moneys becoming available in the future. Whenever the Master Trustee shall apply such moneys, it shall fix the date upon which such application is to be made and upon such date interest on the amounts of principal to be paid on such dates shall cease to accrue. The Master Trustee shall give notice as it may deem appropriate of the deposit with it of any such moneys and of the fixing of any such date, and shall not be required to make payment to the Holder of any unpaid Obligation until such Obligation shall be presented to the Master Trustee for appropriate endorsement of any partial payment or for cancellation if fully paid. (Sec. 4.04)

Holders' Control of Proceedings

If any Event of Default shall have occurred and be continuing, the Holders of not less than a majority in aggregate principal amount of Obligations then Outstanding shall have the right, subject to the terms of the Master Indenture, to direct the method and place of conducting any enforcement proceedings. (Sec. 4.07)

Waiver of Event of Default

No delay or omission of the Master Trustee or of any Holder to exercise any right or power accruing upon any Event of Default shall impair any such right or power or shall be construed to be a waiver of any such Event of Default or an acquiescence therein. Every power and remedy given to the Master Trustee and the Holders, respectively, may be exercised from time to time and as often as may be deemed expedient by them. The Master Trustee may waive any Event of Default which in its opinion shall have been remedied before the entry of final judgment or decree in any suit, action or proceeding instituted by it under the provisions of the Master Indenture or before the completion of the enforcement of any other remedy under the Master Indenture. The Master Trustee, upon the written request of the Holders of not less than a majority of the aggregate principal amount of Obligations then Outstanding, shall waive any Event of Default under the Master Indenture and its consequences (except payment defaults which have not been cured, which may be waived only by written consent of the Holders of all the Obligations (with respect to which such payment default exists) then Outstanding). In case of a waiver by the Master Trustee of an Event of Default under the Master Indenture, all parties shall be restored to their former positions but no such waiver shall extend to any subsequent or other Event of Default. (Sec. 4.09)

Appointment of Receiver

Upon the occurrence of any Event of Default, the Master Trustee shall be entitled to the appointment of a receiver or receivers of the Property of the Obligated Group with such powers as the court making such appointment shall confer. (Sec. 4.10)

Notice of Default

The Master Trustee shall, within 10 days after it has knowledge of the occurrence of an Event of Default, mail to all Holders as the names and addresses of such Holders appear upon the books of the Master Trustee, notice of such Event of Default known to the Master Trustee, unless such Event of Default shall have been cured before the giving of such notice; provided that, except in the case of default in the payment of the principal of or redemption

premium, if any, or interest on any of the Obligations and the Events of Default specified in paragraphs (e) and (f) under "Defaults and Remedies - Events of Default" above, the Master Trustee shall be protected in withholding such notice if and so long as, the board of directors, the executive committee, or a trust committee of directors or a responsible officer of the Master Trustee in good faith determines that the withholding of such notice is in the interests of the Holders. (Sec. 4.12)

Removal of the Master Trustee

The Master Trustee may resign on its own motion or may be removed at any time by a written instrument signed by the Holders of not less than a majority of the principal amount of Obligations then Outstanding, or so long as no Event of Default has occurred and is continuing, by an instrument in writing signed by the Obligated Group Representative. (Sec. 5.04)

Supplements and Amendments

Supplements Not Requiring Consent of Holders

The Master Indenture may be supplemented or amended without the consent of or notice to any of the Holders for one or more of the following purposes: to cure an ambiguity or formal defect or omission; to correct or supplement any provision which may be inconsistent with any other provision, or to make any other provisions with respect to matters or questions arising under the Master Indenture and which shall not materially and adversely affect the interests of the Holders; to grant or confer ratably upon all Holders any additional rights, remedies, powers or authority that may lawfully be granted or conferred upon them; to qualify the Master Indenture under the Trust Indenture Act of 1939, as amended, or corresponding provisions of federal laws from time to time in effect; to create and provide for the issuance of Indebtedness as permitted under the Master Indenture; to obligate a successor to any Member of the Obligated Group; and to comply with any state or federal securities law. (Sec. 6.01)

Supplements Requiring Consent of Holders

Other than supplements referred to in the preceding paragraph, the Holders of not less than a majority in aggregate principal amount of the Obligations then Outstanding shall have the right to approve execution of Supplements modifying, altering, amending, adding to or rescinding, in any particular, the Master Indenture except a Supplement which would:

- (i) Effect a change in the times, amounts or currency of payment of the principal of, premium, if any, and interest on any Obligation or a reduction in the principal amount or redemption price of any Obligation or the rate of interest thereon, without the consent of the Holder of such Obligation;
- (ii) Permit the preference or priority of any Obligation over any other Obligation, without the consent of the Holders of all Obligations then Outstanding; or
- (iii) Reduce the aggregate principal amount of Obligations then Outstanding the consent of the Holders of which is required to authorize such Supplement without the consent of the Holders of all Obligations then Outstanding.

