



TETRA TECH, INC.

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LETTER OF TRANSMITTAL

OCT 2 2006

PUBLIC SERVICE COMMISSION

DATE: September 29, 2006

TO: Ms. Beth O'Donnell, Executive Director
Public Service Commission
211 Sower Boulevard
Frankfort, Kentucky 40602

RE: Case No. 2006-00191
Henry County Water District No. 2
Responses to Interrogatories and Requests for Production of Documents
Ordered August 11, 2006

WE ARE SENDING YOU THE FOLLOWING: [X] Attached [] Under separate cover via _____

- [] Shop Drawings [] Prints [] Plans [] Specifications [] Reports [] Samples
[] Copy of Letter [] Change Order [X] Other

Table with 2 columns: Copies, Description. Row 1: 1, Original of Responses. Row 2: 8, Copies of Responses.

THESE ARE TRANSMITTED:

- [] For Approval [] Approved as submitted [] Resubmit ___ copies for approval
[] For your use [] Approved as noted [] Submit ___ copies for distribution
[X] As requested [] Returned for correction [] Return ___ corrected prints
[] For review and comment [] Rejected [] Other

COMMENTS:

As directed, we submit herewith one original and eight copies of the above referenced document in response to Order issued August 11, 2006.

Signed [Signature]
Thomas Green

Copies to:
Honorable David Spenard, Office of the Attorney General
Merle Brewer, Chairman, HCWD2
Honorable D. Berry Baxter
Central Files - 03299

COMMONWEALTH OF KENTUCKY

RECEIVED

BEFORE THE PUBLIC SERVICE COMMISSION OCT 2 2006

PUBLIC SERVICE
COMMISSION

In the Matter of:

EXAMINATION OF THE OPERATION AND)
REASONABLENESS OF THE OFFSETTING)
IMPROVEMENT CHARGE OF HENRY COUNTY)
WATER DISTRICT NO. 2)

CASE NO. 2006-00191

**RESPONSES TO INTERROGATORIES AND REQUESTS FOR
PRODUCTION OF DOCUMENTS**

As Ordered August 11, 2006

HENRY COUNTY WATER DISTRICT NO. 2

RESPONDENT CERTIFICATIONS

PSC Interrogatories – Case 2006-00191

I certify that, on behalf of Henry County Water District No. 2, I have prepared or supervised the preparation of the responses to Items 1 through 8, 11, 13, 15, 16, 17, 21, 22, 23, 25, 29, and 30, and that these responses are true and accurate to the best of my knowledge, information, and belief formed after a reasonable inquiry.

Tom Green
Thomas Green
Tetra Tech, Inc.

Sept 29 '06
date

I certify that, on behalf of Henry County Water District No. 2, I have prepared or supervised the preparation of the responses to Items 9, 10, 12, 18, 19, 20, 24, 31, and 32, and that these responses are true and accurate to the best of my knowledge, information, and belief formed after a reasonable inquiry.

James Simpson
James Simpson
Chief Operating Officer
HCWD2

date 9-29-06

I certify that, on behalf of Henry County Water District No. 2, I have prepared or supervised the preparation of the responses to Items 14, 26, 27, and 28, and that these responses are true and accurate to the best of my knowledge, information, and belief formed after a reasonable inquiry.

Daniel Shoemaker
Daniel Shoemaker
Tetra Tech, Inc.

date 9/29/06

**1. Refer to Henry District's Response to the Commission's Order of May 22, 2006, Appendix C.
For each project listed,**

a. Describe the need for project.

All projects are for the purpose of accommodating higher flowrates and future growth.

US 421 West - 6" line cannot accommodate increasing demands and flowrates into Pleasureville and maintain minimum pressures at higher elevations in the vicinity

KY 153 - 6" line inadequate to serve growth in corridor from Sligo to I-71 interchange and south to Jericho

KY 1861 & Smithfield - 3" lines have limited capacity to serve new subdivisions

Giltner Jackson - (installed by HCWD 2005) reinforces hydraulics in growing Giltner vicinity and allows additional future service along KY 22 west of Eminence

KY 146 - 3" line cannot accommodate growth along corridor west of Jackson Road

KY 193 - 3" line has limited capacity to serve development and maintain acceptable pressures higher elevations

KY 202- 3" line has limited capacity to serve development and maintain acceptable pressures higher elevations

Bunk-Ellis - Reinforces hydraulics by providing alternate source of flow.

Martini-Webb - 3" line limits capacity of system to accommodate growth in residential areas and along US 421

KY 1359 - Reinforces hydraulics by providing alternate source of flow

KY 1360 - Allows growth by upsizing 3" line north of Bullit Road

Dawkins - Closes gaps and provides alternate sources of flow, reinforces hydraulics

Radcliff - Closes gap and reinforces hydraulics by providing alternate source of flow

b. Identify the system deficiencies or problems that require the construction of the proposed project.

KY 1359, Bunk-Ellis, Dawkins, Radcliff: hydraulically inefficient gaps in distribution network; projects will close loops

All other projects: potentially inadequate diameter lines

c. Identify the area in which the project will be constructed.

Each project is named for the nearest highway, town, or road. Project locations are indicated on the HCWD2 system map provided in response to Item 2 below.

d. State how the project is expected to improve the system.

All projects: more efficiently accommodate higher flowrates while sustaining acceptable future levels of pressure.

e. State the year in which Henry District currently expects construction to commence.

Phase 1 of the KY 153 project, together with the US 421 project, commenced construction on September 5, 2006, and these improvements should be in service by January 2007.

The year in which each remaining project will be constructed depends on funding considerations and ongoing growth patterns. In response to the May 22, 2006 Order, Item 7(b), the OIC-eligible projects are listed in their current priority, however as we stated in that response:

“Changing conditions can compel the reordering of project priorities. For example, when numerous landowners decide to develop subdivisions in a given area, the project which reinforces that area hydraulically can quickly rise in priority. Also, funding considerations can cause high-cost projects to be delayed, despite their high priority ranking.”

Keeping the above considerations in mind, it is our goal to install approximately \$250,000 worth of hydraulic improvements as an annual average, so that we estimate the currently listed OIC-eligible projects would take eight to ten years. If the anticipated order of construction is followed, the work would occur between 2007 and 2015-2017, on pace with available funds.

f. State the expected source of funding.

All projects will be funded by the most advantageous possible combination of OIC revenues, general revenues, and grants. As we stated in our response to a similar question in May 22, 2006 Item 7(a):

“The source of funding will vary with the availability of OIC proceeds, general revenues, loans, grants, etc. The long-term OIC plan excludes all categories of projects other than hydraulic improvements, but this does not mean that those OIC-eligible projects cannot be constructed with other funding sources.”

2. Provide a system map showing all of Henry District's distribution facilities. This map shall, at a minimum, show all master meters, pumping stations, storage tanks, water transmission mains and water distribution mains. The size of all mains shall be clearly indicated on this map.

Please see Appendix A.

3. Describe the methodology that Henry District presently uses to determine if the construction of a system line improvement benefits existing customers.

In our response to Item 3 in the May 22, 2006 Order we state:

“We do not offer grades of service. Water rates are uniform regardless of whether a customer receives minimum daily pressure of 80, 60, or 40 psi, and it can reasonably be concluded that higher pressure is not considered objectively “better” from a regulatory standpoint. HCWD2 does not install fire hydrants or certify flowrates to insurers, which means that a larger, newly installed 6” line provides no additional benefit to existing customers in regard to fire protection. And water quality is not improved due to the larger diameter of new lines; smaller lines provide faster volume turnover and lower travel times.

There is no additional benefit or detriment to existing customers whose pressures may rise or fall within the required range. They, like the new customers, receive the one and entire benefit the District can offer, service in compliance with all regulatory parameters.”

In light of this response, we are surprised the Commission has once again inquired about benefits to existing customers without enumerating and describing those benefits. Also, the Commission does not address whether such “benefits” in the case of *some* existing customers are not counterbalanced by similar “detriments” in the case of *other* existing customers.

It is our position that even where pressures are higher for existing customers, it is not a benefit. Our District, like all other districts, is required to provide service within an acceptable range of pressures. If, within those regulatory parameters, higher pressure is considered by the PSC to be *better* service, it would be reasonable for Kentucky customers in valleys to pay higher water rates than customers on hills.

Hydraulic improvement projects are not undertaken by our District to provide additional “benefits” to anyone, new customers or old. They are undertaken only in order to provide service itself. The service that proposed customers *will* receive is the same service that existing customers will *continue* to receive.

4 Refer to Letter of Tom Green to Thomas Dorman (April 21, 2004).

a. Explain how Henry District's certification to the Henry County Planning and Zoning Commission of the availability of water service to a lot "creates hydraulic impact on the system."

In our letter to Mr. Dorman, we are referring to the hydraulic impact which, like actual connections, either necessitates the construction of hydraulic improvements to the system, or brings that necessity incrementally closer. In this sense, a certification of service is identical in impact to service itself.

Assume a person has \$800 in his bank account, and writes a check for \$500. Because that check has yet to clear the bank, his official balance is still \$800. Can he therefore write a second check for \$500? Or would he first need to deposit at least \$200 into his account?

Assume HCWD2 certifies to a landowner or developer that water service is available for Green Acres Subdivision. The certified plat is recorded, and after a delay of several years due to the ups and downs of the real estate cycle (or the developer's personal finances), he builds and sells homes. If the hydraulic capacity of the system has not been held in reserve, if HCWD2 has instead permitted other development in the vicinity which has consumed system capacity and reduced minimum pressures to near 30 psi, then when new homeowners from Green Acres request their meter connections, they will have to wait until the District has the time and resources to install the necessary line upsizes. This would clearly be unfair to these homeowners, who purchased property for which water service had already been certified available on their subdivision plat of record.

The Planning Commission requires unconditional plat certification that service *is* available, not that service will be provided contingent upon future improvements. And there is no expiration date on plat certifications. So when the Henry District certifies the availability of water service, we permanently commit that specific capacity, and cannot then reassign the same capacity to other subsequent customers. We must refuse service (and make hydraulic improvements) when our actual demand, plus our certifications of service, bring pressures to their regulatory minimum. We maintain a hydraulic model which allows us to "balance our checkbook" by taking these commitments into consideration. We would consider it unfair and irresponsible to do otherwise.

b. Explain why for single tracts of agricultural land it is not more reasonable to require payment of the Offsetting Improvement Charge when a service connection is made instead of when the water district certifies the availability of water service.

We certify plats to the Planning Commission in accordance with their requirements. We have unsuccessfully attempted to make clear in our previous responses that "agricultural" tracts (as distinct from residential properties) do not *exist* in terms of plat certifications to the Planning Commission.

Certification of *residential* service, at minimum, is required by the Planning Commission on all new tracts, regardless of the owner's stated land use intentions. No agricultural land use category in Henry County precludes an existing or future residence. This is explained in our April 21, 2004 letter to the PSC included in Appendix H, as referenced by Item 23(b) of our responses to the May 22, 2006 Order.

It is preferable to treat all classes of customers as equally as is possible. Even if the Planning Commission would accept customized HCWD2 certifications which made exceptions for those who state their tract is only for non-residential agricultural use, this would logically require us to make a similar exception for those who state, for example, that the creation of new lots is only so that the land can be conveniently willed to a number of heirs at some point in the far distant future. Or that the land is only being subdivided to avoid the limitations of an anticipated (rumored) increase in county requirements for minimum lot frontage. If the stated intentions of a subdivider could exempt him from the payment of an impact fee, we would quickly amass a sizable catalogue of such statements.

The more general question of whether to collect the OIC at plat certification versus time of service was discussed during Case 2001-00393. In its approval of the OIC, the Commission made no further mention of this issue, and expressed no concerns about the reasonableness of our policy in this regard. AWWA guidelines caution that collecting SDCs at platting may make it "difficult to determine the number of service units the development will demand." However, HCWD2 has calculated its charge on a per lot basis, so that this difficulty is not an issue. The OIC also includes a provision for a fee refund if the number of lots is subsequently changed.

In terms of our need and responsibility to make hydraulic improvements, certification itself generates impact, as we have explained in Item 4(a). Certification is therefore the appropriate time to collect the OIC.

c. State whether it is Henry District's position that it may refuse water service to an applicant where actual usage, combined with certified commitments of usage, would result in pressures below state regulations even if the applicant's connection would not result in actual pressures below state regulations upon or after his connection.

It is not simply our position that we may refuse service; it is our position that we, or any other responsible water district, must. We would fully expect the PSC to require this level of integrity in hydraulic accounting, just as it does in financial accounting. A certification of service is not an irrelevant prelude to a first come, first served free-for-all, and there is no expiration date on a plat certification. The Planning Commission requires unconditional certification that service *is* available, not that service will be provided contingent upon future improvements. It is only reasonable that we either be obligated to honor that commitment, or that we refuse to make it in the first place.

5. State the number of times since January 1, 1996, that the connection of a customer resulted in system pressure falling below 30 pounds per square inch in either Henry District's transmission or distribution system. For each incident, state the date of the connection, the type of customer added, the amount of demand from the new customer, the size of connection, the location of the connection, the size of water distribution main to which the connection was made, the actions taken to correct the low pressure problem, and the cost of the corrective actions.

Hydraulic modeling and field pressure testing enable us to monitor our distribution system to the extent that we do *not* connect services which will result in pressures below 30 psi. Several times we have delayed the approval of such new services until larger lines could be installed. The number of times since 1996 that we have reduced pressures below 30 psi by connecting new customers is zero. The number of times we have reduced pressures in our hydraulic model below 30 psi by making irresponsible *certifications* of service ("writing bad checks") is also zero.

6. Identify all other water utilities that impose a charge similar to Henry District's "Offsetting Improvement Charge." For each utility identified, provide the rate schedule in which the charge is incorporated.

All unregulated municipal water utilities in Kentucky can, at their discretion, either require developers to upgrade the water system infrastructure in order to offset the hydraulic impact of their development, or levy charges for those purposes. But, as the PSC stated in its July 25, 2002 Order, the Henry District's charge "presents a case of first impression for the Commission." HCWD2 knows of no other Kentucky utility with a PSC-approved charge similar to ours, but here we must defer to the Commission, who would naturally have a more complete knowledge of its own actions.

If there are no other similar charges, that fact could be interpreted to mean that the HCWD2 tariff is so unusual as to be considered ill-conceived or arbitrary. But our tariff could only be judged atypical if the Commission had also approved numerous other, more conventional SDCs. However, with the exception of the three-year approval of the Henry District's OIC, there have been, to our knowledge, no system development charges approved by the PSC.

The history of our charge and the parallel examination of SDCs by the Commission are noteworthy.

In 1999, Henry District sought guidance from the PSC in crafting a charge by which development would offset its hydraulic impact on the distribution system. After conversations with PSC staff, several visits to Frankfort, and extensive tariff research, the only example we could find was a North Shelby charge which required a developer proposing lots along an existing line to pay half the cost of a 6" line equivalent in length to the development's road frontage. From an engineering and hydraulic perspective this methodology made no sense to us, and so, rather than take the easy route of simply submitting a HCWD2 tariff which was cut and pasted from North Shelby's, the Henry District decided to take on the task (and the considerable expense) of creating an approach which not only made good sense hydraulically, but which was very reasonable in its treatment of new and existing customers.

Discussions of our proposed methodology with PSC staff were positive. We were told that our approach seemed reasonable, but that the Commission was conducting a study (Administrative Case 375) to investigate system development charges, and it was therefore suggested we delay our tariff submittal until that case was completed. We followed this suggestion and awaited the outcome of the PSC's investigation. In Administrative Case 375 the Commission researched the need for SDCs:

"The Commission directed all public utilities in Kentucky and all municipal utilities that provide wholesale water service to a public utility to provide information on their operations and need for additional sources of funding. Over 130 responses to the Commission's request were received. These responses indicated a need on the part of 113 respondents for additional funding and rate mechanisms to address increased development and customer growth within their systems."

Among its conclusions, the Commission stated:

"Because of the geographic and demographic diversity of the state and its water utilities, the use of rigid and inflexible standards for SDCs is not in the public interest. The Commission is of the opinion that public and municipal utilities should be afforded sufficient latitude to craft SDCs to meet their unique needs and conditions."

The Commission did not merely permit flexibility; the Commission *encouraged* flexibility by asserting that rigid guidelines were contrary to the public interest. This policy of flexibility regarding alternative SDC methodologies was very promising to us, and when PSC staff told us it was the appropriate time to submit our new tariff, we did so. The review took nine months, and included a meeting in Frankfort and preparation of responses to 23 Interrogatories. Case 2001-00393 resulted in the first approval of an engineering-based impact fee in Kentucky, and, because it was the first, we believe the Commission to have been particularly thorough in examining its reasonableness. During the three-year trial period of the OIC, we have complied with the terms of the tariff by submitting our annual and biennial accountings, and we have maintained our records in order to be well-prepared for the required “full review of the operation of the program...”

In Case 2001-00393, the July, 25, 2002 Order approving our tariff stated:

“We conclude that the Offsetting Improvement Charge appears to be in the public interest in that it will benefit both Henry District and its customers. However, because the proposed charge presents a case of first impression for the Commission, we believe that it should be established for an initial 3-year period only, after which we will conduct a full review of the operation of the program and determine whether it should be renewed.” (emphasis added)

Case 2006-00191, however, begins by inaccurately paraphrasing Case 2001-00393. Referring to the initial case, the 2006 Order incorrectly states:

“Noting that the proposed charge presented a case of first impression, the Commission directed that the operation and reasonableness of the charge be reexamined after three years to determine if it should continue.” (emphasis added)

This modification of the intent of the 2002 Order has had the effect of requiring HCWD2, after taking on the considerable initial expense of developing and obtaining PSC approval of a sensible and equitable impact fee, to defend all over again the rationale which earned PSC approval in 2002, and by which the Commission has permitted HCWD2 to charge prospective customers over \$270,000.

We discuss this issue further in our response to Items 11 and 16.

7. Refer to Henry District's Response to the Commission's Order of May 22, 2006, Item 3. State whether Henry District's OIC is intended to cover "only the cost of installing larger [water distribution] lines."

The OIC would also pay to construct lines which close loops and enhance pressures, which is sometimes a more cost-effective way to provide better pressures than upsizing a line. The OIC does not address water treatment, pumps, or storage tanks. The tariff itself states: "Offsetting improvement charges shall be placed in an escrow account and shall be used only for water line projects which improve hydraulic conditions in the distribution system."

8. Refer to Case No. 2001-00393,' Henry District's Response to Commission Staff's Interrogatories and Requests for Production of Documents, Item 5. Henry District states that "[t]he Offsetting Improvement Charge (OIC) is necessary to avoid imposing substantial and ongoing rate increases on existing HCWD2 customers in order to accommodate the hydraulic demands of development." State if the Offsetting Improvement Charge is necessary if substantial and ongoing rate increases do not materialize or can be avoided through other mechanisms.

Our policy does not stipulate the minimum level of growth which necessitates the OIC. A growth rate threshold was not required, or even suggested, by the PSC in its Case 2001-00393 approval of our tariff. Neither the Administrative Case 375 SDC guidelines nor the consequent 807 KAR 5:090 stipulate a minimum growth rate. The preface to our responses to the May 22, 2006 Order states:

“We understand the underlying principle of a system development charge to be that of fairness in allocating to development the reasonably determined cost of improvements necessitated by growth, and that this principle should take precedence over the procedural expediency of incorporating such costs into general rates. It is our understanding that the need for a system development charge is to be dictated by this principle of fairness, a principle which is neither augmented nor diminished by growth rate.”

We can think of no “other mechanism” which so directly and reasonably assigns to development its fair share of the costs of infrastructure improvements. Ours is a cost-based charge, unlike the ten year estimates and projections of the standard incremental SDC methodology by which development is required to pay what the water district *estimates* improvements may cost.