All Supplements executed pursuant to the Master Indenture shall be binding on all Holders of Obligations. (Sec. 6.02)

Satisfaction and Discharge of Indenture

If (i) an Obligated Group Representative shall deliver to the Master Trustee for cancellation all Obligations theretofore authenticated and not cancelled, or (ii) all Obligations not cancelled or delivered to the Master Trustee for cancellation have become due and payable and money sufficient to pay the same shall have been deposited with the Master Trustee, or (iii) all Obligations that have not become due and payable and have not been cancelled or delivered to the Master Trustee for cancellation shall be Defeased Obligations, and if in all cases the Members of the

Obligated Group will also pay or cause to be paid all other sums payable by the Members of the Obligated Group, then the Master Indenture shall cease to be of further effect, and the Master Trustee, on demand of the Members of the Obligated Group, and at the cost and expense of the Members of the Obligated Group, shall execute proper instruments acknowledging satisfaction of and discharging the Master Indenture. (Sec. 7.01)

SUMMARY OF THE TRUST AGREEMENT

Various Funds Created by the Trust Agreement

The Trust Agreement creates the following funds:

1. The Bond Fund, and
2. The Debt Service Reserve Fund.

The Trust Agreement also creates an Issuance Account. The money in each of the aforementioned funds and account will be held in trust and will be subject to a lien and charge in favor of the Holders of the Series 2003 Bonds until paid out or transferred as provided in the Trust Agreement. (Sec. 401 and Sec. 501)

Issuance Account

All issuance costs incurred in connection with the Series 2003 Bonds and paid from the initial proceeds of the Series 2003 Bonds will be paid from the Issuance Account. (Sec. 401)

Requisitions signed by an appropriate officer or employee of the District will be filed with the Bond Trustee before payments from the Issuance Account are made in accordance with the Trust Agreement. (Sec. 403)

Deposits to the Bond Fund and Reserve Fund

The District will make payments directly to the Bond Trustee for deposit in the Bond Fund in amounts sufficient to pay in full, when due (whether by maturity, acceleration or otherwise), all Series 2003 Bonds issued under the Trust Agreement, together with the total interest thereon.

The Bond Trustee will deposit or transfer, as appropriate, moneys or Investment Obligations maturing prior to the next ensuing Interest Payment Date or the next ensuing October 1 upon which the principal of any Series 2003 Bond is stated to mature in the following order, subject to the credits provided in the Trust Agreement:

(i) into the Bond Fund, beginning on March 31, 2004, and continuing on the Business Day next preceding each Interest Payment Date thereafter, an amount equal to the interest payable on the Series 2003 Bonds due on such Interest Payment Date;

(ii) into the Bond Fund, beginning on September 30, 2004, and continuing on the Business Day next preceding each October 1 thereafter, an amount equal to the principal of all Series 2003 Bonds due on such October 1; and

(iii) unless a Qualified Reserve Fund Substitute shall be in effect, beginning on the 25th day of the month following the month in which money is transferred from the Debt Service Reserve Fund to the Bond Fund to cure a deficiency therein pursuant to the Trust Agreement, into the Debt Service Reserve Fund one-twelfth (1/12) of the amount so transferred until the amount on deposit is equal to the Debt Service Reserve Fund Requirement and, beginning on the 25th day of the month following a valuation made in accordance with the Trust Agreement in which a loss resulting from a decline in the value of Investment Obligations held for the credit of the Debt Service Reserve Fund is computed, into the Debt Service Reserve Fund one-sixth (1/6) of the amount of such loss until the amount of such loss is reimbursed.

If, after giving effect to the credits specified below, any installment of payments made by the District is insufficient to enable the Bond Trustee to make the deposits required above, the Bond Trustee will notify the District and request that each future installment of payments due from the District be increased as may be necessary to make up any previous deficiency in any of the required payments and to make up any deficiency or loss in any of the above-mentioned funds.

To the extent that investment earnings are credited to the Bond Fund in accordance with the Trust Agreement, or amounts are credited thereto as a result of the application of proceeds of the Series 2003 Bonds or a transfer of investment earnings on any other fund or account held by the Bond Trustee, or otherwise, future deposits to the Bond Fund will be reduced by the amount so credited, and the payments due from the District in the months following the date upon which such amounts are credited will be reduced by the amounts so credited. (Sec. 502)

Bond Fund

Money on deposit in the Bond Fund will be transferred by the Bond Trustee to the Bond Registrar on the Business Day prior to each Interest Payment Date or date for payment of Defaulted Interest to pay interest due on the Series 2003 Bonds held by each Holder which is not a Securities Depository Nominee. The Bond Registrar will then, not later than the Business Day next preceding each Interest Payment Date, remit to each Holder which is not a Securities Depository Nominee the amount required to pay interest on such Series 2003 Bonds when due and payable. At such time as to enable the Bond Registrar to make payments of interest on the Series 2003 Bonds in accordance with any existing agreement between the Bond Registrar and any Securities Depository, the Bond Trustee will withdraw from the Bond Fund and remit by wire transfer to the Bond Registrar, in Federal Reserve or other immediately available funds, the amounts required to pay to any Holder which is a Securities Depository Nominee interest on the Series 2003 Bonds on the next ensuing Interest Payment Date. If the balance in the Bond Fund on the Business Day next preceding an Interest Payment Date is insufficient to pay interest due on the Series 2003 Bonds on an Interest Payment Date, then the Bond Trustee will immediately notify the District such deficiency and the District will immediately deliver funds sufficient to cure the same. If the amount so delivered is not sufficient to cure the deficiency in the Bond Fund, the Bond Trustee will transfer to such Fund such amount as may be necessary to remedy the deficiency therein from the Debt Service Reserve Fund.

Money on deposit in the Bond Fund will be transferred by the Bond Trustee to the Bond Registrar on each October 1 to pay the principal of all Series 2003 Bonds maturing on such October 1. In the event that the balance in the Bond Fund on the Business Day next preceding any October 1 is insufficient for the payment of principal of all Series 2003 Bonds becoming due on such October 1, the Bond Trustee will immediately notify the District of the amount of the deficiency. Upon notification, the District, will immediately deliver to the Bond Trustee an amount sufficient to cure the same. If the amount so delivered is not sufficient to cure the deficiency in the Bond Fund, the Bond Trustee will transfer to such Fund such amount as may be necessary to remedy the deficiency therein from the Debt Service Reserve Fund. (Sec. 503)

Debt Service Reserve Fund; Qualified Reserve Fund Substitute

At Closing no funds will be deposited in the Debt Service Reserve Fund. The District agrees that if (a) the Liquidity Ratio of the Obligated Group, as calculated based on (i) the Financial Statements of the Obligated Group as of the end of each Fiscal Year or (ii) the unaudited interim financial statements for the first six months of each Fiscal Year, is less than 1.35 or (b) the Long-Term Debt Service Coverage Ratio, as calculated pursuant to the Master Indenture, is less than 1.35, the District will fund, within six (6) months after the end of such Fiscal Year or such six-month period, as applicable, the Debt Service Reserve Fund in an amount equal to the Debt Service Reserve Fund Requirement. Notwithstanding the foregoing provision, the District may elect at any time to waive such provision and fund the Debt Service Reserve Fund in an amount equal to the Debt Service Reserve Fund Requirement.

The Bond Trustee will use amounts in the Debt Service Reserve Fund to make transfers to the Bond Fund to the extent necessary to pay interest on and principal of the Series 2003 Bonds (whether at maturity or by acceleration), whenever and to the extent that the money on deposit in the Bond Fund is insufficient for such purposes.

If on any date of valuation the value of the money and investments held in the Debt Service Reserve Fund exceeds the Debt Service Reserve Fund Requirement on the Series 2003 Bonds, including any excess created in whole or in part by the interest earnings on such Fund, an amount equal to such excess will be transferred by the Bond Trustee, (i) to the Bond Fund or (ii) if the District shall deliver to the Bond Trustee a written statement setting forth the use which the District proposes to make of such excess amounts, accompanied by an opinion of bond counsel to the District addressed to the Bond Trustee to the effect that such proposed use will not cause the interest on the Series 2003 Bonds to be includable in the gross income of the owners thereof for purposes of federal income taxation, to the District.

The District may, at any time, deliver to the Bond Trustee a Qualified Reserve Fund Substitute. In such event, if the District shall also deliver to the Bond Trustee a written statement setting forth the use which the District proposes to make of the cash and Investment Obligations then on deposit to the credit of the Debt Service Reserve Fund, accompanied by an opinion of bond counsel to the District, addressed to the Bond Trustee, to the effect that such proposed use will not cause the interest on the Series 2003 Bonds to be includable in the gross income of the owners thereof for purposes of federal income taxation, the Bond Trustee will transfer to the District all amounts on deposit to the credit of the Debt Service Reserve Fund.

If any Qualified Reserve Fund Substitute shall be in effect, the Bond Trustee agrees to give such notices and execute such documents as shall be required to assure that funds (i) are available in such amounts and at such times to assure timely payment of principal of and interest on the Series 2003 Bonds and (ii) are drawn to fund the Debt Service Reserve Fund in an amount equal to the Debt Service Reserve Fund Requirement at least six (6) months prior to the expiration date of the Qualified Reserve Fund Substitute unless (a) the Bond Trustee shall have received a substitute Qualified Reserve Fund Substitute to replace such expiring Qualified Reserve Fund Substitute or (b) the expiration date of the expiring Qualified Reserve Fund Substitute is the same date as the final stated maturity date of the Series 2003 Bonds. (Sec. 504 and Sec. 707)

Investment of Money

Money held for the credit of all funds and accounts created under the Trust Agreement will be continuously invested and reinvested by the Bond Trustee in Investment Obligations, subject to the yield restrictions set forth in the Tax Certificate. Any such Investment Obligations shall mature not later than the respective dates when the money held for the credit of such funds or accounts will be required for the purposes intended; provided, however, that Investment Obligations deposited in the Debt Service Reserve Fund shall mature no later than ten (10) years from the date on which such Investment Obligations were deposited therein.

Investment Obligations acquired with money and credited to any fund or account established under the Trust Agreement will be held by or under the control of the Bond Trustee and will be deemed at all times to be part of such fund or account in which such money was originally held. Interest accruing on such Investment Obligations and any profit or loss resulting upon the disposition or maturity of the same will be credited to or charged against the fund or account to which the same are credited. The Bond Trustee will sell at the best price attainable or reduce to cash a sufficient amount of such Investment Obligations whenever it is necessary to provide money to make any payment or transfer of money from any such fund or account. The Bond Trustee will not be liable or responsible for any loss resulting from any such investment. (Sec. 602)

Valuation

For the purpose of determining the amount on deposit in any fund or account, Investment Obligations in which money in such fund or account is invested will be valued (a) at face value if such Investment Obligations mature within six months from the date of valuation, and (b) if such Investment Obligations mature more than six months after the date of valuation thereof, at the price at which such Investment Obligations are redeemable by the holder at his option if so redeemable or, if not so redeemable, at the lesser of (i) the cost of such Investment Obligations minus the amortization of any premium or plus the amortization of any discount thereon and (ii) the market value of such Investment Obligations.