Our response to Item 14 of the May 22, 2006 Order discusses the “two unequal classes of water districts” which would result from a growth rate threshold requirement for an SDC. And in our response to Item 20 we state that growth rate can be:

“...an unreliable indicator of the need for hydraulic improvements. A system which is nearing capacity in several developing areas would need to invest much more in new infrastructure to accommodate moderate growth than would a system with excess capacity experiencing a higher growth rate. And even a system with no net growth could be faced with upsizing expenses if population shifted from older areas in the core of the system to new subdivisions on its periphery.

The Henry District believes that requiring development to pay its fair share is a principle which does not become more or less reasonable depending on the annual number of new lots served. No utility customer could successfully argue that because his bill is so low this month, he not obligated to pay it. Such would be the logic of declaring that an SDC is not justified by a low growth rate.”

Our response to Item 22 of the May 22, 2006 Order states:

“However it is important to reiterate that the Henry District’s Offsetting Improvement Charge does not in any way depend upon our predictions of growth in order to calculate our development charge...”

A ten-year capital improvement plan relies on accurately predicting a specific growth rate. But the HCWD2 fee is cost-based, self-adjusting, and reasonable in addressing growth at any rate.

9. State if Henry District currently applies the policies set forth in its "Water Main Extension to Existing Houses & Refund Policy" to extensions to existing houses.

Yes.

10. State for each of the previous 5 years the amount that Henry District refunded to real estate subdivision developers pursuant to Administrative Regulation 807 KAR 5:066, Section 11 (3).

807 KAR 5:066, Section 11 (3):

“An applicant desiring an extension to a proposed real estate subdivision may be required to pay the entire cost of the extension. Each year, for a refund period of not less than ten (10) years, the utility shall refund to the applicant who paid for the extension a sum equal to the cost of fifty (50) feet of the extension installed for each new customer connected during the year whose service line is directly connected to the extension installed by the developer, and not to extensions or laterals therefrom. Total amount refunded shall not exceed the amount paid to the utility. No refund shall be made after the refund period ends.”

During this period we have not had a circumstance in which a developer built a new line extension in order to reach his subdivision.

11. State why revisions to Henry District's current water main extension policy to permit Henry District to assess to real estate subdivision developers the cost of constructing replacement or supplemental water mains needed as a result of the proposed extension is not a more fair and equitable means of assigning costs related to water main extensions rather than the assessment of an Offsetting Improvement Charge.

In its July 25, 2002 Order the Commission stated that it was in "general agreement with the rationale supporting the charge" with the exception of several specific concerns which were subsequently addressed by a tariff revision made effective August 24, 2003. Nevertheless, Item 11 again calls into question the underlying rationale of the Offsetting Improvement Charge.

A second review of the reasonableness of the charge is not what the PSC directed in 2002, but the Henry District clearly understands that the Commission is empowered to open an investigation of the reasonableness of any rate, at any time, for any reason. We also understand that we can either respond fully and directly, or that we can abandon both our efforts and the considerable investment our District's customers have already made in this approval process. We therefore choose to respond.

In a general sense, the Henry District's OIC *is* a revision to our water main extension policy. It expands the applicability of that policy so as to include improvements to existing distribution facilities. Instead of extending the length of a line, the OIC "extension" increases the size of its diameter. Both types of extensions can be needed to serve additional customers. The OIC calculates the systemwide average cost of these hydraulic "extensions" on a per lot basis.

If the Commission proposes a revision to the "current water main extension policy" which would require individual offsetting improvement projects for each proposed subdivision and each newly created tract, this is an approach which would be inefficient, and on a systemwide basis, inequitable.

Developers, on average, would pay more per lot because of the costliness of individual designs, regulatory approvals, mobilization, construction, inspection, testing, etc. This approach would keep our system under a constant and disruptive construction schedule of concurrent minor projects. Each new proposed development would be contingent upon each minor improvement, causing considerable additional delays to each developer.

In hydraulically marginal areas, a policy which required each developer to restore his specific impact would serve only to maintain that marginal status quo, so that the vicinity would remain vulnerable to low pressures in extreme usage periods such as droughts.

The systemwide OIC methodology efficiently pools resources. This permits the financing of larger projects providing excess capacity which then becomes available to future developers, who repay their impact via the OIC. Pooling resources and constructing "economy of scale" projects where they are most needed and most effective makes better sense for the developers and for the District. There is a uniform charge per lot, rather than the extreme variations in cost which would accompany individualized offsets, as we discussed in our response to Item 3 in the May 22, 2006 Order.

However, if the Commission intends the phrase "needed as a result of the proposed extension" to suggest that improvements would only be "needed" if pressures would fall below 30 psi, then we are back to the situation in which many developers would freely consume hydraulic capacity until pressures become marginal, while developers in other areas of the system would be required to make (and, in effect, *discouraged* from making) expensive offsetting improvements.

Over time this two-tiered process would only serve to diminish the system's strengths while locking in its weaknesses. The OIC levels out the playing field and charges all developers the same systemwide average amount, and thereby achieves a more reasonable result. The fairness of this methodology has been discussed at length in several previous responses. Our charge is cost-based and uniform throughout the system, and is therefore very similar to water rates themselves.

12. Provide a copy of the ordinances for the bond issuances that Henry District executed in 1998 and 2001.

Please see Appendix B for the 1998 ordinance and Appendix C for the 2001 ordinance.

13. State how Henry District intends to finance main replacements necessary to serve customers in areas certified or receiving water service prior to July 25, 2002.

It is important to understand that we do not certify areas, roads, vicinities, or lines; we certify only specific developments, as we first explained in our response to Interrogatory 7 in Case 2001-00393. Any newly created lot, even on the oldest waterline in our system, is assessed the OIC.

If the Commission refers to projects which install new lines "necessary" to replace older ones deteriorated with age and no longer serviceable, then the financing would be accomplished through general revenues as part of the annual budget for replacement expenditures.

If the replacements are necessitated by growth in the general vicinity of previously certified developments, and the new lines are larger diameter hydraulic improvements, then they would be OIC-eligible, as long as they were listed and approved in our biennial submittal to the PSC.

However, if the Commission is envisioning a situation in which growth *within* a previously certified development necessitates larger lines, it is not a feasible scenario. As we discussed in Item 4, we have already taken our prior commitments of service into account hydraulically.

14. Refer to Table I. This table suggests that Henry District collects net annual revenue of \$138.87 from each customer added. Assuming this revenue is used solely for capital improvements, Henry District will collect net revenues from each added customer to offset that customer's hydraulic impact on the distribution system within 7 years. Explain why a one-time charge to each new customer for the cost of his or her hydraulic effect on the water district's distribution system is necessary if present general service rates effectively provide for recovery of that cost over a 7-year period. To the extent that the response refers to "fairness" to existing customers, the response should address why existing customers, who are not assessed an Offsetting Improvement Charge, are effectively permitted to pay for their share of capital improvement costs over 17- to 30-year periods (the payment period for Henry District's long-term debts).

TABLE I

Net Operating Income ("NOI")	\$279,095
Plus: Interest Income	85,905
Income Available to Service Debt	\$365,000
Principal Retirement	\$333,008
Interest Expense	509,830
Coverage at 20 Percent of Principal and Interest	168,568
Total Debt Service	\$1,011,406
Income to Debt Shortfall	\$646,406
Depreciation Expense included in NOI	\$780,845
Less: Income to Debt Shortfall	(646,406)
Depreciation Funded Through Rates	\$134,439
Total Debt Service	\$1,011,406
Plus: Depreciation Funded Through Rates	134,439
Total Fixed Capital Costs Recovered Through Rates	1,145,845
Divide by: Gallons sold	529,879,000
Fixed Capital Costs per Gallon Sold	.00216
Times: Average Annual Gallons Sold per Residential Customer	64,292
Fixed Capital Costs Collected through Rates from the Average Residential Customer in an Annual Period	\$138.87

³ Current Offsetting Improvement Charge (\$950) ÷ \$138.87 per year = years.

Item 14 constructs a pyramid of assumptions. It first assumes that 100% of "net annual revenue" (including restricted-use interest) is available "solely for capital improvements." It next assumes that *all* such capital improvements will be waterlines in the distribution system (no new pumps, tanks, treatment equipment, raw water lines, control valves, telemetry, vehicles, construction equipment, wellfield improvements, billing software, GPS equipment, capitalized legal fees, etc.) It then further assumes that 100% of these distribution-only capital improvements will be hydraulic upsizing projects offsetting the impact of growth (no new line extensions into unserved areas and no projects which replace deteriorated lines, despite the inclusion of \$134,439 depreciation in Table I calculations).

Based on this pyramid of assumptions the conclusion is reached that each new customer will offset his hydraulic impact in seven years. The exclusive allocation of his collected net revenues to hydraulic improvement projects means that he will contribute nothing to the other needs of the system during this period, which assumes that existing customers will subsidize his share of these costs. This assumption undercuts the basic rationale of the system development charge.

Item 14 also broadly implies that we should somehow achieve retroactive historical parity between new and existing customers. It suggests that there can be an equivalency between customer B, who pays for his meter plus an impact fee, and customer A, who got water service for only the cost of his meter before the fee went into effect. But a system development charge must draw a distinct line in time after which development is required to pay its reasonably determined share of growth-specific infrastructure costs, and before which, it was not.

A review of our PSC annual reports indicates that in the 7-year period from 1999 through 2005, if the Table 1 "NOI" figures (called "Utility Operating Income" in the reports) are appropriately adjusted for interest expense, Henry District has had cumulative net income of negative \$289,971, for an average loss of \$41,410 per year, or approximately -\$7 per customer annually:

Net Income Before Contributions

1999	\$145,415
2000	(\$100,278)
2001	\$ 38,422
2002	\$ 7,855
2003	(\$165,849)
2004	(\$ 94,466)
2005	(\$120,970)

15. State the time limit, if any, that should be placed on Henry District's retention of unused proceeds from the Offsetting Improvement Charge.

We would expect that a five year period might be practicable. Accumulating impact fees until there is a sizable balance available for a larger project can allow the District to achieve economy of scale, and to better demonstrate its level of financial commitment, attracting grants or otherwise favorable funding. We would not want to be required to empty the account too frequently, therefore a dollar limit might make more sense than a time limit. For example, once the account balance reaches \$500,000, the District would be required to spend that amount on an OIC project or projects within an eighteen month period. We suggest eighteen months based on our experience with the timeline of initial design, plans and specifications, right-of-way acquisition, state approvals, bidding and construction.

16. State if Henry District has projected the level and characteristics of the customer growth that it will experience in the next 10 years and the demand that such growth will place on its system. If such projections have been made, provide these projections.

Similarly, Item 22 of the May 22, 2006 Order requests that Henry District:

“Provide all studies and reports that Henry District has prepared or commissioned that discuss or otherwise address the projected customer growth or demand in the water district’s area.”

Our response to Item 22 of the May 22, 2006 Order fully addresses our growth projections. Our response also states:

“However it is important to reiterate that the Henry District’s Offsetting Improvement Charge does not in any way depend upon our predictions of growth in order to calculate our development charge...”

And in our response to Item 3 of the May 22, 2006 Order we state:

“In the following pages many of the Interrogatories evaluate our tariff in terms of standard SDC methodology; however, it is not as a standard methodology that we have applied for approval.”

Because the standard incremental SDC in 807 KAR 5:090 assesses developers the *anticipated* costs of growth, growth projections are absolutely crucial. But ten year growth projections are *not* a necessary component of the Henry District’s Offsetting Improvement Charge, because we assess developers what the average cost of growth has been in the recent past. Item 16 equates to Section 3, paragraph 5(b) of the 807 KAR 5:090 SDC methodology checklist. However, we have very clearly acknowledged that ours is an alternative methodology in keeping with Section 14 of the KAR, which permits such deviations.

The brief filed by the Attorney General’s office in Case 2001-00393 stated:

“It is clear the District is seeking approval of a system development charge tariff under an existing regulation addressing this type of mechanism.”

In July of 2002, our tariff could *only* have been approved as a deviation from the existing regulation, as an alternative approach which the Commission found to be reasonable and in the public interest. Since 2002, neither the rationale of the Henry District’s charge nor 807 KAR 5:090 have changed.

17. State if the closing of loops provides benefits to existing customers. If yes, describe how these benefits can be ascertained.

Please refer to Item 3 of these responses.

18. State if Henry District currently has any plans to provide fire protection service.

We do not.

19. List and describe all Henry County Planning and Zoning Commission requirements regarding the availability of fire protection service to real estate subdivision developments.

The Planning Commission has not required us to make fire flow certifications, although they have presented this issue at a meeting of the HCWD2 Board. We explained to the Planning Commission that our PSC-approved tariff states that we do not guarantee pressures for the purpose of fire protection, and further states that we do not permit the installation of fire hydrants on our new lines.

PSC Administrative Case 385 observed:

“Kentucky law does not expressly confer an obligation upon any water utility to provide fire protection service... By this Order, the Commission does not expand or extend any water utility’s obligation to provide fire protection services.”

20. State if Henry District has conducted any analyses or studies to determine if it can provide fire protection flows to portions of its system. If yes, provide a copy of all analyses and studies.

We have not.

21. Refer to Henry District's Response to the Commission's Order of May 22, 2006, Item 6(a). Define "growth area."

In the context of our response to Item 6(a), we mean by "growth area" any geographic portion of our distribution system which has experienced a higher than average number of proposed subdivisions, commercial developments, industrial developments, or which possesses a clear and significant potential for development, such as our two interstate exchanges. These determinations result from the local knowledge and experience of the HCWD2 staff, commissioners, and other county officials, combined with the Commonwealth of Kentucky's projections of growth, and the professional judgment of HCWD2's consultants.

The PSC's concerns about the arbitrary, inappropriate, or unwise allocation of OIC proceeds into improperly determined "growth areas" are addressed by the internal checks and balances of the tariff itself. We submit to the Commission a biennial listing of projects for approval prior to any subsequent project expenditure, and we provide a detailed yearly accounting of OIC proceeds received and spent, specifically identifying those OIC-approved projects which have been funded.

The Henry District, through the judgment of its commissioners, regularly makes a great many decisions about the allocation of substantial resources. If our judgment is suspect in the use of OIC revenues, then what of these other, larger decisions? We have invested considerable amounts of time and money in analyzing, developing, and obtaining PSC approval of a reasonable and equitable SDC methodology. It is unlikely that we would suddenly become irresponsible in its application.

22. Refer to Henry District's Response to the Commission's Order of May 22, 2006, Item 6(b). State the level at which Henry District defines an area as low pressure and requires the construction of additional improvements to raise existing water pressures in the area.

Very generally speaking, when minimum daily pressure falls below 40 psi, we become concerned about future hydraulic adequacy. But in a distribution network with 600 miles of lines and ten tanks feeding interdependent service areas with changing usage, the system dynamics do not always lend themselves to simple rules-of-thumb.

For example, we have about 250 miles of 3-inch line. At given flowrates this diameter generates much higher pressure loss per mile than 6-inch line. Adding a 25-lot subdivision on a 3-inch line with existing minimum daily pressure of 40 psi would be far more likely to produce unacceptably low pressures than adding that 25-lot subdivision on a 6-inch main with the same 40 psi minimum pressure. The smaller line is more hydraulically vulnerable, so 40 psi is more of a red flag.

Or consider two proposed subdivisions on two 3-inch lines with identical 40 psi minimum pressures. One line is a dead end with unidirectional flow, and the other is looped so that flow is available from either direction. The 40 psi is much more of a concern on the one-way line.

Consider a proposed 25-lot subdivision on a four-mile 3" line with 40 psi minimum pressure. If the proposed location of the development is near the flow source of the 3" line, say a half-mile from its connection to a 6" line, the overall hydraulic effect will be moderate because pressure loss due to friction accumulates with distance. However if the proposed location is near the end of the line, the subdivision's effect on minimum pressures would be far greater.

A pressure of 45 psi on a 3" line could be much more of a concern than a pressure of 35 psi on a 16" line. Underlying most of these considerations is the basic question of how near a particular line is to its reaching its maximum useful flowrate. If the 40 psi is only experienced at a single topographical high point along a large diameter line with significant reserve capacity, then the low pressure is essentially the result of the difference in elevation between the meter and the tank level, and not due to headloss in the pipe. Adding flow to this line would not be nearly as detrimental as in alternative scenarios.

These are a few of the factors which limit the working value of any inflexible definition of "low pressure area."

This discussion leads back to the larger point that we have tried to make in response to several other questions, beginning in Case 2001-00393 and carrying over into the present investigation. The needs of our water distribution system are literally *fluid*. The dynamics are interdependent and changing. A road which we might reasonably predict to need no short-term attention could nevertheless be the road where a number of landowners decide over the next few next months to subdivide and develop their properties. In brief period a substantial amount of waterline will be brought much closer to its maximum capacity. The area quickly rises in priority, and an upsizing project must be considered.

To lock a system like HCWD2 into a ten year capital improvement plan, or even into a rigidly prioritized sequence of line upsizing projects, is to ignore the system-specific realities of land development and hydraulics in a distribution system originally designed for limited flow over extensive but sparsely populated areas. To be permitted flexibility in making best use of available resources does not lead to arbitrary and unreasonable decisions, quite the opposite.

23. Refer to Henry District's Response to the Commission's Order of May 22, 2006, Item 6(a).

a. State if Henry District has conducted any study or analysis to determine the component of its present general service rates that covers "the maintenance, operation, debt service, etc. of those existing facilities which are not necessary to serve" customers in areas not certified before July 25, 2002.

The referenced Item 6(a) of the May 22, 2006 Order actually concerns criteria for the upsizing of lines, not the issue of general rate components. We assume the Commission instead intends to refer to our response to May 22, 2006, Item 3, in which we state:

“Ours is a compromise approach which functions as a shorthand solution the following problem regarding incremental SDC methodology: Is it reasonable to levy a system development charge on new customers for the *entire* cost of improvements necessary to serve only that group, and also to charge that same group water rates which include a component for the maintenance, operation, debt service, etc., of those existing facilities which are *not* necessary to serve that group? By excluding from our OIC calculation the future costs of new treatment and storage capacity, our tariff tends to counterbalance this double jeopardy effect, and, we believe, achieves a more reasonable result.”

We have not conducted a study to determine the value of the “...maintenance, operation, debt service...” component. We are certain, however, that is more reasonable to exclude from the OIC some portion of the cost of new infrastructure necessitated by growth than to assess new customers the entire cost of such infrastructure *and* charge them water rates which include the above component.

b. State if isolation of this component will ensure that customers in areas not certified before July 25, 2002 do not contribute to the cost of water distribution mains in certified areas. Explain.

We assume that “customers in areas not certified before July 25, 2002” is intended to mean new customers who pay the OIC. We do not, however, certify areas, roads, vicinities, or lines; we certify only specific developments. A newly created lot on the oldest water distribution main in our system would be assessed the OIC.

The phrase “contribute to the cost of water distribution mains” could either mean the upkeep and debt costs of existing lines, or the cost of constructing new water lines for improving service in “certified areas.” The latter would involve a misinterpretation of certification, so we will address the former.

As we understand it, the question asks whether isolating the upkeep costs of facilities which do not serve new customers will insure that those new customers do not pay for maintenance, etc., on existing water distribution mains which do not serve them.

If isolating this component could be done properly, we assume it would accomplish its aim. But this is a misunderstanding, actually a reversal, of the statement which we made in response to May 22, 2006 Item 3, and which we have cited in Item 23 (a) above. We have *not* isolated from water rates paid by new customers the cost component for the upkeep and debt service of lines which do not serve them. It is precisely because these new customers

do pay rates which *include* this component that it is “more reasonable” to charge them *less* than the entire cost of infrastructure improvements necessitated by growth. The OIC therefore focuses on line improvement projects exclusively, and excludes from its calculation the growth-related costs of treatment and storage.

24. Refer to Henry District's Response to the Commission's Order of May 22, 2006, Item 5(a). State if the documents found at Appendix B comprise Henry District's complete and current long-term plan for the construction of water mains.

Appendix B, Sheet 1 of 5, reflects the Henry District's most recent 2005 KIA project listing, however in preparing this spreadsheet we inadvertently omitted one project.