The Bond Trustee will value the Investment Obligations in the funds and accounts established under the Trust Agreement five Business Days prior to each Interest Payment Date. In addition, the Investment Obligations

will be valued by the Bond Trustee at any time requested by the District Representative on reasonable notice to the Bond Trustee (which period of notice may be waived or reduced by the Bond Trustee), except that the Bond Trustee will not be required to value the Investment Obligations more than once in any calendar month. (Sec. 603)

Compliance with Covenants, Conditions and Agreements in Master Indenture

The District covenants that, so long as the Series 2003 Bonds are Outstanding, it will comply with each and every covenant, condition and agreement in the Master Indenture and in the Trust Agreement. Each such covenant, condition and agreement in the Master Indenture is incorporated by reference and made a part of the Trust Agreement with the same effect intended as though the text of each such covenant, condition and agreement were set forth in the Trust Agreement as express covenants, conditions and agreements of the District. (Sec. 703)

Enforcement of Obligation No. 2

The Bond Trustee may enforce all obligations of the Members of the Obligated Group under the Master Indenture, Supplement No. 2 and Obligation No. 2 for and on behalf of the Holders of the Series 2003 Bonds, whether or not the District is in default thereunder. (Sec. 704)

Designation of Funds

No later than last Business Day of each month, the District shall specifically earmark cash, cash equivalents or marketable securities or any combination thereof in an amount equal to (a) one-sixth (1/6) of the interest payable on the next ensuing Interest Payment Date and (b) one-twelfth (1/12) of the principal of Series 2003 Bonds due on the next ensuing October 1, and such funds shall be used solely for paying such interest on and principal of the Series 2003 Bonds. (Sec. 708)

Events of Default

Each of the following events is an Event of Default under the Trust Agreement:

- (a) payment of any installment of interest on any of the Series 2003 Bonds shall not be made by the District when due and payable; or
- (b) payment of the principal of any Series 2003 Bond shall not be made by the District when due and payable, whether at maturity or by acceleration or otherwise; or
- (c) default in the due and punctual performance of any other of the covenants, conditions, agreements and provisions contained in the Trust Agreement or any agreement supplemental thereto, including any covenant, condition, agreement or provision in the Master Indenture applicable to the District and incorporated by reference in the Trust Agreement, and such default shall continue for thirty (30) days after receipt by the District of a written notice from the Bond Trustee specifying such default and requiring the same to be remedied; provided, however, if prior to the expiration of such 30-day period the District institutes action reasonably designed to cure such default, no Event of Default shall be deemed to have occurred upon the expiration of such 30-day period for so long as the District pursues such curative action with reasonable diligence and provided that such curative action can be completed within a reasonable time; or
- (d) The Master Trustee shall have declared the aggregate principal amount of Obligation No. 2 and all interest due thereon immediately due and payable in accordance with the provisions of the Master Indenture. (Sec. 801)

Remedies on Default

Upon the happening and continuance of an Event of Default specified under "Events of Default" above, the Bond Trustee may take the following remedial steps: (i) in the case of an Event of Default described in paragraph (a) or (b) under "Events of Default" above, the Bond Trustee may take whatever action at law or in equity is necessary

or desirable to collect the payments then due under the Trust Agreement or Obligation No. 2; (ii) in the case of an Event of Default described in paragraph (c) under "Events of Default" above, the Bond Trustee may take whatever action at law or in equity is necessary or desirable to enforce performance, observance or compliance by the District with any covenant, condition, agreement or provision under the Trust Agreement or under the Master Indenture; and (iii) in the case of an Event of Default described in paragraph (d) under "Events of Default" above, the Bond Trustee may take whatever action at law or in equity is necessary or desirable to enforce the Master Indenture, but only as the Master Trustee shall direct. (Sec. 802)

Upon the happening and continuance of any Event of Default under the Trust Agreement, the Bond Trustee may, and upon the written request of the Holders of not less than a majority in aggregate principal amount of Series 2003 Bonds then Outstanding shall, by notice in writing to the District, declare the principal of all Series 2003 Bonds then Outstanding to be due and payable. Such declaration may be rescinded under circumstances specified in the Trust Agreement. (Sec. 803)

The Holders of a majority in aggregate principal amount of Series 2003 Bonds then Outstanding shall be entitled, by an instrument in writing executed and delivered to the Bond Trustee, to direct the method and place of conducting all remedial proceedings to be taken by the Bond Trustee for the benefit of Holders under the Trust Agreement. (Sec. 807)

No Holder may institute any suit, action or proceeding on any Series 2003 Bond for any remedy under the Trust Agreement unless he previously has given to the Bond Trustee written notice of the Event of Default under the Trust Agreement on account of which suit, action or proceeding is to be instituted, and unless the Holders of not less than a majority in aggregate principal amount of the Series 2003 Bonds then Outstanding have requested the Bond Trustee to act and have furnished the Bond Trustee reasonable security and indemnity as required in the Trust Agreement and the Bond Trustee has refused or neglected to comply with such request; except that the Holders of not less than a majority in aggregate principal amount of the Series 2003 Bonds then Outstanding may institute any such suit, action or proceeding in their own names for the benefit of all Holders. Except as provided in the Trust Agreement, no Holder will have any right in any manner whatsoever to enforce any right thereunder, and any individual rights given to such Holders by law are restricted by the Trust Agreement to the rights and remedies therein granted. (Sec. 808)

Notice to Bondholders

Except as described below, notice of any Event of Default will be mailed to all Holders within 30 days after the Bond Trustee receives notice of the same. The Bond Trustee shall not be subject to any liability to any Holder by reason of its failure to send any such notice.

Except upon the happening of an Event of Default with respect to the payment of the principal of and interest on Series 2003 Bonds when due, the Bond Trustee may withhold notice of any Event of Default to the Holders if in its opinion such withdrawal is in the interest of the Holders. (Sec. 812)

Removal of Bond Trustee

The Bond Trustee may be removed at any time by a written instrument, (i) executed by the Holders of not less than a majority in aggregate principal amount of Series 2003 Bonds then Outstanding and filed with the District, or (ii) so long as no Event of Default has occurred and is continuing, an instrument executed by the District, not less than sixty (60) days before such removal is to take effect. (Sec. 914)

Payment of Bond Trustee's and Bond Registrar's Fees

If the District shall fail to cause any required payments to be made to the Bond Trustee or the Bond Registrar for compensation and expenses, the Bond Trustee or the Bond Registrar may make such payment from any moneys in its possession and will be entitled to a preference therefor over any Series 2003 Bonds Outstanding. (Sec. 905)

Holders of Obligation No. 2

In the event that any request, direction or consent is requested or permitted by the Master Indenture of the registered owners of Obligations issued thereunder, including Obligation No. 2, the Holders of Series 2003 Bonds then Outstanding will be deemed to be registered owners of Obligation No. 2 for the purpose of any such request, direction or consent in the proportion that the aggregate principal amount of Series 2003 Bonds then Outstanding held by each such Holder of Series 2003 Bonds bears to the aggregate principal amount of all Series 2003 Bonds then Outstanding. (Sec. 1003)

Modification of the Trust Agreement

The District and the Bond Trustee may from time to time execute such supplemental trust agreements as shall be consistent with the terms and provisions of the Trust Agreement and, in the opinion of the Bond Trustee, who may rely upon a written Opinion of Counsel, shall not materially and adversely affect the Holders: to cure any ambiguity or formal defect or omission, to correct or supplement any inconsistent provision, to make any other provisions with respect to matters or questions arising under the Trust Agreement, or to modify, alter, amend, add to or rescind in any particular, any of the terms or provisions contained in the Trust Agreement; to grant or confer upon the Bond Trustee for the benefit of the Holders any additional rights, remedies, powers, authority or security that may lawfully be granted to or conferred upon the Holders or the Bond Trustee; to add to the Trust Agreement other conditions, limitations and restrictions thereafter to be observed; to add other covenants and agreements to be observed by the District or to surrender any right or power reserved to or conferred upon the District; to comply with any federal or state securities law; to provide for the issuance of Series 2003 Bonds in bearer form; or to provide for the issuance of Series 2003 Bonds under a book-entry system. (Sec. 1101)

The Trust Agreement may be amended in any particular, with the consent of the Holders of not less than a majority in aggregate principal amount of the Series 2003 Bonds then Outstanding, provided, that nothing contained in the Trust Agreement will permit (a) any extension of the maturity of principal or interest on any Series 2003 Bonds without the consent of the Holders of such Bonds, (b) a reduction in the principal amount of or the rate of interest on any Series 2003 Bonds without the consent of the Holders of such Bonds, (c) the creation of a pledge of receipts and revenues superior to the pledge created under the Trust Agreement without the consent of the Holders of all Series 2003 Bonds Outstanding, (d) a preference or priority of any Series 2003 Bonds over any other Series 2003 Bonds without the consent of the Holders of all Series 2003 Bonds Outstanding, or (e) a reduction in the aggregate principal amount of Series 2003 Bonds required for consent to such supplemental trust agreement without the consent of the Holders of all Series 2003 Bonds Outstanding. (Sec. 1102)

Defeasance

When among other things, the principal and interest due upon all of the Series 2003 Bonds is paid or sufficient money or Defeasance Obligations are held by the Bond Trustee for such purpose, then the right, title and interest of the Bond Trustee in the funds and accounts created in the Trust Agreement will cease and the Bond Trustee will release the Trust Agreement. (Sec. 1201)

No Recourse Against Members, Officers and Employees of the Commission and District

The members, officers and employees of the Commission and District are not personally liable for any costs, losses, damages or liabilities caused or incurred by the Commission or the District in connection with the Trust Agreement, or any Series 2003 Bond or for the payment of any sum or for the performance of any obligation under the Trust Agreement or any Series 2003 Bond. (Sec. 1307)

APPENDIX D

Proposed Opinion of Bond Counsel

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SIDLEY AUSTIN BROWN & WOOD LLP

BEIJING
BRUSSELS
CHICAGO
DALLAS
GENEVA
HONG KONG
LONDON

787 SEVENTH AVENUE
NEW YORK, NEW YORK 10019
TELEPHONE 212 839 5300
FACSIMILE 212 839 5599
www.sidley.com
FOUNDED 1866

LOS ANGELES
NEW YORK
SAN FRANCISCO
SHANGHAI
SINGAPORE
TOKYO
WASHINGTON, D.C.