PWSID# WX021103015 is the "KY 1861 & KY 22 Smithfield Loop" project, which does appear in Appendix B on Sheet 2 of 5 (our 2003 KIA listing) and Sheet 4 of 5 (our 2002 listing). We regret this oversight.

Several projects in the 2005 KIA listing have been completed or are under construction. Sweeney (3046) and Union Church (3047) were recently installed by HCWD2 personnel. Systemwide Betterment (3042) and Cemetary Hill (3029) projects are currently under construction by Sedam Contracting.

Please see also our response to Item 22 herein.

25. Refer to Henry District's Response to the Commission's Order of May 22, 2006, Item 10. Describe how Henry District intends to finance the construction of water mains to remedy pre-existing deficiencies in its water distribution system.

Our response to Item 10 of the May 22, 2006 Order states:

“There are no areas of the system in which customers receive service which does not comply with state regulatory standards. Although no hydraulic deficiencies currently exist, the west/southwest portions of the HCWD2 system have very limited capacity for growth due primarily to the bottleneck in a six-inch line along US 42/KY 153. There is in addition, a similar bottleneck along US 421/KY 22 in the southeast portion of the District. Several other areas are currently adequate but also nearing capacity.”

A clarification of the PSC’s definition of “deficiency” would seem to be in order. Regulatory deficiencies would mean unacceptable water quality, or inadequate pressures. The Henry County system is in compliance with these regulations, and therefore as stated above “no hydraulic deficiencies currently exist.” There are areas where in our judgment it would be wise to anticipate new demand and install larger lines. To the extent possible, we hope that growth will pay for its reasonably determined share of such costs, but as we stated in response to May 22, 2006 Item 16 (b):

“Making only those hydraulic improvements which the OIC fund can afford to finance at any given time would not allow the District to get ahead of the demand curve. Hydraulic improvements funded through general rates provide excess capacity, the cost of which can be recouped through the OIC. In this sense the general rates fund hydraulic projects as loans to the system which can eventually be repaid by future development.”

26. Refer to Henry District's Response to the Commission's Order of May 22, 2006, Item 12. Define "minor replacement expenditures."

We have budgeted an estimated \$100,000 annually to replace pumps and lines, etc., which have reached the end of their useful life. This expenditure is sometimes exceeded or not reached, depending on yearly circumstances in the system. An old creek crossing may fail and need replacing, an electric control valve or pump may wear out, or a section of cast iron line may be replaced after having corroded badly or accumulated deposits which constrict flow.

27. Refer to Henry District's Response to the Commission's Order of May 22, 2006, Item 12. State if Henry District agrees with the following statement: "If a water district fails to include depreciation expense in calculating its general rates, it fails to assess its customers the actual cost of providing water service and requires future customers to bear a share of the costs necessary to provide service to current customers." Explain.

We disagree completely. We would rephrase the statement to read:

If a water district includes full depreciation expense in calculating its general rates, it assesses its customers more than the actual current cost of providing water service and requires its current customers to bear a share of the costs necessary to provide service to future customers.

Our response to Item 12 of the May 22, 2006 Order contains a clear explanation of our policy:

“We disagree with the concept of including major depreciation expense in general water rates, because existing customers have already paid the rates which over the years have built the system. Charging these same customers again for depreciation imposes a double burden on them in order to provide new facilities as required by future customers. We believe it is more reasonable to allow future rate increases and debt to provide funding for major infrastructure replacement projects.”

28. Refer to Henry District's Response to the Commission's Order of May 22, 2006, Item 13. Henry District states that "general rates should recover the cost of providing water service including an annual allowance for replacing capital equipment and facilities, not the full expense of depreciation."

a. Describe how this "annual allowance" should be determined.

Based on the experience and budget of the District we have arrived at an annual estimate of \$100,000. Please see also our response to Item 26.

b. Explain why recovery of the amount of depreciation expense is inappropriate.

We assume the Commission means recovery of the *full* amount of depreciation expense. Our response to Item 12 of the May 22, 2006 Order contains an explanation of our policy, as noted previously.

29. Explain why Mr. Green requested Henry District's Board of Commissioners on June 13, 2006 to adopt the two resolutions regarding depreciation policy and the upsizing of water mains.

The Commission requested, in Item 6(a) of the May 22, 2006 Order, the criteria which HCWD2 uses to locate and upsize mains. Item 6(b) requested the "policy statement, resolution or other documents that reflect that Henry District's Board of Commissioners has adopted these criteria."

Because the document which clearly stipulates the upsizing criteria of "growth, low pressure, and cost-effectiveness" is the OIC tariff itself, which was approved by both the HCWD2 Board and by the PSC, we concluded that the Commission in Item 6(b) must have been requesting some further official affirmation or clarification of this policy. To be as responsive as possible we therefore provided an expanded Board resolution.

The HCWD2 depreciation policy had never been the specific subject of a specific Board resolution, except of course that water rates containing only limited depreciation expense were regularly approved by the Board, as were annual budgets which provided for these limited replacement expenditures.

Our understanding is that over the years the PSC itself has changed its policy regarding the inclusion of depreciation costs, and we thought it would be appropriate in response to May 22, 2006 Item 12 to reaffirm in the form of a resolution what has, in effect, been the HCWD2 policy toward depreciation for a number of years.

30. Refer to Henry District's Response to the Commission's Order of May 22, 2006, Item 16(b).

a. Explain how the cost of hydraulic improvements funded through general rates can later be recouped though the Offsetting Improvement Charge.

These costs can be recouped when the OIC account is adequate to directly reimburse the District's general fund for any OIC-eligible projects which have been financed through general revenues. In its discussion of incremental methodology in PSC Administrative Case 375 (SDC guidelines), the Commission states:

“This method is used most commonly where SDCs are used to finance capital expansion as well as to recoup investments creating excess capacity for new demand.”

b. Provide the written procedures or policies that Henry District has to govern the use of Offsetting Improvement Charge proceeds to reimburse projects funded through general service rates.

The written procedure and policy is the OIC tariff itself. It states:

“At the time of each biennial offsetting improvement charge recalculation, the District shall supply the Public Service Commission with a written, long term construction plan for the proposed use of proceeds from the offsetting improvement charge.”

These submitted projects are exclusively hydraulic improvements to the distribution system, i.e. line upsizings and loop closures. Any project listed in this biennial submittal to the PSC will therefore be eligible for OIC funding. If the listed project is instead built with general revenue funds, the OIC account can later be used to reimburse the project cost to the District.

The OIC tariff also states:

“At the end of each year the District shall submit to the Public Service Commission a list of all offsetting improvement charges collected and an accounting of all expenditures from said escrow account for hydraulic improvement projects.”

The Commission will therefore be notified on an annual basis of the specific projects which OIC funds have financed, and whether this involved directly funding construction, or reimbursement to the District for a listed OIC-eligible project financed by general revenues.

However, the current OIC projects will require several million dollars to construct, and the District will need all available sources of funding to accomplish this work. Therefore, as a practical matter, it will be many years before the District seeks such project reimbursements. When we do, we will clearly identify the reimbursements in our annual reporting to the PSC.

31. State if Henry District classifies its customers into different customer classes (e.g., residential, industrial, agricultural) for customer usage or billing. If yes, define each classification and describe how that classification is used for billing and planning purposes.

The customer categories we currently track are those of commercial, residential, dairy, and wholesale usage. These classifications have been set up by our software company as modifications to categories we have historically used for internal information purposes at our office.

Commercial customers include businesses and factories. Residential customers include all domestic and agricultural users with the exception of dairy farms, which are particularly water-intensive. Wholesale users include cities and districts which purchase from us under wholesale contracts for resale to their own customers.

Wholesale billing is done according to a separate wholesale rate schedule, but the other customer classifications have no significance as regards billing. Their rate schedules, times of billing, and conditions of service are identical.

We use these categories in assigning levels of demand throughout the hydraulic model of our system. We customize daily demand curves to reflect certain commercial/factory operations, and we break out dairies so as to pinpoint high usage. Therefore when we hydraulically evaluate future scenarios, we incorporate some of the usage patterns of our customer classifications.

32. Refer to Henry District's Response to the Commission's Order of May 22, 2006, Item 20. Provide for each year from January 1, 1996 to December 31, 2005 the number of new meters set on previously unserved new lots.

1996	152
1997	114
1998	138
1999	217
2000	169
2001	147
2002	137
2003	130
2004	116
2005	134
Total	1454

BOND RESOLUTION

HENRY COUNTY WATER DISTRICT NO. 2

AUTHORIZING

HENRY COUNTY WATER DISTRICT NO. 2
WATERWORKS REFUNDING REVENUE BONDS, SERIES 1998

IN THE AMOUNT OF

\$8,470,000

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EXHIBIT A - Schedule of Principal Maturities
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BOND RESOLUTION

RESOLUTION OF THE HENRY COUNTY WATER DISTRICT NO. 2, AUTHORIZING AND PROVIDING FOR THE ISSUANCE AND SALE OF \$8,470,000 (PLUS OR MINUS \$850,000) PRINCIPAL AMOUNT OF HENRY COUNTY WATER DISTRICT NO. 2 WATERWORKS REFUNDING REVENUE BONDS, SERIES 1998, DATED OCTOBER 1, 1998, FOR THE PURPOSE OF FINANCING THE COST (NOT OTHERWISE PROVIDED) OF THE REFUNDING OF CERTAIN OUTSTANDING OBLIGATIONS OF THE DISTRICT.

WHEREAS, the waterworks system (the "System") of the Henry County Water District No. 2 (the "District") is owned and operated by said District pursuant to Chapter 74 of the Kentucky Revised Statutes (the "Act"), and

WHEREAS, the District has heretofore issued the following obligations:

- (a) Henry County Water District No. 2 Waterworks System Revenue Bonds, dated November 20, 1967, in the original authorized principal amount of \$1,850,000 (the "Bonds of 1967") authorized by a Resolution adopted by the District on September 14, 1967 (the "1967 Bond Resolution");
- (b) Henry County Water District Waterworks Refunding and Improvement Revenue Bonds, Series B, dated April 1, 1967, in the original authorized principal amount of \$175,000 (the "Bonds of 1968") authorized by a Resolution adopted by the District on August 14, 1967 (the "1968 Bond Resolution");
- (c) Henry County Water District No. 2 Waterworks Revenue Bonds, Series of 1974, dated June 4, 1975, in the original authorized principal amount of \$239,000 (the "Bonds of 1974") authorized by a Resolution adopted by the District on February 12, 1974 (the "1974 Bond Resolution");
- (d) Henry County Water District No. 2 Waterworks Revenue Bonds of 1986, dated June 29, 1987, in the original authorized principal amount of \$500,000 (the "Bonds of 1986") authorized by a Resolution adopted by the District on March 11, 1986 (the "1986 Bond Resolution");
- (e) Henry County Water District No. 2 Waterworks Revenue Bonds of 1987, dated October 28, 1988, in the original authorized principal amount of \$1,999,000, (the "Bonds of 1987") authorized by a

Resolution adopted by the District on October 18, 1987 (the "1987 Bond Resolution");

- (f) Henry County Water District No. 2 Waterworks Revenue Bonds, Series 1996, dated April 29, 1997, in the original authorized principal amount of \$3,000,000 (the "Bonds of 1996") authorized by a Resolution adopted by the District on September 10, 1996 (the "1996 Bond Resolution");
- (g) Non-interest bearing Note payable to the Shelby Rural Electric Cooperative Corporation ("SRECC"), now known as Shelby Energy Cooperative, Inc., dated April 29, 1997, in the original authorized principal amount of \$400,000 (the "SRECC Note") authorized by a Loan Agreement entered into by the District, dated April 29, 1997 (the "SRECC Loan Agreement"); and
- (h) Interim Loan from the Kentucky Infrastructure Authority to the District in the approximate principal amount of \$5,250,000, pursuant to an Assistance Agreement dated as of October 1, 1996 (the "KIA Loan").

Hereinafter the Bonds of 1967, Bonds of 1974, Bonds of 1996 and the SRECC Note are collectively referred to as the "Prior Bonds" and the 1967 Bond Resolution, 1974 Bond Resolution, and SRECC Loan Agreement are referred to as the "Prior Bond Resolution"; and

WHEREAS, the District has determined it is necessary and desirable in the public interest that the District currently refund and retire the outstanding Bonds of 1968, Bonds of 1986, Bonds of 1987 and KIA Loan (collectively, the "Refunded Bonds"), which may be paid and discharged immediately, in order to effect substantial debt service savings; and to provide funds for such refunding it is now appropriate for the District to cause the sale and issuance of its Waterworks Refunding Revenue Bonds, Series 1998 (the "Current Bonds"), according to the authority of KRS Chapters 58 and 74 and the applicable provisions of the Prior Bond Resolution permitting the issuance of bonds on a parity with the Prior Bonds, which Current Bonds shall be payable as to both principal and interest solely from the income and revenues to be derived from the operation of the System, as extended and improved from time to time, on a parity with the Prior Bonds, and shall not constitute an indebtedness of the District within the meaning of provisions of the Constitution and statutes of the Commonwealth of Kentucky; and

WHEREAS, the United States of America, acting by and through the U.S. Department of Agriculture, Rural Development (the "RD"), as holder of the Bonds of 1967, Bonds of 1974 and Bonds of 1996, has consented in writing to permit the issuance of the Current Bonds on a parity basis with the Prior Bonds, and accordingly, the Current Bonds shall be payable from and secured

by a pledge of the gross revenues of the System, on a parity with the Bonds of 1967, Bonds of 1974 and Bonds of 1996;

WHEREAS, the SRECC, as holder of the SRECC Note has consented in writing to permit the issuance of the Current Bonds on a parity basis with the SRECC Note, and accordingly, the Current Bonds shall be payable from and secured by a pledge of the gross revenues of the System, on a parity with the SRECC Note and the Prior Bonds;

WHEREAS, in proceedings before the Public Service Commission of Kentucky, the District has obtained, or will obtain prior to issuance of the Current Bonds, an order approving the issuance of the Current Bonds; and

WHEREAS, under the provisions of Chapters 58 and 74 of the Kentucky Revised Statutes, the District is authorized to issue the Current Bonds to provide such funds for the purpose aforesaid,

NOW, THEREFORE, BE IT RESOLVED BY THE HENRY COUNTY WATER DISTRICT NO. 2, AS FOLLOWS:

**ARTICLE 1. DEFINITIONS; PURPOSE; AUTHORIZATION OF BONDS;
SECURITY.**

Section 101. Definitions. As used in this Resolution, unless the context requires otherwise:

"Act" refers to Chapters 58 and 74 of the Kentucky Revised Statutes.

"Beginning Month" means the month following the month in which the Current Bonds authorized herein are issued, sold and delivered to the Purchaser thereof.

"Bond Counsel" refers to an attorney or firm of attorneys recognized nationally as experts in the field of municipal bond law and shall be deemed to refer to Rubin & Hays, Louisville, Kentucky, or their successors.

"Bondowner" or *"Owner"* mean and contemplate the registered Owners of the Current Bonds at the time issued and outstanding hereunder.

"Bonds" refers to the Current Bonds, the Prior Bonds, and any Parity Bonds issued hereinafter.

"Bonds of 1967" or *"Series 1967 Bonds"* refer to the outstanding Henry County Water District No. 2 Waterworks System Revenue Bonds, dated November 20, 1967, in the original authorized principal amount of \$1,850,000.

"Bonds of 1968" or *"Series 1968 Bonds"* refer to the outstanding Henry County Water District Waterworks Refunding and Improvement Revenue Bonds, Series B, dated April 1, 1967, in the original authorized principal amount of \$175,000.

"Bonds of 1974" or *"Series 1974 Bonds"* refer to the outstanding Henry County Water District No. 2 Waterworks System Revenue Bonds, Series of 1974, dated June 4, 1975, in the original authorized principal amount of \$239,000.

"Bonds of 1986" or *"Series 1986 Bonds"* refer to the outstanding Henry County Water District No. 2 Waterworks System Revenue Bonds of 1986, dated June 29, 1987, in the original authorized principal amount of \$500,000.

"Bonds of 1987" or *"Series 1987 Bonds"* refer to the outstanding Henry County Water District No. 2 Waterworks Revenue Bonds of 1987, dated October 28, 1988, in the original authorized principal amount of \$1,999,000.

"Bonds of 1996" or *"Series 1996 Bonds"* refer to the outstanding Henry County Water District No. 2 Waterworks Revenue Bonds, Series 1996, dated April 29, 1997, in the original authorized principal amount of \$3,000,000.

"Bond Registrar", "Transfer Agent", or "Paying Agent" refers to the bank which shall constitute the Bond Registrar, Transfer Agent and Paying Agent with respect to the Current Bonds, which Paying Agent shall have the duties and responsibilities of (a) issuing semiannual checks in payment of interest requirements as to the Current Bonds, (b) paying the principal (and redemption price, if any) of same at maturity or applicable redemption prior to maturity upon surrender of the Current Bonds, (c) authenticating, issuing and delivering the Current Bonds to the original purchasers of same in accordance with the sale of the Current Bonds, at the direction of the District (d) maintaining the Current Bonds register, and (e) handling exchanges, cancellations, reissuance, redemption and all apparent duties of a Bond Registrar and Transfer Agent with respect to the Current Bonds, as hereinafter set out. The Bond Registrar, Transfer Agent and Paying Agent hereby designated is The Fifth Third Bank, Cincinnati, Ohio; provided, however, it is understood that the District reserves the right to designate a different Federal Deposit Insurance Corporation instrumentality to perform any and all of such functions of Bond Registrar, Transfer Agent and Paying Agent as to the Current Bonds.

"Bond Resolution of 1967" or "1967 Bond Resolution" refer to the Resolution authorizing the Bonds of 1967, duly adopted by the Board of Commissioners of the District on September 14, 1967.

"Bond Resolution of 1968" or "1968 Bond Resolution" refer to the Resolution authorizing the Bonds of 1968, duly adopted by the Board of Commissioners of the District on August 14, 1967.

"Bond Resolution of 1974" or "1974 Bond Resolution" refer to the Resolution authorizing the Bonds of 1974, duly adopted by the Board of Commissioners of the District on February 12, 1974.

"Bond Resolution of 1986" or "1986 Bond Resolution" refer to the Resolution authorizing the Bonds of 1986, duly adopted by the Board of Commissioners of the District on March 11, 1986.

"Bond Resolution of 1987" or "1987 Bond Resolution" refer to the Resolution authorizing the Bonds of 1987, duly adopted by the Board of Commissioners of the District on October 13, 1987.

"Bond Resolution of 1996" or "1996 Bond Resolution" refer to the Resolution authorizing the Bonds of 1996, duly adopted by the Board of Commissioners of the District on September 10, 1996.

"Certified Public Accountants" refers to an independent Certified Public Accountant or firm of Certified Public Accountants, duly licensed in affairs of the System and/or of other District financial matters. Until otherwise directed by the governing body of the District, such term shall be deemed to refer to Donald R. Baxter, CPA, Louisville, Kentucky.

"Chairman" refers to the elected or appointed Chairman or Chairperson of the Commission.

"Code" refers to the Internal Revenue Code of 1986, as amended, and the Treasury Regulations relating thereto.

"Commission" or "Governing Body" means the Board of Commissioners of the District, or such other body as shall be the governing body of said District under the laws of Kentucky at any given time.

"Current Bond Resolution" or "Resolution" refers to this Resolution authorizing the Current Bonds.

"Current Bonds" refers to the \$8,470,000 (plus or minus \$850,000) of Henry County Water District No. 2 Waterworks Refunding Revenue Bonds, Series 1998 authorized by this Resolution, dated as of October 1, 1998.

"Depository Bank" means the bank, which shall be members of the FDIC, and which have served and shall continue to serve as the depository of all of the Funds created in the Prior Bond Resolution and this Current Bond Resolution, which bank is United Citizens Bank & Trust Company, Campbellsburg, Kentucky.