December 10, 2003

Hampton Roads Sanitation District Commission
Virginia Beach, Virginia

We have examined Chapter 66 of the Acts of Assembly of Virginia of 1960, as amended (the "Act"), and certified copies of the proceedings of the Hampton Roads Sanitation District Commission (the "Commission"), the governing body of Hampton Roads Sanitation District (a political subdivision of the Commonwealth of Virginia and herein sometimes called the "District"), authorizing the execution and delivery of a Trust Agreement, dated as of December 1, 2003 (the "Trust Agreement"), by and between the District and The Bank of New York, New York, New York, as bond trustee (the "Bond Trustee"), and the issuance of

\$55,890,000
HAMPTON ROADS SANITATION DISTRICT
Wastewater Refunding Revenue Bonds
Series 2003

Dated, maturing, and bearing interest,
all as provided in the Trust Agreement.

The above-described bonds (the "Bonds") are secured by, among other things, payments to be made by the District on Obligation No. 2, dated as of its date of delivery ("Obligation No. 2"), issued under the Master Trust Indenture, dated as of December 1, 1993, as amended (the "Master Indenture"), by and between the District and The Bank of New York, New York, New York, as successor master trustee (the "Master Trustee"), as supplemented by Supplemental Indenture for Obligation No. 2, dated as of December 1, 2003 (the "Supplemental Indenture"), by and between the District and the Master Trustee, and delivered to the Bond Trustee as security for the payment of the Bonds. Pursuant to the Master Indenture, as security for the payment of the amounts due on Obligation No. 2 and any additional Obligations issued under the Master Indenture in the future, the District, as the sole Member of the Obligated Group (as defined in the Master Indenture), has pledged its Net Revenues to the Master Trustee, subject to Permitted Liens (as defined in the Master Indenture). Net Revenues of the District consist of all revenues derived by the District from the Wastewater System (as defined in the Master Indenture) except such part thereof as may be required to pay the cost of maintaining, repairing and operating such Wastewater System. To the extent permitted by law, the Master Indenture permits any Person (as defined in the Master Indenture) which is not a Member of the Obligated Group to become a Member of the Obligated Group upon compliance with certain financial and other requirements, including the requirement that such Member pledge to the Master Trustee its Net Revenues if such Member is a Governmental Entity (as defined in the Master Indenture) or its Gross Receipts (as defined in the Master Indenture) if such Member is not a Governmental Entity, in each case subject to Permitted Liens. The Master Indenture also provides that any obligations of a Governmental Member of the Obligated Group shall be limited to its Designated Units (as defined in the Master Indenture). The Wastewater System is currently the only Designated Unit of the District.

Based upon such examination, we are of the opinion that:

1. The Bonds have been duly authorized, executed and issued for the purpose of providing funds, together with other available funds, to (i) refund all of the District's outstanding Wastewater Refunding and Capital Improvement Revenue Bonds, Series 1993 and (ii) pay certain expenses incurred in connection with the issuance of the Bonds.
2. The Trust Agreement has been duly authorized and executed by the District and, assuming due authorization and execution by the Bond Trustee, is a valid, binding and enforceable obligation of the District in accordance with its terms.
3. The Bonds are valid and binding special obligations of the District payable solely from moneys paid by the Members of the Obligated Group on Obligation No. 2 and the revenues and other funds pledged as security therefor under the Trust Agreement and as security for Obligation No. 2 under the Master Indenture.
4. The Bonds do not constitute a debt of the Commonwealth of Virginia or of any county, city, town or political subdivision thereof, or a pledge of the faith and credit of the Commonwealth of Virginia or of any county, city, town or political subdivision thereof. The issuance of the Bonds does not directly or indirectly or contingently obligate the Commonwealth of Virginia or any county, city, town or political subdivision thereof to levy or to pledge any form of taxation whatever therefor.
5. The Master Indenture has been duly authorized and executed by the District and, assuming due authorization and execution by the Master Trustee, is a valid, binding and enforceable agreement in accordance with its terms.
6. Obligation No. 2 is a valid and binding special obligation of the District payable solely from its Net Revenues.
7. The Supplemental Indenture has been duly authorized and executed by the District and, assuming due authorization and execution by the Master Trustee, is a valid and binding agreement enforceable in accordance with its terms.
8. Except as provided in the following sentences and assuming compliance by the District with its covenant to comply with the requirements of the Internal Revenue Code of 1986, as amended (the "Code"), interest on the Bonds is not includable in the gross income of the owners of the Bonds for purposes of federal income taxation under existing law. Interest on the Bonds will be includable in the gross income of the owners thereof retroactive to the date of issue of the Bonds in the event of a failure by the District to comply with applicable requirements of the Code and its covenant regarding use, expenditure and investment of proceeds of the Bonds and the timely payment of certain investment earnings to the United States Treasury. The opinion with respect to the exclusion from gross income of the interest on the Bonds for federal income tax purposes may not be relied upon to the extent that such exclusion is adversely affected as a result of any action taken in reliance upon the opinion of counsel other than this firm delivered subsequent to the issuance of the Bonds.

Interest on the Bonds is not a specific preference item for purposes of the federal individual or corporate alternative minimum tax. The Code contains other provisions that could result in tax consequences, as to which we render no opinion, as a result of (i) ownership of the Bonds or (ii) the inclusion in certain computations (including without limitation those related to the corporate alternative minimum tax) of interest that is excluded from gross income. Interest on the Bonds will be included in the calculation of a corporation's federal alternative minimum tax liability.
9. As provided by the Act, the Bonds, their transfer and the income therefrom, including any profit made on the sale thereof, shall be free and exempt from taxation by the Commonwealth of Virginia and any political subdivision thereof.