"Depreciation Fund" refers to the Henry County Water District No. 2 Waterworks Revenue Bond Depreciation Reserve Fund, described in Section 401(E) of this Resolution.

"District" refers to the Henry County Water District No. 2 of Henry, Trimble, Carroll, Shelby and Oldham Counties, Kentucky.

"Event of Default" refers to one or more of the Events of Default set forth in Section 701 of this Resolution.

"FDIC" refers to the Federal Deposit Insurance Corporation, or its successors.

"Financial Advisor" refers to the firm of J.J.B. Hilliard, W.L. Lyons, Inc., Louisville, Kentucky.

"Fiscal Year" refers to the annual accounting period of the District, beginning on January 1 and ending on December 31 of each year.

"Funds" refers to the Revenue Fund, the Sinking Fund, the Depreciation Fund, the Reserve Fund and the Operation and Maintenance Fund.

"Government" means the United States of America, or any agency thereof, including the RD.

"Independent Consulting Engineer" refers to a consulting engineer or a firm of consulting engineers of recognized excellent reputation in the field of waterworks system engineering.

"Interest Payment Date" shall mean January 1 and July 1 of each year, commencing January 1, 1999.

"KIA Loan" refers to the interim loan from the Kentucky Infrastructure Authority to the District in the approximate principal amount of \$5,250,000, pursuant to an Assistance Agreement dated as of October 1, 1996.

"Operation and Maintenance Fund" refers to the Henry County Water District No. 2 Waterworks Operation and Maintenance Fund described in Section 401(F) of this Resolution.

"Outstanding Bonds" refers to the outstanding Prior Bonds, the Current Bonds, and any additional outstanding Parity Bonds, and does not refer to, nor include, any Bonds for the payment of the principal and interest of which sufficient funds will have been deposited and earmarked for payment of Bonds; provided all Outstanding Bonds of any series held by the RD shall be deemed to constitute Outstanding Bonds until paid regardless of the deposit of funds to pay for same.

"Parity Bonds" means bonds which may be issued in the future, in addition to the Prior Bonds and the Current Bonds, which Parity Bonds issued in the future will, pursuant to the provisions of this Current Bond Resolution and the Prior Bond Resolution, rank on a basis of parity with said Outstanding Bonds, as to priority, security and source of payment, and does not refer to bonds which might be issued so as to rank inferior to the security and source of payment of the outstanding Current Bonds.

"Permitted Investments" refers to and includes (a) direct obligations of or obligations guaranteed by the United States of America, including bookkeeping entries; and (b) interest-bearing time deposits or certificates of deposit issued by banks insured by the FDIC and fully secured, to the extent of the amount in excess of the amount insured by the FDIC, by a pledge of direct obligations of, or obligations guaranteed by, the United States of America having a fair market value, exclusive of accrued interest, equal to not less than 100% of such excess amount.

"Prior Bonds" refers to the Bonds of 1967, Bonds of 1974, Bonds of 1996 and SRECC Note.

"Prior Bond Resolution" refers to the 1967 Bond Resolution, 1974 Bond Resolution, 1996 Bond Resolution and SRECC Loan Agreement.

"Purchaser" means the agency, person, firm or firms, or their successors, to whom the Current Bonds herein authorized are awarded at the public sale of the Current Bonds.

"RD" means the Rural Development of the Department of Agriculture of the United States of America.

"Record Date" shall mean with respect to any Interest Payment Date, the close of business on June 15 or December 15, as the case may be, next preceding such Interest Payment Date, whether or not such June 15 or December 15 is a business day.

"Refunded Bonds" refers to the Bonds of 1968, Bonds of 1986, Bonds of 1987 and KIA Loan.

"Refunding Program" refers to the refinancing and current refunding of the Refunded Bonds.

"Reserve Amount" refers to an amount, as of any particular date of computation, equal to the lesser of (i) the maximum annual debt service on the Current Bonds; (ii) 10% of the proceeds of the Current Bonds issued; or (iii) 125% of the average annual principal and interest requirements on the Current Bonds.

"Reserve Fund" refers to the Henry County Water District No. 2 Waterworks Debt Service Reserve Fund of 1998, created in Section 401(C) of this Resolution.

"Revenue Fund" refers to the Henry County Water District No. 2 Waterworks Revenue Fund, described in Section 401(A) of this Resolution.

"Secretary" refers to the elected or appointed Secretary of the Governing Body.

"Sinking Fund" refers to the Henry County Water District No. 2 Waterworks Revenue Bond Sinking Fund, described in Section 401(B) of this Resolution.

"SRECC" refers to the Shelby Rural Electric Cooperative Corporation, now known as Shelby Energy Cooperative, Inc.

"SRECC Note" refers to the non-interest bearing Note payable to the SRECC, dated April 29, 1997, in the original authorized principal amount of \$400,000.

"SRECC Loan Agreement" refers to the Loan Agreement between the District and SRECC authorizing the SRECC Note, dated as of April 29, 1997.

"System" refers to the existing waterworks system of the District, together with all extensions, additions and improvements to said System.

"Treasurer" refers to the appointed Treasurer of the District.

"U.S. Obligations" means bonds or notes which are the direct obligations of the United States of America, or obligations the principal of and interest on which are guaranteed by the United States of America.

All words and terms importing the singular number shall, where the context requires, import the plural number and vice versa. Unless otherwise indicated, references to Articles or Sections refers to those in this Resolution.

Section 102. Authorization of Bonds. For the purpose of defraying the costs (not otherwise provided) of the Refunding Program, there are hereby authorized to be presently issued and sold Eight Million Four Hundred Seventy Thousand Dollars (\$8,470,000) [plus or minus up to \$850,000] principal amount of Henry County Water District No. 2 Waterworks Refunding Revenue Bonds, Series 1998, dated and bearing interest from October 1, 1998. In order to provide sufficient revenues to undertake the Refunding Program the principal amount of the Current Bonds shall be adjusted upward or downward as deemed necessary by the Governing Body on the date of the sale of the Current Bonds. Said Current Bonds shall mature serially on the first day of January of the respective years, as set out in Exhibit A attached hereto, and shall bear interest payable semiannually on the first days of January and July of each year, beginning on January 1, 1999, at an interest rate or rates and in the maturities to be fixed by Resolution of the Governing Body as a result of the advertised sale of the Bonds.

Section 103. Recognition of Outstanding Bonds. The District hereby expressly recognizes and acknowledges that the District has previously created for the benefit and protection of the owners of the Outstanding Bonds, a certain lien and pledge and certain security rights relating to the System, all as set forth in the Outstanding Bonds and in the documents authorizing such Outstanding Bonds.

Section 104. Current Bonds Shall be Payable on First Lien Basis Out of Gross Revenues. The Prior Bonds, the Current Bonds and any additional Parity Bonds that may be issued under the conditions and restrictions hereinafter set forth, shall be payable solely on a first lien basis out of the gross revenues of the System, and shall be a valid claim of the Owners thereof against the Sinking Fund created for the benefit of such owners.

**ARTICLE 2. THE BONDS; PRINCIPAL INSTALLMENTS; BOND FORM;
EXECUTION; PREPAYMENT.**

Section 201. Principal Installments. Principal installments due on the Current Bonds shall be as set forth in the schedule of maturities set out in **Exhibit A** attached to this Resolution, adjusted by the Resolution approving the sale of the Current Bonds, and incorporated herein by reference.

Section 202. Issuance of Current Bonds; Bond Form. The Purchaser of the Current Bonds at the public sale thereof shall take delivery of the Current Bonds in the form of one or more fully registered bonds, as set forth in **Exhibit B** attached hereto and incorporated herein by reference, amounting in the aggregate to the principal amount of the Current Bonds authorized herein, maturing as to principal in installments as set out in **Exhibit A**. The Current Bonds shall be numbered R-1 and consecutively upward thereafter. Such Current Bonds shall, upon appropriate execution on behalf of the District as prescribed herein, constitute the entire bond issue herein authorized, shall be negotiable (subject to registration requirements as to transferability), and payable as to principal and interest to the registered Owner.

Section 203. Place of Payment and Manner of Execution. The principal of (and redemption price, if any) and interest on the Current Bonds shall be payable in lawful money of the United States of America as they respectively become due, whether at maturity or by prior redemption. Principal of each Current Bond is payable upon surrender of same at the main office of the Paying Agent and Bond Registrar. Interest on the Current Bonds shall be paid by check or draft mailed by the Paying Agent to the Bondowners as of the Record Date, at the respective addresses appearing on the bond register.

So long as any Current Bonds remain outstanding, the Bond Registrar shall keep at its principal office a bond register showing and recording a register of the Owners of the Current Bonds and shall provide for the registration and transfer of Current Bonds in accordance with the terms of this Current Bond Resolution, subject to such reasonable regulations as the Bond Registrar may prescribe.

The Current Bonds shall be executed on behalf of the District with the duly authorized reproduced facsimile signature of the Chairman, and the reproduced facsimile of its corporate seal shall be imprinted thereon and attested by the reproduced facsimile signature of the Secretary; and said officials, by the execution of appropriate certifications, shall adopt as and for their own proper signatures, their respective facsimile signatures on said Current Bonds; provided the Authentication Certificate of Registrar must be executed by the manual signature of the Bond Registrar on each Current Bond before such Current Bond shall be valid.

The Bond Registrar shall have the right to order the preparation of whatever number of Current Bond certificates as, in the sole discretion of the Bond Registrar, shall be deemed necessary in order to enable the Bond Registrar to maintain an adequate reserve supply of such certificates to effect properly the continuing transfers and exchanges of ownership of the Current Bonds as same

are sold, exchanged and/or otherwise surrendered in the future. No further action regarding the authorization or execution of additional certificates shall be required by the Governing Body, the Chairman or the Secretary.

At least 5 business days prior to the delivery of the Current Bonds, the Purchasers shall furnish to the Bond Registrar the name, address, social security number or taxpayer identification number of each party to whom the Current Bonds shall have been resold and in whose name the Current Bonds are to be registered and the principal amounts and maturities thereof. The Bond Registrar shall then issue and deliver to the Purchasers, on the closing date, fully registered Current Bond certificates for each registered owner so designated.

Pending the preparation of printed Current Bonds the District may execute and, upon the District's request, the Bond Registrar shall authenticate and deliver one or more temporary Current Bond which may be printed, lithographed, typewritten, mimeographed or otherwise reproduced, in any denomination, substantially of the tenor of the printed Current Bonds in lieu of which they are delivered, in fully registered form without coupons, and with such appropriate insertions, omissions, substitutions and other appropriate and necessary variations as the officers of the District executing such temporary Current Bonds may determine, as evidenced by their signing such temporary Current Bonds.

All Current Bonds shall be exchangeable and transferable upon the presentation and surrender thereof at the office of the Bond Registrar, duly endorsed for transfer or accompanied by an assignment duly executed by the registered owner or his authorized representative, for a Current Bond or Current Bonds of the same maturity and interest rate and in any authorized denomination of \$5,000 and/or a multiple thereof within a single maturity, in an aggregate principal amount or amounts equal to the unpaid principal amount of the Current Bond or Current Bonds presented for exchange. The Bond Registrar shall be and is hereby authorized to (authenticate and) deliver exchange Current Bonds in accordance with the provisions of this Section 203. Each exchange Current Bond delivered in accordance with this Section 203 shall constitute an original contractual obligation of the District and shall be entitled to the benefits and security of this Current Bond Resolution to the same extent as the Current Bond or Current Bonds in lieu of which such exchange Current Bond is delivered.

Section 204. Redemption of Current Bonds.

(A) Mandatory Sinking Fund Redemption

If the successful bidder and original purchaser of the Current Bonds so elects in accordance with the provisions of the Official Terms and Conditions of Sale, and as may be provided in the Resolution of the Commission awarding the Current Bonds to such original purchaser, the Current Bonds stated to mature on the maturity dates set out in the successful bid of such original purchaser shall be combined to comprise the maturities of Term Bonds as set out in said successful bid and in said Resolution; and such Term Bonds shall be subject to mandatory redemption in part, at the

selection of the Paying Agent and Bond Registrar by lot in such manner as the Paying Agent and Bond Registrar may determine, from moneys in the Sinking Fund on each applicable January 1 at par plus accrued interest to the redemption date, according to the mandatory sinking fund redemption schedule or schedules set out in said Resolution and in principal amounts corresponding to the above maturity schedule set out in **Exhibit A** hereto.

(B) Optional Redemption

The Current Bonds maturing on and after January 1, 2010, are subject to redemption by the District, at its option, prior to maturity in whole or from time to time in part at any time on or after January 1, 2009, in any order of maturities (less than all of a single maturity to be selected by lot in such manner as the Paying Agent and Bond Registrar may determine) at the redemption prices (expressed as percentages of principal amount) set forth in the table below plus accrued interest to the redemption date:

<u>Redemption Dates (inclusive)</u>	<u>Redemption Price</u>
January 1, 2009, through December 31, 2009	102%
January 1, 2010, through December 31, 2010	101%
January 1, 2011 and thereafter	100%

(C) Other Redemption Provisions

The Paying Agent and Bond Registrar shall, upon being satisfactorily indemnified as to expenses, cause notice of the call for any redemption, identifying the Current Bonds or portions thereof (\$5,000 or any integral multiples thereof) to be redeemed, to be sent by registered or certified mail at least thirty (30) days prior to the date fixed for redemption to the Registered Holder of each Current Bond to be redeemed at the address shown on the registration books. Failure to give such notice by mailing or any defect therein in respect of any Current Bond shall not affect the validity of any proceedings for the redemption of any other Current Bond. Any notice mailed as provided in this Section shall be conclusively presumed to have been duly given, irrespective of whether the Registered Holder receives the notice. The redemption notice shall set forth in detail the redemption provisions.

Prior to the date fixed for redemption of Current Bonds, funds shall be deposited by the District with the Paying Agent and Bond Registrar to pay, and the Paying Agent and Bond Registrar is hereby authorized and directed to deposit such funds into the Sinking Fund hereinafter identified and to apply such funds to the payment of, the Current Bonds or portions thereof called for redemption, together with accrued interest thereon to the redemption date and any required premium. Upon the giving of notice and the deposit of adequate funds in the Sinking Fund for redemption of Current Bonds, interest on the Current Bonds or portions thereof so called for redemption shall cease to accrue after the date fixed for redemption. No payment of principal, premium or interest shall be made by the Paying Agent and Bond Registrar upon any Current Bond or portion thereof called for

redemption until such Current Bond or portion thereof shall have been delivered to the Paying Agent and Bond Registrar for payment or cancellation, or the Paying Agent and Bond Registrar shall have received the items required by Section 205 hereof with respect to any mutilated, lost, stolen or destroyed Current Bond.

A portion of any Current Bond maturing on or after January 1, 2010, may be redeemed, but Current Bonds shall be redeemed only in the principal amount of \$5,000 each or any integral multiples thereof. Upon surrender of any Current Bond for redemption in part only, the District shall execute and the Paying Agent and Bond Registrar shall register, authenticate and deliver to the holder thereof, within a period of three days from surrender of such Current Bond to the Paying Agent and Bond Registrar, at the expense of the District, a new Current Bond or Current Bonds of the same maturity, of authorized denominations and in aggregate principal amount equal to the unredeemed portion of the Current Bond surrendered.

Section 205. Mutilated, Lost, Stolen or Destroyed Current Bonds. If any Current Bond shall be mutilated, lost, stolen or destroyed, the District may execute, authenticate and deliver a new Current Bond of like maturity and tenor in lieu of and in substitution for the Current Bond mutilated, lost, stolen or destroyed; provided that, in the case of any mutilated Current Bond, such mutilated Current Bond shall first be surrendered to the District, and in the case of any lost, stolen or destroyed Current Bond, there shall be first furnished to the District satisfactory evidence of the ownership of such Bond and of such loss, theft or destruction, together with indemnity satisfactory to the Bond Registrar. If any such Current Bond shall have matured, the District (through the Bond Registrar) may pay the same instead of issuing a new Current Bond. The District and/or the Bond Registrar may charge the owner of such Current Bond its (their) reasonable fees and expenses in this connection.

Section 206. Authentication of Current Bonds. The Current Bonds, after execution by the District, shall be delivered to the Bond Registrar. No Current Bond shall be valid or obligatory for any purpose or be entitled to any security or benefit of this Current Bond Resolution unless and until such Current Bond has been duly authenticated by the Bond Registrar by the execution of the Authentication Certificate of Bond Registrar appearing on such Current Bond. Such Certificate appearing on any Current Bond shall be deemed to have been duly executed by the Bond Registrar if manually signed by an authorized officer of the Bond Registrar. It shall not be required that the same officer of the Bond Registrar sign such Certificate on all of the Current Bonds.

The District shall deliver to the Bond Registrar a sufficient quantity of Current Bonds in blank to enable the Bond Registrar to hold a quantity of Current Bonds in blank, after the initial delivery of the Current Bonds, for future authentication and exchange for such Current Bonds as may be exchanged and transferred from time to time.

Section 207. Disposition of Current Bonds Proceeds. All sums received as accrued interest from the sale of the Current Bonds shall be deposited in the Sinking Fund hereinafter

continued (for payment of interest first due on the Current Bonds) and the remaining Current Bond proceeds shall be applied as follows:

(a) There shall first be paid from the Current Bond proceeds by or on the order of the Chairman the contractual fee of the District's Financial Advisor, the fee and any expenses of the Bond Counsel, Bond Registrar and Paying Agent, all counsel fees and expenses, rating service fees, if any, printing and publication charges and any other necessary or desirable fees and expenses with respect to the issuance of the Current Bonds and the redemption of the Refunded Bonds.

(b) A sufficient portion of the Current Bond proceeds together with such other legally available funds of the District as may be necessary, including such sums previously accrued specifically to pay interest on and all principal of the Refunded Bonds (which funds are hereby appropriated for such purpose), shall be applied to the current refunding, redemption or prepayment and retirement of the Refunded Bonds as herein described, and in this connection each of the Chairman, Secretary and Treasurer is hereby authorized and directed to take all necessary action on behalf of the District to provide for such redemption or prepayment and retirement immediately upon delivery of the Current Bonds, and in any event no later than thirty days thereafter.

(c) A sufficient portion of the Current Bond proceeds together with other available funds of the District as shall be necessary to cause the aggregate amount on deposit in the Reserve Fund hereinafter referred to be equal to the Reserve Amount shall be deposited in the Reserve Fund.

(d) The balance of the Current Bond proceeds, if any, shall be deposited in the Sinking Fund.

Section 208. Application of Remaining Funds Held for Refunded Bonds. The District covenants that simultaneously with the delivery of the Current Bonds and with the written approval of the RD, all amounts remaining in funds and accounts previously created and maintained by the District specifically for payment of principal of and accrued interest on the Refunded Bonds shall be transferred and applied according to the written direction of the Chairman or the Treasurer.

ARTICLE 3. ARBITRAGE LIMITATIONS.

Section 301. Arbitrage Limitations on Investment of Proceeds. The District covenants and certifies, in compliance with the Code, that on the basis of known facts and reasonable expectations on the date of enactment of this Resolution, that it is not expected that the proceeds of the Current Bonds will be used in a manner which would cause the Current Bonds to be "arbitrage bonds" within the meaning of Section 148 of the Code. The District covenants to the Purchaser and/or Owners of the Current Bonds that (1) the District will make no use of the proceeds of said Current Bonds which, if such use had been reasonably expected on the date of issue of such Current Bonds, would have caused such Current Bonds to be "arbitrage bonds" and (2) the District will comply with all of the requirements of the Code to whatever extent is necessary to assure that the Current Bonds shall not be treated as or constitute "arbitrage bonds" and that the interest on the Current Bonds shall be excludable from gross income for Federal income tax purposes.

Prior to or at the time of delivery of the Current Bonds, the Chairman and/or the Treasurer (who are jointly and severally charged with the responsibility for the issuance of the Current Bonds) are authorized to execute the appropriate certification with reference to the matters referred to above, setting out all known and contemplated facts concerning such anticipated construction, expenditures and investments, including the execution of necessary and/or desirable certifications of the type contemplated by Section 148 of the Code in order to assure that interest on the Current Bonds shall be excludable from gross income for Federal income tax purposes and that the Current Bonds will not be treated as "arbitrage bonds".

ARTICLE 4. FLOW OF FUNDS.

Section 401. Flow of Funds. From and after issuance and delivery of the Current Bonds, and so long as any of the Current Bonds or Parity Bonds remain outstanding and unpaid, the System shall continue to be operated on a Fiscal Year basis, and on that basis the income and revenues of the System shall be collected, segregated, accounted for and distributed as follows:

(A) A separate and special fund or account of the District, distinct and apart from all other funds and accounts, was created by the Prior Bond Resolution designated and identified as the District's "Water Revenue Fund", which shall continue to be maintained by the District, and into which shall be deposited all income and revenues of the System (to the extent not otherwise provided to be deposited hereinafter). The moneys in the Revenue Fund from time to time shall be used and disbursed and applied by the District, as permitted by applicable statutes, as follows:

(B) A separate and special fund or account of the District, distinct and apart from all other funds and accounts, was created in and by the Prior Bond Resolution and designated and identified as the "Waterworks Bond and Interest Sinking Fund", which shall continue to be maintained so long as any of the Outstanding Bonds or any additional Parity Bonds herein permitted to be issued are outstanding; and all moneys deposited therein from time to time shall be used and disbursed and applied, and are hereby irrevocably pledged, solely for the purpose of paying the principal of and interest on the Outstanding Bonds and any Parity Bonds hereafter issued and outstanding pursuant to the provisions of this Resolution.

There shall be set aside and transferred on or before the 20th day of each month from the Revenue Fund, as a first charge thereon, and deposited in the Sinking Fund sums sufficient to pay when due the principal and interest requirements on the Outstanding Bonds. Specifically, there shall be paid into the Sinking Fund on or before the 20th day of each month, on account of the Outstanding Bonds, not less than the following:

- (i) a sum which together with other funds available in the Sinking Fund for such purpose will be equal to one-sixth (1/6) of the next succeeding interest installment to become due on all Outstanding Bonds; and
- (ii) a sum which together with other funds available in the Sinking Fund for such purpose will be equal to one-twelfth (1/12) of the principal of all Outstanding Bonds maturing on the next succeeding January 1.

In the event additional Parity Bonds are issued pursuant to the conditions and restrictions hereinafter prescribed, the monthly deposits to the Sinking Fund shall be increased to provide for payment of interest thereon and the principal thereof as the same respectively become due.

If for any reason there should be a failure to pay into the Sinking Fund the full amounts above stipulated, then an amount equivalent to such deficiency shall be set apart and paid into the

Sinking Fund from the first available income and revenues of the System, subject to the aforesaid priorities.

No further payments need to be made into the Sinking Fund if and when the amount held therein and in any other available fund is at least equal to the amount required to retire all Outstanding Bonds and Parity Bonds and paying all interest that will accrue thereon.

(C) A separate and special fund or account of the District, distinct and apart from all other funds and accounts, is hereby created, designated and identified as the "Henry County Water District No. 2 Waterworks Revenue Bond Debt Service Reserve Fund of 1998", which shall continue to be maintained so long as there are outstanding any Parity Bonds herein permitted to be issued on a parity with the Outstanding Bonds, except those Parity Bonds the original purchaser or purchasers of which have waived the benefit of, and any claim to, the Reserve Fund. Parity Bonds which may be issued and outstanding from time to time as hereinafter permitted and with respect to which the original purchaser or purchasers have not waived the benefit of and claim to the Reserve Fund are hereafter referred to as "Qualified Parity Bonds". The holders of the Prior Bonds, have elected, for themselves and on behalf of all subsequent holders of the Prior Bonds, to waive the benefit of and any claim to the Reserve Fund.

All moneys deposited in the Reserve Fund from time to time shall be held and applied, and are hereby irrevocably pledged, solely for the purpose of paying the principal of and interest on the outstanding Qualified Parity Bonds, if any, if and to the extent insufficient funds are available therefor in the Sinking Fund. Whenever the amount in the Reserve Fund is less than the Reserve Amount, the amount necessary to restore balance in the Reserve Fund to the Reserve Amount shall be paid into the Reserve Fund in thirty-six (36) equal monthly installments, each payable on the twentieth (20th) day of the month (except that when the twentieth (20th) day of any month shall be a Sunday or a legal holiday, then such payment shall be made on the next succeeding business day) from the Revenue Fund, after making the deposits set out in subsection (B) above, until the Reserve Amount is on deposit in the Reserve Fund.

Any amount in the Reserve Fund in excess of the Reserve Amount shall be transferred to the Sinking Fund and applied as credit against payments into the Sinking Fund from the Revenue Fund on a monthly basis as described in the foregoing subsection (B).

(D) A separate and special fund or account of the District was created by the Prior Bond Resolution designated and identified as the District's "Depreciation Fund". After observing the priority of deposits set forth in (A) through (C) above, which are cumulative, there shall be set apart and paid into the Depreciation Fund each month, such sum as is required by the Prior Bond Resolution, from the remaining funds in the Revenue Fund, such monthly deposits to continue so long as any Prior Bonds payable from the income and revenues of the System remain outstanding and unpaid or until the minimum balance set forth in said Prior Bond Resolution is reached.

In addition to the above deposits from the Revenue Fund, there shall also be deposited in the Depreciation Fund, as received, the proceeds of all property damage insurance (except public liability) maintained in connection with the System, and the cash proceeds of any surplus, worn-out or obsolescent properties of the System, if the same be sold upon order of the Commission.

The Depreciation Fund shall be available and may be withdrawn and used by the District, upon appropriate certification as to the authorization for such withdrawal, for the purpose of paying the cost of unusual or extraordinary maintenance, repairs, renewals or replacements, and the cost of constructing additions and improvements to the System which will either enhance its revenue-producing capacity or provide a higher degree of service. The Depreciation Fund shall also be available for transfer to the Sinking Fund in order to avoid default in connection with any Outstanding Bonds payable from the Sinking Fund or to redeem or purchase Outstanding Bonds in advance of maturity.

At any time when the accumulations in the Depreciation Fund shall exceed the anticipated current needs for authorized purposes, all or any portion of such excess may be invested and reinvested upon order of the Commission in Permitted Investments maturing or subject to redemption at the option of the holder not later than the time anticipated to be needed by the District, but in any event not later than five (5) years after the date of investment; but as and when funds may be required for authorized purposes a sufficient portion thereof shall be converted into cash and so applied. All investments of money in the Depreciation Fund shall be carried to the credit of the Depreciation Fund; all income from investments and any profit from the sale thereof shall be credited thereto; and any expenses incident to investment or reinvestment, together with any loss from forced conversion of investments into cash, shall be charged thereto.

(E) A separate and special fund or account of the District was created by the Prior Bond Resolution designated the District's "Operation and Maintenance Fund", which shall continue to be maintained for the benefit of the System and all Outstanding Bonds payable from the income and revenues of the System. The District covenants that it will transfer monthly from the moneys in the Revenue Fund, after making the transfers required by (A) through (E) above, to the Operation and Maintenance Fund sums sufficient to pay as they accrue the Current Expenses of operating and maintaining the System pursuant to the Proposed Budget, for which provision is hereafter made, and to accrue an operation and maintenance reserve not in excess of anticipated requirements for a two-month period pursuant to the Proposed Budget.

At any time when the accumulations in the Operation and Maintenance Fund shall exceed the anticipated current needs for authorized purposes, all or any portion of such excess may be invested and reinvested upon order of the Commission in Permitted Investments maturing or subject to redemption at the option of the holder not later than the time anticipated to be needed by the District, but in any event not later than ninety (90) days after the date of investment; but as and when funds may be required for authorized purposes a sufficient portion thereof shall be converted into cash and so applied. All investments of money in the Operation and Maintenance Fund shall be carried to the credit of the Operation and Maintenance Fund; all income from investment or

reinvestment, together with any loss from forced conversion of investments into cash, shall be charged thereto.

(F) All moneys held in the Revenue Fund, the Sinking Fund, the Reserve Fund and the Depreciation Fund shall be deposited in a bank or banks which are members of the FDIC, and all such deposits which cause the aggregate deposits of the District in any one bank to be in excess of the amount insured by FDIC shall be continuously secured by a valid pledge of direct obligations of the United States of America having an equivalent market value. All or any part of the Revenue Fund and the Sinking Fund shall be continuously secured by a valid pledge of direct obligations of the United States of America having an equivalent market value. All or any part of the Revenue Fund and the Sinking Fund may, and the Reserve Fund shall, be invested in Permitted Investments, as hereinafter defined, maturing or being subject to retirement at the option of the holder on such dates as the same may be needed for meeting interest and/or principal payments, and all such investments shall be carried to the credit of the Fund which supplied the funds for such investments, and the income from such investments shall be credited to the Sinking Fund; provided, however, if the amount in the Reserve Fund is less than the Reserve Amount, income from investments in the Reserve Fund shall be credited to the Reserve Fund until the Reserve Amount is accumulated therein. Permitted Investments in the Reserve Fund shall be valued at cost.

Investment income accruing to the Sinking Fund shall be credited against payments into the Sinking Fund from the Revenue Fund on a monthly basis as set out in the foregoing subsection (B) hereof.

(G) Subject to the provisions of subsections (A) through (F) above, which are cumulative, and after paying or providing for the payment of debt service on any subordinate obligations, there shall be transferred within sixty (60) days after the end of each Fiscal Year the balance of excess funds in the Revenue Fund on such date to the District's General Fund.

All payments into the above special funds shall be made on or before the twentieth (20th) day of each month, except that when the twentieth (20th) day of any month shall be a Sunday or a legal holiday, then such payment shall be made on the next succeeding business day.

All moneys held in any of the above special funds shall be kept apart from all other District funds and shall be deposited in the Depository Bank, and all such deposits which cause the aggregate of all deposits of the District in any Depository Bank to be in excess of the amount secured by FDIC shall (unless invested as herein authorized) be secured by a surety bond or bonds or by pledge of direct obligations or by guaranteed bonds or securities of the United States Government having a market value at least equivalent to such excess deposit.

Section 402. Current Bonds on a Parity with Outstanding Bonds. It is hereby certified and declared that prior to the issuance of any of the Current Bonds, there will have been procured and filed with the District (i) a certificate from the RD to the effect that the RD agrees to the issuance of the Current Bonds ranking on a parity as to security and source of payment with the Bonds of

1967, Bonds of 1974 and Bonds of 1996, all of which are owned by the RD, together with (ii) a certification signed by the RD to the effect that a legend has been typed, stamped or otherwise affixed on each of the Bonds of 1967, Bonds of 1974 and Bonds of 1996 held by the RD, evidencing the agreement of the RD as the then Owner of the Bonds of 1967, Bonds of 1974 and Bonds of 1996, to the issuance of the Current Bonds so as to rank on a parity with the Bonds of 1967, Bonds of 1974 and Bonds of 1996, such legend to be in substantially the following form:

The holder of this Bond has consented to the issuance of \$8,470,000 of Henry County Water District No. 2 Waterworks Refunding Revenue Bonds, Series 1998, ranking on a parity as to security and source of payment with this Bond.

It is also hereby certified and declared that prior to the issuance of any of the Current Bonds, there will have been procured and filed with the District a certificate from the SRECC to the effect that the SRECC agrees to the issuance of the Current Bonds ranking on a parity as to security and source of payment with the SRECC Note.

Accordingly, it is hereby found and declared that the Current Bonds shall rank and be payable on a parity with the Prior Bonds from the gross income and revenues of the System.

ARTICLE 5. COVENANTS OF DISTRICT.

Section 501. Rates and Charges. The District covenants that while the Current Bonds remain outstanding and unpaid, such rates and charges for services of the System will be imposed and collected so that the gross income and revenues of the System will be sufficient to provide for all principal and interest requirements of all Outstanding Bonds, to provide for all expenses of operation, repair, maintenance and insurance, of the System and to produce net revenues in each year equal to not less than 120% of the average annual principal and interest requirements of all Outstanding Bonds, calculated in the manner (and with the defined terms) specified in Section 602 hereof, authorizing the issuance of future Parity Bonds, except that for the purpose of such calculation, no adjustment shall be permitted for future projections or for any other matter; and the District shall enact promptly and enforce increased rates whenever such increase shall be necessary to fulfill any covenants of or payments required by this Resolution.

The District covenants that it will not reduce the rates and charges for services rendered by the System without first filing with the Secretary a certification of an Independent Consulting Engineer to the effect that the annual net revenues (defined as gross revenues less essential operation and maintenance expenses) of the then existing System for the fiscal year preceding the date on which such reduction is proposed, as such annual revenues are adjusted, after taking into account the projected reduction in revenues anticipated to result from such proposed rate decrease, are equal to not less than 120% of the average annual debt service requirements falling due in any year thereafter, calculated in the manner specified in Section 602 hereof.

The District also covenants to cause a coverage report to be filed with the Governing Body within four months after the end of each fiscal year by Certified Public Accountants and/or Independent Consulting Engineers, setting forth what was the precise percentage of the average annual debt service requirements falling due thereafter for principal of and interest on all of the then Outstanding Bonds payable from the revenues of the System, calculated in the manner specified in Section 602 hereof; and the District covenants that if and whenever such report so filed shall establish that such coverage of net revenues for such year was less than 120% of the average future annual debt service requirements, the District shall increase the rates by an amount sufficient, in the opinion of such Certified Public Accountants and/or Independent Consulting Engineers, to establish the existence of or immediate projection of, such minimum 120% coverage.

Section 502. Books and Accounts; Audit. The District covenants to maintain proper records and accounts relating to the operation of the System and the District's financial affairs; and the Owners of any of the Current Bonds, or their authorized representatives, shall have the right at all reasonable times to inspect the facilities of the System and all records, accounts and data relating thereto. An annual audit shall be made of the books and accounts pertinent to the System by a Certified Public Accountant licensed in Kentucky. No later than ninety days after the close of each Fiscal Year, copies of such audit reports certified by such Certified Public Accountant shall be promptly mailed to any Bondowner that may have made a written request for same.

Section 503. System to Continue to be Operated on Fiscal Year Basis; Annual Budget.

While any of the Current Bonds, and any Parity Bonds are outstanding and unpaid, and to the extent permitted by law, the System shall continue to be operated and maintained on a Fiscal Year basis.

Not later than sixty days after the end of each Fiscal Year, beginning immediately after the issuance of the Current Bonds, the District agrees to cause to be prepared a detailed statement of income and expenditures for the Fiscal Year, a current financial statement and a proposed annual budget of current expenses (the "Proposed Budget") of the System for the then ensuing Fiscal Year, itemized on the basis of monthly requirements. A copy of said Proposed Budget shall be mailed to any Bondowner who may request in writing a copy of such Proposed Budget.

For the purpose of the Proposed Budget, current expenses shall include all reasonable and necessary expenses of operating, repairing, maintaining and insuring the System, but shall exclude depreciation and payments into the Sinking Fund, the Reserve Fund, the Depreciation Fund. The District covenants that the current expenses incurred in any year will not exceed the reasonable and necessary amounts therefor, and that the District will not expend any amount or incur any obligation for operation or maintenance and repair in excess of the amounts provided for current expenses in the annual budget, except upon resolution by the District that such expenses are necessary to operate and maintain the System.

Not later than sixty days after the end of each Fiscal Year, the District shall prepare an estimate of gross revenues to be derived from the operation of the System for said Fiscal Year, and, to the extent that said gross revenues are insufficient (a) to pay debt service requirements on all Outstanding Bonds during the ensuing Fiscal Year, (b) to accumulate and maintain all required reserves enumerated herein and (c) to pay current expenses, the District shall revise the rates and charges sufficiently to provide the funds required.

If the Owners of at least 50% of the principal amount of the Outstanding Bonds, or the Government so long as it is the Owner of any of said Outstanding Bonds, so request, the District Council shall hold an open hearing not later than thirty days before the beginning of the ensuing Fiscal Year, at which time any Bondowner may appear by agent or attorney and may file written objections to such proposed budget. Notice of the time and place of such hearing shall be mailed at least fifteen days prior to the hearing to each registered Bondowner and to the Government.

The District covenants that annually before the first day of December, the annual budget for the then current Fiscal Year will be adopted substantially in accordance with the Proposed Budget, and that no expenditures for operation and maintenance expenses of the System in excess of the budgeted amount shall be made during such Fiscal Year unless directed by said District by a specific resolution duly adopted.

Section 504. General Covenants. The District, through its Commission, hereby covenants and agrees with the Owners of the Current Bonds that:

- (1) It will faithfully and punctually perform all duties with reference to the System required by the Constitution and laws of the Commonwealth of Kentucky;
- (2) It will make and collect reasonable and sufficient rates and charges for services and facilities rendered by the System;
- (3) It will segregate the revenues and income from the System and make application thereof consistent with and as provided by this Resolution;
- (4) Unless the written consent of the Owners of a majority of the principal amount of the Outstanding Bonds has been obtained, the District agrees not to sell, lease, mortgage or in any manner dispose of any integral part of the System, including any and all appurtenances thereto and extensions, additions and improvements that may be made thereto, until all of the Outstanding Bonds shall have been paid or provided for in full, as provided herein; subject to the provisions of Section 607 hereof;
- (5) It will maintain in good condition and continuously operate the System and appurtenances thereto and will charge such rates and charges for the services rendered thereby so that the gross income and revenues will be sufficient at all times (i) to pay the interest on and principal of the Outstanding Bonds as same become due, (ii) to pay the cost of operating and maintaining the System, and (iii) to provide for an adequate depreciation account; and
- (6) It will carry and maintain insurance on properties of the System subject to loss or damage in amounts and against hazards substantially in accordance with the practices of other districts, cities or corporations which own and maintain waterworks systems under similar conditions; and so long as the Government is the Owner of any of the Outstanding Bonds, the Government will be listed as co-beneficiary on any such policy; and the District shall further comply with the insurance requirements of Section 505 hereof (involving insurance on motors, tanks and structures); and

Section 505. Insurance on Motors, Tanks and Structures. If and to the extent not now fully required by the Prior Bond Resolution, the District shall immediately after the adoption of this Resolution insure all electric motors, pumping stations and major structures of the System in an amount recommended by an Independent Consulting Engineer for the hazards usually covered in such area.

ARTICLE 6. INFERIOR BONDS AND PARITY BONDS.

Section 601. Inferior Bonds. Except as provided below in this Article, the District shall not, so long as any of the Current Bonds and/or Parity Bonds are outstanding, issue any additional bonds payable from the revenues of the System unless the security and/or pledge of the revenues to secure such additional bonds are made inferior and subordinate in all respects to the security of the Current Bonds and any Parity Bonds.

The District expressly reserves the right at any time to issue its bonds or other obligations payable from the revenues of the System and not ranking on a parity basis with the Current Bonds, without any proof of previous earnings or net revenues, provided that the consent of the RD must be obtained prior to the issuance of any inferior bonds so long as the RD owns any of the Outstanding Bonds, and provided further that, such inferior bonds may be issued only for the purpose of providing for future extensions, additions and improvements to the System, and only in express recognition of the priorities, liens and rights created and existing for the security, source of payment and protection of the Outstanding Bonds; provided further, that nothing in this Section is intended to restrict or shall be construed as a restriction upon, the ordinary refunding of the Outstanding Bonds.

Section 602. Parity Bonds to Finance Future Improvements. The District reserves the right and privilege, of issuing additional Parity Bonds, but only under the following conditions:

The District further reserves the right to add new combined and consolidated water and sewer facilities and/or to finance future extensions, additions and improvements to the System by the issuance of one or more additional series of Parity Bonds to be secured by a parity lien on and ratably payable on a parity with the Outstanding Bonds, from the revenues of the System, provided:

(a) The facilities to be constructed from the proceeds of the additional Parity Bonds are made a part of the System and their revenues are pledged as additional security for the additional Parity Bonds and for the Outstanding Bonds.