The enforceability of the Trust Agreement, the Master Indenture and the Supplemental Indenture and the obligations of the aforementioned parties with respect to such documents described above are subject to bankruptcy, insolvency, fraudulent conveyance, reorganization and other laws affecting creditors' rights generally. To the extent that the remedies under the Trust Agreement, the Master Indenture and the Supplemental Indenture require enforcement by a court of equity, the enforceability thereof may be limited by such principles of equity as the court having jurisdiction may impose.

Respectfully submitted,

[To be signed "Sidley Austin Brown & Wood LLP"]

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APPENDIX E

Form of Continuing Disclosure Agreement

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CONTINUING DISCLOSURE AGREEMENT

This Continuing Disclosure Agreement (the "Disclosure Agreement") is executed and delivered by Hampton Roads Sanitation District (the "District") in connection with the issuance by the District of \$55,890,000 aggregate principal amount of its Wastewater Refunding Revenue Bonds, Series 2003 (the "Bonds" or "2003 Bonds") pursuant to the provisions of a Trust Agreement, dated as of December 1, 2003 (the "Trust Agreement"), by and between the District and The Bank of New York, as bond trustee. The proceeds of the 2003 Bonds are being used by the District to refund certain bonds previously issued by the District. The District hereby covenants and agrees as follows:

SECTION 1. Purpose of the Disclosure Agreement. This Disclosure Agreement is being executed and delivered by the District for the benefit of the holders of the 2003 Bonds and in order to assist the Participating Underwriters (defined below) in complying with the Rule (defined below). The District acknowledges that it is undertaking primary responsibility for any reports, notices or disclosures that may be required under this Disclosure Agreement.

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

"Annual Report" shall mean any Annual Report provided by the District pursuant to, and as described in, Sections 3 and 4 of this Disclosure Agreement.

"Dissemination Agent" shall mean the District, acting in its capacity as Dissemination Agent hereunder, or any successor Dissemination Agent designated in writing by the District and which has filed with the District a written acceptance of such designation.

"Filing Date" shall have the meaning given to such term in Section 3(a) hereof.

"Fiscal Year" shall mean the twelve-month period at the end of which financial position and results of operations are determined. Currently, the District's Fiscal Year begins July 1 and continues through June 30 of the next calendar year.

"Holder" or "holder" shall mean, for purposes of this Disclosure Agreement, any person who is a record owner or beneficial owner of a 2003 Bond.

"Listed Events" shall mean any of the events listed in subsection (b)(5)(i)(C) of the Rule, which are as follows:

- 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 2003 Bonds;
- 7) modifications to rights of holders;
- 8) bond calls;

- 9) defeasances;
- 10) release, substitution, or sale of property securing repayment of the 2003 Bonds; and
- 11) rating changes.

"National Repository" shall mean any Nationally Recognized Municipal Securities Information Repository for purposes of the Rule.

"Participating Underwriter" shall mean any of the original underwriters of the 2003 Bonds required to comply with the Rule in connection with the offering of such Bonds.

"Repository" shall mean each National Repository and each State Repository.

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

"State Repository" shall mean any public or private depository or entity designated by the State as a state depository for the purpose of the Rule. As of the date of this Agreement, there is no State Repository.

SECTION 3. Provision of Annual Reports.

A. The District shall, or shall cause the Dissemination Agent to, provide to each Repository an Annual Report which is consistent with the requirements of Section 4 of this Disclosure Agreement. Such Annual Report shall be filed on a date (the "Filing Date") that is not later than December 31 after the end of any Fiscal Year (commencing with its Fiscal Year ending June 30, 2004). Not later than ten (10) days prior to the Filing Date, the District shall provide the Annual Report to the Dissemination Agent (if applicable). In such case, the Annual Report (i) may be submitted as a single document or as separate documents comprising a package, (ii) may cross-reference other information as provided in Section 4 of this Disclosure Agreement and (iii) shall include the District's audited financial statements or, if audited financial statements are not available, such unaudited financial statements as may be required by the Rule. In any event, audited financial statements of the District must be submitted, if and when available, together with or separately from the Annual Report.

B. The annual financial statements of the District shall be prepared on the basis of generally accepted accounting principles and will be audited. Copies of the audited annual financial statements, which may be filed separately from the Annual Report, will be filed with the Repositories when they become publicly available.

C. If the District fails to provide an Annual Report to the Repositories by the date required in subsection (a) hereto or to file its audited annual financial statements with the Repositories when they become publicly available, the District shall send a notice to the Municipal Securities Rulemaking Board and any State Repository in substantially the form attached hereto as Exhibit B.

SECTION 4. Content of Annual Reports. Except as otherwise agreed, any Annual Report required to be filed hereunder shall contain or incorporate by reference, at a minimum, annual financial information relating to the District, including operating data, updating such information relating to the District as described in Exhibit A, all with a view toward assisting the Participating Underwriters in complying with the Rule.

Any or all of such information may be incorporated by reference from other documents, including official statements of securities issues with respect to which the District is an "obligated person" (within the meaning of the Rule), which have been filed with each of the Repositories or the Securities and Exchange Commission. If the document incorporated by reference is a final official statement, it must be available from the Municipal Securities Rulemaking Board. The District shall clearly identify each such other document so incorporated by reference.

SECTION 5. Reporting of Listed Events. The District will provide in a timely manner to the Municipal Securities Rulemaking Board and to each State Repository, if any, notice of any of the Listed Events, if material.