(b) The District is in compliance with all covenants and undertakings in connection with all of the Outstanding Bonds.

(c) The annual net revenues (defined as gross revenues less operation expenses), of the then existing System for the Fiscal Year preceding the year in which such Parity Bonds are to be issued, adjusted as hereinafter provided, shall be certified by an independent Certified Public Accountant to be equal at least one hundred twenty percent (120%) of the average annual debt service requirements for principal and interest on all Outstanding Bonds payable from the revenues of the System, including such requirements of the Current Bonds, any Parity Bonds then outstanding plus the anticipated debt service requirements of any Parity Bonds then proposed to be issued. The calculation of average annual debt service requirements of principal and interest on the additional Parity Bonds to be issued shall,

regardless of whether such additional Parity Bonds are to be serial or term bonds, be determined on the basis of the principal of and interest on such Parity Bonds being payable in approximately equal annual installments.

(d) The annual net revenues referred to above may be adjusted for the purpose of the foregoing computations to reflect:

(1) any revisions in the System's schedule of rates or charges being imposed at the time of the issuance of any such additional Parity Bonds, and

(2) any increase in the annual net revenues to be realized from the proposed extensions, additions and improvements being financed (in whole or in part) by such additional Parity Bonds;

provided all such adjustments shall be based upon and included in a certification of an Independent Consulting Engineer.

The District hereby further reserves the right and privilege of issuing additional Parity Bonds for the purpose of refunding any of the Outstanding Bonds and any additional Parity Bonds, or any portion thereof, as may be outstanding, provided that before any additional Parity Bonds are issued for such purpose, there shall have been procured and filed with the Secretary of the District either (a) the written consent of the holders of all Outstanding Bonds and any additional Parity Bonds (other than the bonds being refunded) to such issuance or (b) a statement by an independent Certified Public Accountant reciting the opinion based upon necessary investigation that after the issuance of such additional Parity Bonds, the net income and revenues, as adjusted and defined above, of the System for the fiscal year preceding the date of issuance of such additional Parity Bonds, after taking into account the revised maximum annual debt service resulting from the issuance of such additional Parity Bonds and from the elimination of the bonds being refunded, are equal to not less than 120% of the maximum annual debt service requirement for any year ending January 1 with respect to the Outstanding Bonds and any additional Parity Bonds then outstanding and the proposed additional Parity Bonds and calculated in the manner specified above.

The original purchaser or purchasers of a series of additional Parity Bonds may waive the benefit of and any claim to the Reserve Fund, in which event such bonds shall not be secured by or payable from the Reserve Fund; and the District may make it a condition to the original sale of any series of additional Parity Bonds that the purchaser or purchasers thereof, by offering to purchase or by purchasing the same, has agreed to such waiver.

Section 603. Covenants to be Complied with at Time of Issuance of Parity Bonds. The District hereby covenants and agrees that in the event any Parity Bonds are issued, the District shall:

(a) Adjust the monthly amount to be deposited into the Sinking Fund on the same basis as that prescribed in the provisions establishing such Sinking Fund, to reflect the average annual debt service requirements of the Parity Bonds;

(b) Adjust the minimum annual amount to be deposited monthly into the Depreciation Fund on the same basis as that prescribed in the provisions establishing such Depreciation Fund, taking into account the future debt service requirements of all bonds payable out of the Sinking Fund which will then be outstanding against the System; and

(c) Make such Parity Bonds payable as to principal on January 1 of each year in which principal falls due and payable as to interest on January 1 and July 1 of each year until the final maturity of such Parity Bonds.

Section 604. Prepayment Provisions Applicable to Parity Bonds. If, in connection with any subsequently issued series of Parity Bonds, it is provided that excess revenues in the Revenue Fund shall be used to prepay Outstanding Bonds in advance of scheduled maturity, or if the District at its option undertakes to prepay Outstanding Bonds in advance of scheduled maturity, it is agreed and understood, for so long as the Government owns any of the Outstanding Bonds, that no such prepayment will be effected without the approval of the RD.

Section 605. Priority of Lien; Permissible Disposition of Surplus or Obsolete Facilities. The District covenants and agrees that so long as any of the Current Bonds are outstanding, the District will not sell or otherwise dispose of any of the facilities of the System, or any part thereof, and, except as provided above, the District will not create or permit to be created any charge or lien on the revenues thereof ranking equal or prior to the charge or lien of the Current Bonds. Notwithstanding the foregoing, the District may at any time permanently abandon the use of, or sell at fair market value, any part of the facilities of the System, provided that:

- (a) The District is in compliance with all covenants and undertakings in connection with all of the Outstanding Bonds, and the required reserves for such Outstanding Bonds will have been accumulated;
- (b) The District will, in the event of any such sale, apply the proceeds to either (1) redemption of Outstanding Bonds in accordance with the provisions governing prepayment of bonds in advance of maturity or (2) replacement of the facility so disposed of by another facility, the revenues of which shall be incorporated into the System, as hereinbefore provided;
- (c) The District certifies, in good faith, prior to any abandonment of use, that the facilities to be abandoned are no longer economically feasible of producing net revenues; and

- (d) The District certifies, in good faith, that the estimated net revenues of the remaining facilities of the System for the then next succeeding Fiscal Year, plus the estimated net revenues of the facilities, if any, to be added to the System, comply with the earnings requirements hereinbefore provided in the provisions and conditions governing the issuance of Parity Bonds.

ARTICLE 7. DEFAULT AND CONSEQUENCES.

Section 701. Events of Default. The following items shall constitute an Event of Default on the part of the District:

- (a) The failure to pay principal of the Current Bonds as and when same shall become due and payable, either at maturity or by proceedings for redemption.
- (b) The failure to pay any installment of interest on the Current Bonds when the same shall become due and payable.
- (c) The default by the District in the due or punctual performance of any of the covenants, conditions, agreements and provisions contained in the Current Bonds or in this Resolution.
- (d) The failure to promptly repair, replace or reconstruct facilities of the System that have been damaged and/or destroyed.
- (e) The entering of any order or decree with the consent or the acquiescence of the District, appointing a receiver of all or any part of the System or any revenues thereof; or if such order or decree shall be entered without the acquiescence or consent of the District, its failure to have the order vacated, discharged or stayed on appeal within 60 days after entry.

Section 702. Consequences of Event of Default. Any Owner of the Current Bonds may enforce and compel the performance of all duties and obligations of the District set forth herein. Upon the occurrence of an Event of Default, then upon the filing of a suit by any Owner of said Bonds, any court having jurisdiction of the action may appoint a receiver to administer said System on behalf of the District with power to charge and collect rates sufficient to provide for the payment of operating and maintenance expenses and for the payment of principal of and interest on the Current Bonds and to provide and apply the income and revenues in conformity with this Resolution and with the laws of the Commonwealth of Kentucky.

The District hereby agrees to transfer to any bona fide receiver or other subsequent operator of the System, pursuant to any valid court order in a proceeding brought to enforce collection or payment of the District's obligations, all contracts, and other rights of the District pertaining to the System, conditionally, for such time only as such receiver or operator shall operate by authority of the court. Upon the occurrence of an Event of Default, the Owner of any of the Bonds may require the governing body of the District by appropriate order to raise the rates a reasonable amount consistent with the requirements of this Resolution.

ARTICLE 8. CONTRACTUAL PROVISIONS; MISCELLANEOUS PROVISIONS.

Section 801. Resolution Contractual with Bondowners. The provisions of this Current Bond Resolution shall constitute a contract between the District and the Owners of the Current Bonds, and after the issuance of any of the Current Bonds, no change, variation or alteration of any kind, in the provisions of this Current Bond Resolution shall be made in any manner, except for the purpose of curing any ambiguity or of curing, correcting, or supplementing any defective or inconsistent provisions contained herein or in any proceeding pertaining hereto, and except as herein provided, until such time as all of the Current Bonds and the interest thereon have been paid in full; provided, however, that the Owners of eighty percent (80%) in principal amount of the Current Bonds may agree to a modification or amendment to this Current Bond Resolution; provided, however, that no such modifications or amendments shall be made which will permit: (a) an extension of the maturity of any of the Current Bonds or of any Parity Bonds, (b) a reduction in the principal amount of any Current Bond or the redemption price or the rate of interest thereon, (c) the creation of a lien upon or a pledge of revenues ranking prior to or on a parity with the lien or pledge of the Current Bonds, (d) a preference or priority of any Current Bonds or Parity Bonds over any other bond or bonds, (e) a reduction in the aggregate principal amount of the Current Bonds required to consent to any such modification or amendment, or (f) impair in any way the rights of the Owners of the Current Bonds.

Section 802. All Current Bonds are Equal. The Current Bonds authorized herein shall not be entitled to priority one over the other in the application of the income and revenues of the System, or with respect to the security for their payment, regardless of the time or times of their issuance, it being the intention that there shall be no priority among any of the Current Bonds regardless of the fact that they may be actually issued and delivered at different times.

Section 803. Signatures of Officers. If any of the officers whose signatures or facsimile signatures appear on the Current Bonds cease to be such officers before delivery of the Current Bonds, such signatures shall nevertheless be valid for all purposes the same as if said officers had retained in office until delivery, as provided in KRS 58.040 and KRS 61.390.

Section 804. Appointment and Duties of Bond Registrar, Transfer Agent, and Paying Agent. The Fifth Third Bank, Cincinnati, Ohio, is hereby designated as the Bond Registrar, Transfer Agent and Paying Agent.

A. Duties as Bond Registrar and Transfer Agent. The Bond Registrar and Transfer Agent shall have the following duties

- (1) To authenticate the Current Bonds authorized herein.
- (2) To register all of the Current Bonds in the names of the respective owners thereof;

(3) Upon being supplied with a properly authenticated assignment satisfactory to the Bond Registrar (in the sole discretion of such Bond Registrar), to transfer the ownership of Current Bonds from one registered Bondowner to another within three (3) business days of the receipt of such proper assignment by the Bond Registrar; and

(4) To cancel and destroy (or remit to the District for destruction, if so requested by the District) all exchanged, matured, retired and redeemed Current Bonds, and to maintain adequate records relevant thereto.

B. Duties as Paying Agent. The Paying Agent shall have the following duties:

(1) To hold the Sinking Fund in accordance with the provisions of hereof;

(2) To remit, but only to the extent that all required funds are made available to the Paying Agent by the District, semiannual interest payments directly to the registered owner of each Bond by regular United States mail. Said interest payments shall be deposited in the United States mail no later than each interest due date. Matured or redeemed Bonds shall be payable upon presentation to the Paying Agent. For interest payment purposes, the Paying Agent shall be entitled to rely on its records as Bond Registrar as to the ownership of each Bond as of the 15th day of the month preceding an interest due date, and the Paying Agent's check shall be drawn and mailed accordingly;

(3) To notify the Owner of each Current Bond to be redeemed and to redeem Bonds prior to their stated maturity upon their presentation in accordance with the provisions of this Current Bond Resolution upon receiving, sufficient funds; and

(4) To supply the District with a written accounting evidencing the payment of interest on and principal of the Current Bonds within 30 days following each respective due date.

The Bond Registrar/Paying Agent shall be entitled to the advice of counsel and shall be protected for any acts taken by it in good faith in reliance upon such advice. The Bond Registrar/Paying Agent shall not be liable for any actions taken in good faith and believed by it to be within its discretion or the power conferred upon it by this Current Bond Resolution, or the responsibility for the consequences of any oversight or error of judgment.

The Bond Registrar/Paying Agent may at any time resign from its duties set forth in this Current Bond Resolution by filing its resignation with the Secretary and notifying the Purchaser of the Bonds. Thereupon, the District shall designate a successor Bond Registrar/Paying Agent which shall be an incorporated bank or trust company authorized to transact business in the United States of America. Notwithstanding the foregoing, in the event of the resignation of the Bond Registrar/Paying Agent, provision shall be made for the orderly transition of the books, records and

accounts relating to the Current Bonds to the successor Bond Registrar/Paying Agent in order that there will be no delinquencies in the payment of interest or principal due on the Current Bonds.

The Bond Registrar/Transfer Agent/Paying Agent shall indicate its acceptance of its duties as Bond Registrar, Transfer Agent and Paying Agent by signing the acceptance at the conclusion of this Current Bond Resolution.

ARTICLE 9. SALE OF CURRENT BONDS.

Section 901. Sale of Current Bonds. The Current Bonds shall be offered publicly for sale upon the basis of sealed, competitive bids at such time as the District shall designate.

A suggested form of "Notice of Bond Sale", a suggested form of "Official Notice of Sale of Bonds" and a suggested form of "Bid Form", having been prepared in advance by Bond Counsel, and all of such documents having been found to be in satisfactory form, the same are hereby approved, and a copy of each is hereby ordered to be filed in the records of the Secretary with the Minutes of the meeting at which this Resolution is enacted. The Notice of Bond Sale shall be signed by the Secretary and may be used for the purpose of publishing notice of the sale of the Current Bonds. Copies of such documents shall be furnished to any interested parties who may request same.

In the event that there is no bid or that all bids are rejected, the District may readvertise the sale pursuant to this Resolution.

ARTICLE 10. CONCLUDING PROVISIONS.

Section 1001. Covenant of District to Take All Necessary Action To Assure Compliance with Internal Revenue Code. In order to assure the Purchaser and any subsequent owner of the Current Bonds that such Current Bonds shall continue to be legal and that interest thereon will continue to be excludable from gross income for Federal income tax purposes and exempt from all Kentucky income taxation, the District covenants to and with the owners of the Current Bonds to take the following action:

(a) The District will (1) take all actions necessary to comply with the provisions of the Code necessary to assure that interest on the Current Bonds will be excludable from gross income for Federal income tax purposes, (2) will take no actions which will violate any of the provisions of the Code, and (3) not use the proceeds of the Current Bonds for any purpose which will cause interest on the Current Bonds to become includable in gross income for Federal income tax purposes.

(b) The District hereby certifies that it does not reasonably anticipate that the total principal amount of "qualified tax-exempt obligations" within the meaning of Section 265(b)(3) of the Code which the District, or any subordinate entity of the District, will issue during the calendar year during which the Current Bonds are issued, will exceed \$10,000,000; and therefore the District hereby designates the Current Bonds as "qualified tax-exempt obligations".

(c) Within the meaning of Section 141 of the Code, (i) less than 10% of the proceeds of the Current Bonds, if any, will be applied for any private business use, and the payment of principal of or interest on less than 10% of the amount of the Current Bonds, if any, will be secured directly or indirectly by any interest in property used for a private business use, or payments in respect of such property, or will be derived from payments in respect of such property; (ii) at least 90% of the proceeds of the Current Bonds will be applied for a governmental use of the District; (iii) any private business use of the System will be related to such governmental use of the District and will not be unrelated or disproportionate; and (iv) none of the proceeds of the Current Bonds will be used, directly or indirectly, to make or finance loans to private persons.

(d) The Current Bonds are not federally guaranteed within the meaning of Section 149(b) of the Code.

(e) The District will comply with the information reporting requirements of Section 149(e) of the Code.

(f) The District covenants and agrees to comply with the rebate requirements on certain excess earnings imposed by Section 148 of the Code, and in the event it is determined by the District, upon the advice of Bond Counsel, that any Fund established hereunder, is

subject to said rebate requirements and does in fact generate earnings from "non-purpose investments" in excess of the amount which said investments would have earned at a rate equal to the "yield" on the Current Bonds, plus any income attributable to such excess, there shall be established a separate and special fund with the Depository Bank, which fund shall be designated the "Excess Earnings and Rebate Fund", which shall be utilized for the collection and payment and special fund with the Depository Bank, which fund shall be designated the "Excess Earnings and Rebate Fund", which shall be utilized for the collection and payment of any excess generated from investments and the remittance thereof to the United States of America on or before the anniversary of the fifth (5th) year from the date of the Current Bonds, and once every five (5) years thereafter until the final retirement of the Current Bonds; the last installment, to the extent required, to be made no later than sixty (60) days following the date on which the funds sufficient for the complete retirement of the Current Bonds are deposited with any escrow agent. The District further covenants to file any and all reports, if any, as may be required to be filed with the Government with regard to the liability or non-liability of the District as to any such rebate requirements and to maintain records in regard thereto for the period of time required by applicable Treasury regulations.

Section 1002. Annual Disclosure Requirements. In accordance with the requirements of Rule 15c2-12 (the "Rule") promulgated by the Securities and Exchange Commission (the "SEC"), the District agrees to provide or cause to be provided through a designated agent (the "Agent"), in a timely manner, to (i) each nationally recognized municipal securities information repository ("NRMSIR") designated by the SEC in accordance with the Rule or to the Municipal Securities Rulemaking Board ("MSRB") and (ii) the appropriate state information depository ("SID"), if any, designated by the Commonwealth of Kentucky, notice of the occurrence of any of the following events with respect to the Current Bonds, if such event is material:

- (a) principal and interest payment delinquencies;
- (b) non-payment related defaults;
- (c) unscheduled draws on debt service reserves reflecting financial difficulties;
- (d) unscheduled draws on credit enhancements reflecting financial difficulties;
- (e) substitution of credit or liquidity providers, or their failure to perform;
- (f) adverse tax opinion or events affecting the tax-exempt status of the Current Bonds;
- (g) modifications to rights of the Bondholders;
- (h) Current Bond calls;
- (i) defeasances;
- (j) release, substitution or sale of property securing repayment of the Current Bonds; and/or
- (k) rating changes.

The District may from time to time choose to provide notice of the occurrence of certain other events, in addition to those listed above, if the District determines that such other event is

material with respect to the Current Bonds, but the District does not undertake to commit to provide any such notice of the occurrence of any material event except those events listed above.

The District shall make publicly available the financial information and operating data on the System. Such information may be obtained from the District Manager, P.O. Box 219, Campbellsburg, Kentucky 40011, telephone: (502) 532-6279.

The District also agrees to provide to each nationally recognized NRMSIR and to the SID, if any, for the Commonwealth of Kentucky, in each case as designated by the SEC in accordance with the Rule, its audited financial statements prepared in accordance with generally accepted auditing standards and Government Auditing Standards issued by the Comptroller General of the United States and the American Institute of Certified Public Accountants' Audit and Accounting Guide, Audits of State and Local Governmental Units, and certain annual financial data and operating data, similar to that contained in Appendix A of the Official Statement. Such information is expected to be available with respect to the fiscal year of the District ending December 31, 1998 and each fiscal year thereafter no later than the following April 1st of each respective year commencing April 1, 1999.

If the District is unable to provide to each NRMSIR or the MSRB and the SID, if any, the required financial information by the date required in the Continuing Disclosure Certificate, the District shall send a notice to each NRMSIR, the MSRB, and the SID, if any, notifying them of the inability, at that time, to file such financial information.

If the District's fiscal year changes, the District shall send a notice of such change to each NRMSIR or the MSRB and the SID, if any. If such change will result in the District's fiscal year ending on a date later than the ending date prior to such change, the District shall provide notice of such change to each NRMSIR or the MSRB, and the SID, if any, on or prior to the deadline for filing the required financial information in effect when the District operated under its prior fiscal year. Such notice may be provided to each NRMSIR or the MSRB and the SID, if any, along with the required financial information, provided that it is filed at or prior to the deadline described above.

As of the date of this Resolution, the District is in compliance with the reporting requirements of the Rule for all undertakings for which they are an "obligated person" as defined in the Rule.

The obligations of the District described above will remain in effect only for such period that (i) the Bonds are outstanding in accordance with their terms and (ii) that the District remains an obligated person with respect to the Bonds within the meaning of the Rule. The District reserves the right to terminate its obligation to provide notices of material events, as set forth above, if and when the District no longer remains an obligated person with respect to the Bonds within the meaning of the Rule. The District acknowledges that its undertaking pursuant to the Rule described under this Section is intended to be for the benefit of the Bondholders (including holders of beneficial interests in the Bonds).