SECTION 6. Termination of Reporting Obligation. The District's obligations under this Disclosure Agreement shall terminate upon the earlier to occur of the legal defeasance or final retirement of all the 2003 Bonds.

SECTION 7. Dissemination Agent. The District may, from time to time, appoint or engage a Dissemination Agent to assist it in carrying out its obligations under this Disclosure Agreement and may discharge any such Agent, with or without appointing a successor Dissemination Agent. If at any time there is not any other designated Dissemination Agent, the District shall be the Dissemination Agent.

SECTION 8. Amendment. Notwithstanding any other provision of this Disclosure Agreement, the District may amend this Disclosure Agreement, if such amendment is supported by an opinion of independent counsel with expertise in federal securities laws, to the effect that such amendment is permitted or required by the Rule.

SECTION 9. Additional Information. Nothing in this Disclosure Agreement shall be deemed to prevent the District from disseminating any other information, using the means of dissemination set forth in this Disclosure Agreement or any other means of communication, or including any other information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is required by this Disclosure Agreement. If the District chooses to include any information in any Annual Report or notice of occurrence of a Listed Event, in addition to that which is specifically required by this Disclosure Agreement, the District shall have no obligation under this Agreement to update such information or include it in any future Annual Report or notice of occurrence of a Listed Event.

SECTION 10. Default. Any person referred to in Section 11 (other than the District) may take such action as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the District to file its Annual Report or to give notice of a Listed Event. The holders of not less than a majority in aggregate principal amount of 2003 Bonds Outstanding may take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to challenge the adequacy of any information provided pursuant to this Disclosure Agreement, or to enforce any other obligation of the District hereunder. A default under this Disclosure Agreement shall not be deemed an event of default under the Trust Agreement or the 2003 Bonds, and the sole remedy under this Disclosure Agreement in the event of any failure of the District to comply herewith shall be an action to compel performance. Nothing in this provision shall be deemed to restrict the rights or remedies of any holder pursuant to the Securities Exchange Act of 1934, the rules and regulations promulgated thereunder, or other applicable laws.

SECTION 11. Beneficiaries. This Disclosure Agreement shall inure solely to the benefit of the District, the Participating Underwriters and the holders from time to time of the 2003 Bonds, and shall create no rights in any other person or entity.

Date: _____, 2003

HAMPTON ROADS SANITATION DISTRICT

By: _____
Director of Finance and Administration

**CONTENT OF ANNUAL REPORT
HAMPTON ROADS SANITATION DISTRICT**

(a) **Financial Information.** Updated information including summary financial results, treatment charge collection rate, revenue collections from the District's largest customers, and a five-year comparison of revenues, expenses, debt service and debt service coverage ratios.

(b) **Debt Information.** Updated information including the debt service requirements of long-term indebtedness.

(c) **Operating Data.** Updated operating data including wastewater flows to the Wastewater System and its major treatment plants, the treatment capacities of its major treatment plants, total billed wastewater flows, and changes in rates and charges.

In general, the foregoing will include information as of the end of the most recent fiscal year or as of the most recent practicable date. Where information for the fiscal year just ended is provided, it may be preliminary and unaudited. Where information has historically been provided for more than a single period, comparable information will in general be provided for the same number of periods where valid and available. Where comparative demographic or economic information for the District and the United States as a whole is contemporaneously available and, in the judgment of the District, informative, such information may be included. Where, in the judgment of the District, an accompanying narrative is required to make data presented not misleading, such narrative will be provided.

EXHIBIT B

**NOTICE OF FAILURE TO FILE ANNUAL REPORT
[AUDITED ANNUAL FINANCIAL STATEMENTS]**

**Re: HAMPTON ROADS SANITATION DISTRICT
WASTEWATER REFUNDING REVENUE BONDS,
SERIES 2003**

CUSIP NOS.: _____ - _____

Dated: _____, 2003

NOTICE IS HEREBY GIVEN that Hampton Roads Sanitation District has not provided an Annual Report [Audited Annual Financial Statements] as required by Section 3 of the Continuing Disclosure Agreement, which was entered into in connection with the above-named bonds, the proceeds of which were used to refund certain outstanding bonds of the District. [The District anticipates that the Annual Report [Audited Annual Financial Statements] will be filed by _____.]

Dated: _____

HAMPTON ROADS SANITATION DISTRICT

By _____

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HAMPTON ROADS SANITATION DISTRICT

A Political Subdivision of the Commonwealth of Virginia

Major facilities include the following:

- | | |
|------------------------------------|---------------------------------------|
| 1. Atlantic, Virginia Beach | 8. Williamsburg, James City County |
| 2. Army Base, Norfolk | 9. York River, York County |
| 3. Chesapeake-Elizabeth, Va. Beach | 10. Mathews, Mathews County |
| 4. Virginia Initiative, Norfolk | 11. West Point, King William County |
| 5. Nansemond, Suffolk | 12. Urbanna, Middlesex County |
| 6. Boat Harbor, Newport News | 13. King William, King William County |
| 7. James River, Newport News | |

Serving the Cities of
Chesapeake, Hampton,
Newport News, Norfolk,
Poquoson, Portsmouth,
Suffolk, Virginia Beach,
and Williamsburg, and the
Counties of Gloucester,
Isle of Wight, James City,
King William, Mathews,
Middlesex and York