Notwithstanding any other provision of this Resolution, this Section may be amended, if the District receives an opinion of independent legal counsel to the effect that:

- (i) such amendment is made in connection with a change in circumstances that arises from a change in legal requirements, a change in law or a change in the types of activities in which the District is engaged;
- (ii) this Section as so amended, would have complied with the requirements of the Rule at the time of the primary offering of the Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and
- (iii) such amendment does not materially impair the interests of the Bondholders.

In the event of a failure of the District to comply with any provision of this Section, any Bondholder may take such actions as may be necessary and appropriate, including seeking mandamus or specific performance by court order, to cause the District to comply with its obligations under this Section. A default under this Section shall not be deemed an Event of Default under this Resolution, and the sole remedy under this Section in the event of any failure of the District to comply with this Section shall be an action to compel performance.

Section 1003. Severability Clause. If any section, paragraph, clause or provision of this Resolution shall be held invalid, the invalidity of such section, paragraph, clause or provision shall not affect any of the remaining provisions of this Resolution, which shall continue in full force and effect.

Section 1004. All Provisions in Conflict Repealed. All motions, resolutions and orders, or parts thereof, in conflict with the provisions of this Resolution, are to the extent of such conflict hereby repealed. It is hereby specifically ordered and provided that any proceedings heretofore taken for the issuance of other bonds of the District payable or secured in any manner by all or any part of the income and revenues of said System or any part thereof, and which have not been heretofore sold, are hereby revoked and rescinded, and none of such other bonds shall be issued and delivered. The District covenants to correct by appropriate proceedings any required procedure previously taken invalidly.

Section 1005. Effective Date. This Resolution shall take effect upon its adoption and publication by title and summary, as provided by law.

Adopted on September 23, 1998.

Henry County Water District No. 2

William P. Hawthorne
Chairman

(Seal of District)

Attest:

Merle Brewer
Secretary

CERTIFICATION

I, the undersigned, hereby certify that I am the duly qualified and acting Secretary of the Henry County Water District No. 2, and that the foregoing Resolution is a true copy of a Resolution duly adopted by the Commission of said District, signed by the Chairman of said District and attested under Seal by me as Secretary, at a properly convened meeting of said Commission held on September 23, 1998, as shown by the official records of said District in my custody and under my control.

I further certify that said meeting was duly held in accordance with all applicable requirements of Kentucky law, including KRS 61.810, 61.815, 61.820 and 61.825, that a quorum was present at said meeting, that said Resolution has not been modified, amended, revoked or repealed, and that same is now in full force and effect.

IN TESTIMONY WHEREOF, witness my signature as Secretary and the official Seal of the District this September 23, 1998.

Merle Brewer
Secretary

(Seal of District)

ACCEPTANCE BY THE FIFTH THIRD BANK
BOND REGISTRAR, TRANSFER AGENT, AND PAYING AGENT

The undersigned, The Fifth Third Bank, hereby agrees to the provisions of the foregoing Resolution to the extent there are contained therein provisions as to the rights and duties of it as Bond Registrar, Transfer Agent and Paying Agent.

Dated: September 23, 1998.

The Fifth Third Bank

By Fred T. Overbeck
Signature

Assistant Vice President
Title

EXHIBIT A

Maturity Schedule

<u>Maturity Date</u> <u>January 1</u>	<u>Principal</u> <u>Maturity*</u>	<u>Maturity Date</u> <u>January 1</u>	<u>Principal</u> <u>Maturity*</u>
1999	\$160,000	2014	\$265,000
2000	155,000	2015	280,000
2001	165,000	2016	295,000
2002	170,000	2017	310,000
2003	170,000	2018	325,000
2004	165,000	2019	345,000
2005	170,000	2020	365,000
2006	175,000	2021	385,000
2007	185,000	2022	405,000
2008	195,000	2023	430,000
2009	205,000	2024	455,000
2010	215,000	2025	480,000
2011	225,000	2026	455,000
2012	235,000	2027	480,000
2013	250,000	2028	355,000

*subject to adjustment

UNITED STATES OF AMERICA
COMMONWEALTH OF KENTUCKY
HENRY COUNTY WATER DISTRICT NO. 2
WATERWORKS REFUNDING REVENUE BOND
SERIES 1998

NO. _____

DOLLARS \$ _____

DATE OF ORIGINAL ISSUE: October 1, 1998

INTEREST RATE: MATURITY DATE: CUSIP:

REGISTERED OWNER:

PRINCIPAL AMOUNT:

KNOW ALL MEN BY THESE PRESENTS: That the Henry County Water District No. 2 (the "District"), in the Commonwealth of Kentucky, for value received, hereby promises to pay to the Registered Owner named above, or registered assigns or legal representatives, as herein provided, solely from the special fund hereinafter identified, upon presentation and surrender of this Bond, the Principal Amount specified above, on the Maturity Date specified above, and to pay interest on said sum at the per annum Interest Rate specified above, from the interest payment date to which interest has been paid next preceding the date on which this Bond is authenticated, unless this Bond is authenticated on an interest payment date to which interest has been paid, in which event this Bond shall bear interest from such date, or if this Bond is authenticated prior to the first interest payment date, this Bond shall bear interest from the Date of Original Issue set out above, semiannually on January 1 and July 1 of each year, commencing on January 1, 1999, until payment of the Principal Amount, except as the provisions hereinafter set forth with regard to redemption prior to maturity may be and become applicable hereto. The principal amount of this Bond (and redemption price, if redeemed prior to maturity) is payable upon surrender of this Bond, at maturity or at earlier redemption prior to maturity, in lawful money of the United States of America at the main office of The Fifth Third Bank, Cincinnati, Ohio (the "Paying Agent" and "Bond Registrar"). Interest due on this Bond shall be paid by check or draft by mail postmarked no later than the due date thereof by the Paying Agent to the registered owner hereof at the address shown as of the 15th day of the month preceding each interest payment date on the bond register kept by the Bond Registrar.

This Bond is part of a duly authorized issue of Eight Million Four Hundred Seventy Thousand Dollars (\$8,470,000), principal amount of Henry County Water District No. 2 Waterworks Refunding Revenue Bonds, Series 1998 (the "Series 1998 Bonds") issued by the District pursuant to a Resolution duly adopted (the "Current Bond Resolution") under and in full compliance with the Constitution and Statutes of the Commonwealth of Kentucky, and more specifically, Chapters 58 and 74 of the Kentucky Revised Statutes (the "Act"), for the purpose of providing funds sufficient for the current refunding of the outstanding (i) Henry County Water District Waterworks Refunding and Improvement Revenue Bonds, Series B, dated April 1, 1967; (ii) Henry County Water District No. 2 Waterworks Revenue Bonds of 1986, dated June 29, 1987; (iii) Henry County Water District

No. 2 Waterworks Revenue Bonds of 1987, dated October 28, 1988; and (iv) Interim Loan from the Kentucky Infrastructure Authority.

The Current Bond Resolution reaffirms that so long as any of the Series 1998 Bonds and/or any additional bonds ranking on a parity therewith, are outstanding, the System shall be owned and operated as a combined and consolidated revenue-producing public project or system within the meaning of the Act, for the security and source of payment of any and all of such outstanding the Series 1998 Bonds or any additional Parity Bonds.

Reference is made to the Current Bond Resolution for provisions with respect to the nature and extent of the security, rights, duties and obligations of the holders of the Series 1998 Bonds, the District and the Paying Agent and Bond Registrar, the terms upon which the Series 1998 Bonds are issued and the terms and conditions upon which the Bonds will be deemed to be paid at or prior to their scheduled maturity or redemption upon the making or provision for the payment thereof in the manner set forth in the Current Bond Resolution.

*The Series 1998 Bonds maturing on January 1, _____, are subject to mandatory sinking fund redemption in part, at the selection of the Paying Agent and Bond Registrar by lot, from moneys in the special fund identified hereinafter on each January 1, _____, at the principal amount thereof plus accrued interest to the redemption date, according to the following schedule of mandatory sinking fund installments:

<u>January 1</u>	<u>Amount</u>
	\$

The Series 1998 Bonds do not constitute an indebtedness of the District within the meaning of any constitutional or statutory provisions or limitations, but are payable as to both principal and interest solely out of the revenues of the System, as aforesaid.

The Series 1998 Bonds are issuable as fully registered bonds in the denomination of \$5,000 and any authorized multiple thereof within a single maturity.

This Series 1998 Bond is transferable by the registered owner hereof in person or by his attorney duly authorized in writing at the main office of the Bond Registrar, but only in the manner and subject to the limitations provided in the Current Bond Resolution, and upon surrender and

*Paragraph to be added if Term Bonds are issued.

cancellation of this Bond, duly endorsed for transfer or accompanied by an assignment duly executed by the registered owner or his authorized representative. Upon such transfer being made, a new fully registered Series 1998 Bond or Series 1998 Bonds of the same series and the same maturity of authorized denomination, for the same aggregate principal amount, will be issued to the transferee in exchange for this Series 1998 Bond.

The District and the Bond Registrar may deem and treat the registered owner hereof as the absolute owner hereof for the purpose of receiving payment of principal hereof, redemption price, if any, and interest due hereon and for all other purposes, and neither the District nor the Bond Registrar shall be affected by any notice to the contrary.

The Series 1998 Bonds maturing on and after January 1, 2010 shall be subject to redemption by the District prior to maturity, in whole or in part in the inverse order of their maturities (less than all of a single maturity to be selected by lot), at any time falling on or after January 1, 2009, at a redemption price expressed as a percentage of the principal amount of the Series 1998 Bonds called for redemption, plus unpaid interest accrued to the date of redemption as follows:

<u>Redemption Dates (inclusive)</u>	<u>Redemption Price</u>
January 1, 2009, through December 31, 2009	102%
January 1, 2010, through December 31, 2010	101%
January 1, 2011 and thereafter	100%

In the event that a Series 1998 Bond subject to redemption is in a denomination larger than \$5,000, a portion of such Series 1998 Bond may be redeemed, but only in a principal amount equal to \$5,000 or an integral multiple thereof. Upon surrender of any Series 1998 Bond for redemption in part, the Bond Registrar, in accordance with the Current Bond Resolution, shall authenticate and deliver an exchange Series 1998 Bond or Series 1998 Bonds in an aggregate principal amount equal to the unredeemed portion of the Series 1998 Bond so surrendered.

The Registrar shall give notice of any redemption by sending such notice by United States Mail, first class, postage prepaid by registered or certified mail, at least 30 days prior to the date fixed for redemption, to the registered owner of this Bond at the address shown on the bond register as of the date of mailing of such notice.

It is hereby certified, recited and declared that all acts, conditions and things required to exist, happen and be performed precedent to and in the issuance of the Series 1998 Bonds, have existed, have happened and have been performed, in due time, form and manner as required by law, that the amount of this Bond, together with all other obligations of said District, does not exceed any limit prescribed by the Constitution or Statutes of the Commonwealth of Kentucky, and that a sufficient portion of the gross income and revenues of the System has been pledged to and will be set aside into the Sinking Fund by the District for the prompt payment of the principal of and interest on this Bond and all of the Series 1998 Bonds, and all other bonds ranking on a parity therewith.

IN WITNESS WHEREOF, said Henry County Water District No. 2, in the Commonwealth of Kentucky, has caused this Bond to be executed on its behalf with the duly authorized reproduced facsimile signature of the Chairman of said District, and the reproduced facsimile of its Corporate Seal to be imprinted hereon and attested by the reproduced facsimile signature of its Secretary, dated as of the first day of October, 1998; provided, however, that this Bond shall not be valid or become obligatory for any purpose, or be entitled to any security or benefit under the Current Bond Resolution pursuant to which it was authorized until the Authentication Certificate of Registrar printed hereon shall have been executed by the manual signature of a duly authorized representative of the Bond Registrar.

Henry County Water District No. 2

By _____
Chairman

Attest:

Secretary

AUTHENTICATION CERTIFICATE OF REGISTRAR

This is to certify that this Bond is one of the Series 1998 Bonds referred to in the within Bond and in the Current Bond Resolution authorizing same.

The Authentication Date of this Bond is: _____

The Fifth Third Bank

By _____
Authorized Officer

ASSIGNMENT

For value received, the undersigned hereby sells, assigns, and transfers unto _____ the within Bond and hereby irrevocably constitutes and appoints _____ attorney to transfer said Bond on the books kept for registration and transfer of this Bond, with full power of substitution in the premises.

Dated: _____

Signature Guaranteed By:

Social Security Number or other taxpayer identification number:

Notice: Signature must be guaranteed by a member firm of the New York Stock Exchange or a commercial bank or trust company.

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RESOLUTION

RESOLUTION OF THE HENRY COUNTY WATER DISTRICT NO. 2 APPROVING AND AUTHORIZING AN ASSISTANCE AGREEMENT WITH THE KENTUCKY RURAL WATER FINANCE CORPORATION FOR THE PURPOSE OF FINANCING A CONSTRUCTION PROJECT OF THE DISTRICT

WHEREAS, the Board of Commissioners ("Governing Authority") of the Henry County Water District No. 2 (the "District") has previously determined that it is in the public interest to make improvements and extensions to the District's waterworks system (the "System");

WHEREAS, the District desires the Kentucky Rural Water Finance Corporation (the "Corporation") to act as its agency and instrumentality for the purpose of providing monies to finance the cost of said improvements and extensions consisting of improvements to raw water supply, storage, transmission and distribution of treated water. Major work items include:

- 1) New Raw Water Supply Well (24-inches, 107 feet),
- 2) 1,500-gallon per minute Well Pump (vertical turbine),
- 3) 20-inch D.I. Raw Water Main (est. 80,000 feet),
- 4) 16-inch to 20-inch D.I. Water Main (est. 14,500 ft.),
- 5) 4-inch to 12-inch PVC and D.I. Waterline (est. 73,500 ft.),
- 6) Control Valve and Meter Vault,
- 7) New Telemetry sites and Modifications to Existing Telemetry System, and
- 8) 300 gpm Duplex Booster Pump Station.

(the "Project") and has made an application to the Corporation therefore;

WHEREAS, in order to obtain such monies, the District is required to enter into an Assistance Agreement with the Corporation; and

NOW, THEREFORE, BE IT RESOLVED by the Governing Authority of the Henry County Water District No. 2, as follows:

1. Authorization of Assistance Agreement and the Obligations Thereunder. For the purpose of paying the costs, not otherwise provided, of the financing of the Project, the District hereby authorizes and approves the issuance of its obligations pursuant to the Assistance Agreement in the aggregate principal amount of \$900,000 (subject to adjustment minus ten percent (10%)) [the "Obligations"], which amount as adjusted shall be the maximum amount of such Obligations to be outstanding at any one time under the Assistance Agreement, issued as fully registered Obligations, in said maturities and terms as more fully provided for in the Assistance Agreement. The Obligations shall bear interest at such rates and shall be payable in such amounts and at such times as specified in the Assistance Agreement, all as agreed upon by the District and the Corporation.

2. Approval and Authorization of Execution of Assistance Agreement. The Assistance Agreement by and between the District and the Corporation in the respective form attached to this Resolution, is hereby approved, subject to such minor changes, changes of dates, insertions or omissions as may be approved by the Chairman, such approval to be conclusively evidenced by the execution of said Assistance Agreement, in order to effectuate the purposes of this Resolution; and the Chairman, or any other officer of the District, is hereby authorized to execute and acknowledge same for and on behalf of the District; and the Secretary is authorized to attest same and to affix thereto the corporate seal of the District. The Assistance Agreement is hereby ordered to be filed in the office of the Secretary with this Resolution in the official records of the District.

3. Disbursement of Proceeds of Obligations. The District's officers, employees and agents are authorized to carry out the procedures specified in the Assistance Agreement for the financing of the Project and for the payment from time to time of the costs and related expenses associated therewith.

4. Revenues of the Project. The revenues of the System are determined to be sufficient to pay the principal of and interest on the Obligations, as the same become due and payable; and said revenues, pursuant to the terms of the Assistance Agreement, are hereby pledged to secure all such payments, and in addition, for such other purposes as are more fully specified in the Assistance Agreement.

5. Chairman and Other District Officials to Take Any Other Necessary Action. Pursuant to the Constitution and Laws of the Commonwealth of Kentucky, the Chairman, the Treasurer, the Secretary and all other appropriate officials of the District are hereby authorized and directed to file any and all applications necessary to obtain approval of the issuance of the Obligations from the Kentucky Public Service Commission and to take any and all further action and to execute and deliver all other documents as may be reasonably necessary to effect the issuance and delivery of the Obligations and the Assistance Agreement.

6. Severability Clause. If any section, paragraph, clause or provision of this Resolution shall be ruled by any court of competent jurisdiction to be invalid, the invalidity of such section, paragraph, clause or provision shall not affect any of the remaining provisions hereof.

7. Captions of Clauses. The captions of this Resolution are for convenience only and are not to be construed as part of this Resolution nor as defining or limiting in any way the scope or intent of the provisions hereof.

8. Provisions in Conflict Repealed. All resolutions and orders, or parts thereof, in conflict with the provisions of this Resolution are, to the extent of such conflict, hereby repealed.

9. Effective Date of Resolution. This Resolution shall take effect from and after its adoption and approval.

Adopted on August 13, 2002.

HENRY COUNTY WATER DISTRICT
NO. 2

By 
Chairman

Attest:

By 
Secretary

CERTIFICATE

I, the undersigned, hereby certify that I am the duly qualified and acting Secretary of the Henry County Water District No. 2; that the foregoing is a full, true and correct copy of a Resolution adopted by the Governing Authority of the Henry County Water District No. 2 at a meeting duly held on August 13, 2002; that said official action appears as a matter of public record in the official records or Journal of the Governing Authority; that said meeting was held in accordance with all applicable requirements of Kentucky law, including KRS 61.810, 61.815, 61.820 and 61.823; that a quorum was present at said meeting; that said official action has not been modified, amended, revoked or repealed and is now in full force and effect.

IN TESTIMONY WHEREOF, witness my signature this 13th day of August, 2002.


Secretary

ASSISTANCE AGREEMENT

BETWEEN

KENTUCKY RURAL WATER FINANCE CORPORATION

AND

HENRY COUNTY WATER DISTRICT NO. 2

DATED SEPTEMBER 25, 2002

This document was prepared by:

RUBIN & HAYS
Kentucky Home Trust Building
450 South Third Street
Louisville, Kentucky 40202
(502) 569-7525

By Christian Z. Judd

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ASSISTANCE AGREEMENT

This Assistance Agreement made and entered into as of the 25th day of September, 2002 (the "Assistance Agreement") by and between the Kentucky Rural Water Finance Corporation, a non-profit corporation and instrumentality of the various entities of the Commonwealth of Kentucky (the "Issuer") and the Henry County Water District No. 2, Henry County, Kentucky (the "Governmental Agency"):

WITNESSETH

WHEREAS, the Issuer has established its Public Projects Flexible Term Program (the "Program") designed to provide financing for the expansion, addition and improvements of public projects for governmental entities under which the Issuer issued its Kentucky Rural Water Finance Corporation Multimodal Public Projects Revenue Bonds (Flexible Term Program), Series 2001, dated April 4, 2001, in the aggregate principal amount of \$46,000,000 (the "Series 2001 Bonds") pursuant to a Trust Indenture dated as of April 4, 2001 (the "Indenture") between the Issuer and Fifth Third Bank, trustee (the "Trustee"), the net proceeds of which will be applied for the benefit of such governmental entities by making loans, pursuant to Assistance Agreements; and

WHEREAS, pursuant to the Indenture, the Issuer has authorized the issuance of the Kentucky Rural Water Finance Corporation Public Projects Revenue Bonds (Flexible Term Program), Series 2001D, in the aggregate principal amount of \$2,830,000 (the "Series 2001D Bonds") pursuant to Supplemental Trust Indenture No. 5, dated as of September 25, 2002 by and between the Issuer and the Trustee (the "Series 2001D Indenture"), which Series 2001D Bonds will rank on a parity with the Series 2001 Bonds and the proceeds of which will be used by certain Governmental Agencies to acquire, construct and equip public projects described in various Assistance Agreements by and between the Governmental Agencies and the Issuer; and

WHEREAS, the Issuer has previously remarketed, reissued and delivered \$5,315,000 of the Series 2001 Bonds in a Fixed Rate Mode to be known as Kentucky Rural Water Finance Corporation Multimodal Public Projects Revenue Bonds (Flexible Term Program), Series 2001A (the "Series 2001A Bonds") pursuant to Supplemental Trust Indenture No. 1, dated as of June 27, 2001 by and between the Issuer and the Trustee (the "Series 2001A Indenture"); and

WHEREAS, the Issuer has previously remarketed, reissued and delivered \$1,005,000 of the Series 2001 Bonds in a Fixed Rate Mode to be known as Kentucky Rural Water Finance Corporation Multimodal Public Projects Revenue Bonds (Flexible Term Program), Series 2001B (the "Series 2001B Bonds") pursuant to Supplemental Trust Indenture No. 2, dated as of December 19, 2001 by and between the Issuer and the Trustee (the "Series 2001B Indenture"); and

WHEREAS, the Issuer has previously remarketed, reissued and delivered \$900,000 of the Series 2001 Bonds in a Fixed Rate Mode to be known as Kentucky Rural Water Finance Corporation Multimodal Public Projects Revenue Bonds (Flexible Term Program), Series 2001C (the "Series 2001C Bonds") pursuant to Supplemental Trust Indenture No. 3, dated as of May 15, 2002 by and between the Issuer and the Trustee (the "Series 2001C Indenture"); and

WHEREAS, the Issuer has previously issued and delivered \$1,640,000 of Kentucky Rural Water Finance Corporation Public Projects Refunding Revenue Bonds (Flexible Term Program), Series 2002 (the "Series 2002 Bonds"), which rank on a parity with the Series 2001 Bonds, pursuant to Supplemental Trust Indenture No. 4, dated as of July 15, 2002 by and between the Issuer and the Trustee (the "Series 2002 Indenture"); and

WHEREAS, the Governmental Agency has determined that it is necessary and desirable and in the public interest to finance improvements to the Governmental Agency's waterworks system (the "Project"), and the Issuer has determined that the Project is a project within the meaning of the Act and the Indenture, thereby qualifying for financial assistance from the Issuer; and

WHEREAS, the Issuer has found and determined that the Project will be in furtherance of the purposes of the Issuer and the Governmental Agency under the Act; and

WHEREAS, the Governmental Agency has designated the Issuer as its instrumentality and agency; and

WHEREAS, pursuant to this Assistance Agreement the Governmental Agency will proceed with the Project; and

WHEREAS, the Governmental Agency, presently owns and operates the waterworks system (the "System") of said Governmental Agency; and

WHEREAS, the Governmental Agency has heretofore issued its Prior Bonds (as hereinafter defined); and

WHEREAS, in and by the Prior Bond Legislation (as hereinafter defined), the right and privilege was reserved by the Governmental Agency under conditions and restrictions set out in said Prior Bond Legislation, of issuing additional bonds from time to time, payable from the income and revenues of the System and ranking on a parity with the outstanding Prior Bonds, for the purpose, among other things, of financing the costs of extensions, additions and improvements to the System, and refinancing certain outstanding indebtedness, which conditions and restrictions are found to currently exist and prevail so as to permit the issuance of certain proposed additional bonds so as to rank, when issued, on a parity with the outstanding Prior Bonds; and

WHEREAS, it is deemed necessary and advisable for the best interests of the Governmental Agency that it enter into this Assistance Agreement with the Issuer in order to borrow funds (the "Loan") in the amount of \$900,000 [the "Obligations"], for the purpose of providing funds for the Project, and to reaffirm the conditions and restrictions whereunder similar bonds or obligations may be subsequently issued ranking on a parity therewith; and

WHEREAS, under the provisions of Sections 58.010 through 58.140, inclusive, of the Kentucky Revised Statutes, and under the provisions of the Prior Bond Legislation, the Governmental Agency is authorized to enter into this Assistance Agreement and to borrow the Obligations to provide such funds for the purpose aforesaid; and

WHEREAS, the Issuer is willing to cooperate with the Governmental Agency in making available the Loan pursuant to the Act and the Indenture to be applied to the Project upon the conditions hereinafter enumerated and the covenants by the Governmental Agency herein contained; and

WHEREAS, the Issuer and the Governmental Agency have determined to enter into this Assistance Agreement pursuant to the terms of the Act and the Indenture and to set forth their respective duties, rights, covenants, and obligations with respect to the construction and financing of the Project subject to the repayment of the Loan and the Obligations and the interest thereon;

NOW, THEREFORE, FOR AND IN CONSIDERATION OF THE MUTUAL COVENANTS HEREIN SET FORTH, THE LOAN HEREBY EFFECTED AND OTHER GOOD AND VALUABLE CONSIDERATION, THE RECEIPT OF WHICH IS HEREBY ACKNOWLEDGED BY EACH PARTY, THE PARTIES HERETO MUTUALLY COVENANT AND AGREE, EACH WITH THE OTHER AS FOLLOWS:

Section 1. Definitions. As used in this Assistance Agreement, unless the context requires otherwise:

"*Act*" refers to Chapters 58 and 74 of the Kentucky Revised Statutes.

"*Assistance Agreement*" refers to this Assistance Agreement authorizing the Loan and the Obligations.

"*Bond Counsel*" refers to a nationally recognized firm of Bond Counsel which firm has prepared the legal proceedings for the Obligations, has furnished all of the customary services of Bond Counsel in this financing and will continue to furnish such services until the Obligations are delivered and paid for, including the rendering of the final approving legal opinion with regard to the legality of the Obligations and the tax exemption of the interest thereon.

"*Bond Legislation of 1967*" or "*1967 Bond Legislation*" refers to the resolution authorizing the Series 1967 Bonds, which was adopted by the Governing Body on September 14, 1967.

"*Bond Legislation of 1974*" or "*1974 Bond Legislation*" refers to the resolution authorizing the Series 1974 Bonds, which was adopted by the Governing Body on February 12, 1974.

"*Bond Legislation of 1996*" or "*1996 Bond Legislation*" refers to the resolution authorizing the Series 1996 Bonds, which was adopted by the Governing Body on September 10, 1996.

"*Bond Legislation of 1998*" or "*1998 Bond Legislation*" refers to the resolution authorizing the Series 1998 Bonds, which was adopted by the Governing Body on October 1, 1998.

"*Bondowner*", "*Owner*", "*Bondholder*" means and contemplates, unless the context otherwise indicates, the registered owner of one or more of the Bonds at the time issued and outstanding hereunder.

"*Bonds*" refers to the Obligations, the Prior Bonds and any additional Parity Bonds.

"*Certified Public Accountants*" refers to an independent Certified Public Accountant or firm of Certified Public Accountants, duly licensed in Kentucky and knowledgeable about the affairs of the System and/or of other Governmental Agency financial matters.

"*Code*" refers to the United States Internal Revenue Code of 1986, as amended, and any regulations issued thereunder.

"*Compliance Group*" refers to the Compliance Group identified and defined in the Indenture.

"*Depository Bank*" refers to the bank or banks in which the Funds referred to in this Assistance Agreement will be deposited and maintained as the depository(ies) for such Funds; as determined by the Governmental Agency.

"*Depreciation Fund*" refers to the Henry County Water District No. 2 Waterworks Revenue Bond Depreciation Reserve Fund created in the Prior Bond Legislation and which Depreciation Fund will continue to be maintained for the benefit of all of the Bonds.

"*Engineer*" or "*Independent Consulting Engineer*" refers to an Independent Consulting Engineer or firm of Engineers of excellent national reputation or of recognized excellent reputation in Kentucky in the fields of waterworks and sewer engineering.

"*Funds*" refers to the Revenue Fund, the Sinking Fund, the Depreciation Fund, the Operation and Maintenance Fund and the Governmental Agency Account.

"*Governing Body*" means the Board of Commissioners of the Governmental Agency or such other body as shall be the governing body of said Governmental Agency under the laws of Kentucky at any given time.

"*Governmental Agency*" refers to the Henry County Water District No. 2.

"*Governmental Agency Chief Executive*" refers to the Chairman of the Governmental Agency.

"*Governmental Agency Clerk*" refers to the Secretary of the Governmental Agency.

"*Indenture*" means the Trust Indenture, dated as of April 4, 2001, as originally executed or as it may from time to time be supplemented, modified or amended by any supplemental mortgage, by and between the Issuer and the Trustee.

"*Interest Payment Date*" shall mean the 1st day of each month, commencing January 1, 2003 and continuing through and including January 1, 2018 or until the Loan has been paid in full.

"*Issuer*" refers to the Kentucky Rural Water Finance Corporation.

"*Obligations*" refers to the Loan authorized by this Assistance Agreement in the principal amount of \$900,000.

"*Operation and Maintenance Fund*" refers to the "Henry County Water District No. 2 Waterworks Operation and Maintenance Fund" created and confirmed in the Prior Bond Legislation and which Operation and Maintenance Fund will continue to be maintained for the benefit of the System.

"*Outstanding Bonds*" refers collectively to all outstanding Prior Bonds, the outstanding Obligations and any outstanding Parity Bonds, and does not refer to any bonds which have been defeased.

"*Parity Bonds*" means bonds issued in the future, which will, pursuant to the provisions of this Assistance Agreement, rank on a basis of parity with the Obligations and shall not be deemed to include, nor to prohibit the issuance of, bonds ranking inferior in security to the Obligations.

"*Permitted Investments*" refers to investments of funds on deposit in the various funds created herein and includes:

- (1) direct obligations of the United States of America (including obligations issued or held in book-entry form on the books of the Department of the Treasury of the United States of America) or obligations the timely payment of the principal of and interest on which are fully guaranteed by the United States of America, including instruments evidencing an ownership interest in securities described in this clause (1);
- (2) obligations, debentures, notes or other evidences of indebtedness issued or guaranteed by any of the following:

Federal Home Loan Bank System, Export-Import Bank of the United States, Federal Financing Bank, Federal Land Banks, Government National Mortgage Association, Federal Home Loan Mortgage Corporation or Federal Housing Administration;
- (3) repurchase agreements (including those of the Trustee or the Bank) fully secured by collateral security described in clause (1) or (2) of this definition, which collateral (a) is held by the Trustee or a third party agent during the term of such repurchase agreement, (b) is not subject to liens or claims of third parties and (c) has a market value (determined at least once every fourteen days) at least equal to the amount so invested;
- (4) certificates of deposit of, or time deposits in, any bank (including the Trustee or the Bank) or savings and loan association (a) the debt obligations of which (or in the case of the principal bank of a bank holding company, the debt obligations of the bank holding company of which) have been rated at least equal to the rating assigned to the Bonds by each Rating Agency then rating the Bonds or (b) which are fully insured by the Federal Deposit Insurance Corporation or (c) which are secured at all

times, in the manner and to the extent provided by law, by collateral security (described in clause (1) or (2) of this definition) of a market value (valued at least quarterly) of no less than the amount of money so invested;

- (5) shares in any investment company registered under the Federal Investment Governmental Agency Act of 1940 whose shares are registered under the Federal Securities Act of 1933 and whose only investments are government securities described in clause (1) or (2) of this definition and repurchase agreements fully secured by government securities described in clause (1) or (2) of this definition and/or other obligations rated AAA by S&P;
- (6) tax-exempt obligations of any state of the United States, or political subdivision thereof, which are rated AA or better by S&P or mutual funds invested only in such obligations;
- (7) units of a taxable or nontaxable government money-market portfolio composed of U.S. Government obligations and repurchase agreements collateralized by such obligations;
- (8) commercial paper rated A-1 or A-1+ by S&P;
- (9) corporate notes or bonds with one year or less to maturity rated in one of the two highest Rating Categories by S&P; or
- (10) shares of mutual funds, each of which shall have the following characteristics:
 - (i) The mutual fund shall be an open-end diversified investment company registered under the Federal Investment company Act of 1940, as amended;
 - (ii) The management company of the investment company shall have been in operation for at least five (5) years; and
 - (iii) All of the securities in the mutual fund shall be in investments in any one or more of the investments described in (1) and (3) above.

"*Prior Bond Legislation*" refers collectively to the 1967, 1974, 1996, and the 1998 Bond Legislation the SRECC Loan Agreement.

"*Prior Bonds*" refers to the Series 1967 Bonds, Series 1974 Bonds, Series 1996 Bonds and SRECC Note.

"*Prior Bonds*" refers collectively to the Series 1967 Bonds, Series 1974 Bonds, Series 1996 Bonds, Series 1998 Bonds and the SRECC Note.

"*Program*" refers to the Issuer's Public Projects Flexible Term Program designed to provide financing for the expansion, addition and improvements of public projects for governmental entities.

"*Program Administrator*" refers to the Kentucky Rural Water Association, Inc., Bowling Green, Kentucky.

"*Program Reserve Fund*" refers to the Reserve Fund created and established pursuant to Section 4.2 of the Indenture.

"*Project*" refers to financing , with the proceeds of the Obligations, improvements to raw water supply, storage, and transmission and distribution of treated water. Major work items include:

- 1) New raw water supply well (24 inches, 107 feet),
- 2) 1,500 gallon per minute well pump (vertical turbine),
- 3) 20 inch D.I. raw water main (est. 80,000 feet),
- 4) 16 inch to 20 inch D.I. water main (est. 14,500 feet),
- 5) 4 inch to 12 inch PVC and D.I. waterline (est. 73,500 feet),
- 6) control valve and meter vault,
- 7) new telemetry sites and modifications to existing telemetry system, and
- 8) 300 gpm duplex booster pump station.

"*Record Date*" shall mean with respect to any Interest Payment Date, the close of business on the 15th day next preceding such Interest Payment Date, whether or not such day is a business day.

"*Requisition Certificate*" means the form attached hereto as Exhibit C to be utilized by the Governmental Agency in obtaining disbursements of the Loan from the Governmental Agency Account as construction of the Project progresses.

"*Reserve Fund*" refers to the Henry County Water District No. 2 Waterworks Debt Service Reserve Fund of 1998, created in Section 401(C) of the 1998 Bond Legislation and which Reserve Fund will continue to be maintained for the benefit of all of the Bonds.

"*Revenue Fund*" refers to the Henry County Water District No. 2 Waterworks Revenue Fund created in the Prior Bond Legislation and which Revenue Fund will continue to be maintained for the benefit of all of the Bonds.

"*Prior Bonds*" refers collectively to the Series 1967 Bonds, Series 1974 Bonds, Series 1996 Bonds, Series 1998 Bonds and the SRECC Note.

"*Series 1967 Bonds*" refers to the original authorized \$1,850,000 of Henry County Water District No. 2 Waterworks System Revenue Bonds, dated November 20, 1967.

"*Series 1974 Bonds*" refers to the original authorized \$239,000 of Henry County Water District No. 2 Waterworks System Revenue Bonds, Series of 1974, dated June 4, 1975.

"*Series 1996 Bonds*" refers to the original authorized \$3,000,000 of Henry County Water District No. 2 Waterworks Revenue Bonds, Series 1996, dated April 29, 1997.

"*Series 1998 Bonds*" refers to the original authorized \$8,245,000 of Henry County Water District No. 2 Waterworks Refunding Revenue Bonds, Series 1998, dated October 1, 1998.

"*Sinking Fund*" refers to the Henry County Water District No. 2 Waterworks Revenue Bond Sinking Fund created and confirmed in the Prior Bond Legislation and which Sinking Fund will continue to be maintained for the benefit of the System.

"*SRECC*" refers to the Shelby Rural Electric Cooperative Corporation, now known as Shelby Energy Cooperative, Inc.

"*SRECC Note*" refers to the non-interest bearing Note payable to the SRECC, dated April 29, 1997, in the original authorized principal amount of \$400,000.

"*SRECC Loan Agreement*" refers to the Loan Agreement between the District and SRECC authorizing the SRECC Note, dated as of April 29, 1997.

"*System*" refers to the Governmental Agency's waterworks system, together with all future extensions, additions and improvements to said System.

"*Treasurer*" refers to the Treasurer of the Governmental Agency.

"*Trustee*" refers to Fifth Third Bank, Cincinnati, Ohio.

"*U.S. Obligations*" refers to bonds, notes, or Treasury Bills which are direct obligations of the United States of America or obligations fully guaranteed by the United States of America, including book-entry obligations of the United States Treasury-State and Local Government Series, and Trust Receipts representing an ownership interest in direct obligations of the United States.

Section 2. Reaffirmation of Declaration of Waterworks System. That all proceedings heretofore taken for the establishment of and the supplying of water service in and to said Governmental Agency as a waterworks system are hereby in all respects ratified and confirmed; and so long as any of the obligations hereinafter authorized or permitted to be issued remain outstanding, said System shall be owned, controlled, operated and maintained for the security and source of payment of said obligations. Said System is hereby declared to constitute a public project within the meaning and application of Sections 58.010 to 58.140, inclusive, of the Kentucky Revised Statutes.

Section 3. Authorization of Obligations; Place of Payment; Manner of Execution. That pursuant to the Constitution and laws of Kentucky, and particularly said Sections 58.010 to 58.140, inclusive of the Kentucky Revised Statutes, the Governmental Agency hereby authorizes the

borrowing of \$900,000 from the Program, for the purpose of providing funds for the Project. Said Obligations shall mature on each January 1 beginning January 1, 2004 and continuing thereafter through and until January 1, 2018, in such principal amounts, and shall bear interest payable on the Interest Payment Dates, commencing January 1, 2003 in the maturities and at the interest rates set forth in Exhibit A attached hereto.

The principal of, redemption price, if any, and interest on the Obligations shall be payable in lawful money of the United States of America on the Interest Payment Dates, beginning January 1, 2003 to the Trustee for the Program. Such payment shall be made by the Governmental Agency from funds on deposit in the Sinking Fund pursuant to the ACH Debit Direct Payment Method (the "ACH Debit Direct Payment Method") as described and detailed in the ACH Debit Direct Payment Authorization Form (the "ACH Authorization Form") attached hereto as Exhibit B. The ACH Authorization Form shall be completed, signed and forwarded to the Trustee prior to the Governmental Agency receiving any of the proceeds of the Loan.

Pursuant to the ACH Debit Direct Payment Method, there shall be transferred to the Trustee on or before the first day of each month, from the Sinking Fund, the amounts hereinafter specified:

- (1) An amount equal to one-sixth (1/6) of the interest becoming due on the Obligations on the next succeeding interest due date [provided that for the first seven payments one-seventh (1/7) of the interest due on the Obligations on the next succeeding interest due date], and subject to a credit for the amount on deposit in the Sinking Fund transferred thereto on the date of issue of the Obligations; plus
- (2) An amount equal to one-twelfth (1/12) of the principal amount of all Obligations maturing on the next succeeding January 1 [provided that for the first seven payments one-seventh (1/7) of the principal due on the Obligations on January 1].

In addition, in the event the Issuer is required to withdraw moneys from the Program Reserve Fund established pursuant to the Indenture to pay the principal of and interest on the Obligations and any other payments due under this Assistance Agreement on behalf of the Governmental Agency (the "Reserve Withdrawal"), the Governmental Agency shall pay to the Trustee, in each month, pursuant to the ACH Debit Direct Payment Method an amount equal to at least 1/12 of the Reserve Withdrawal, plus accrued interest thereon at the rate equal to the highest rate of interest paid by the investments making up the Program Reserve Fund until such Reserve Withdrawal has been replenished.

Section 4. Redemption. (a) *Optional Redemption.* Subject to the prior written approval of the Compliance Group, Obligations maturing on or after January 1, 2014, are subject to redemption, in whole or in part, at any time, by the Governmental Agency prior to their stated maturities, on any date falling on or after January 1, 2013, upon payment of the principal amount to be redeemed plus accrued interest to the date of redemption, on the dates, subject to redemption premium stated as a percentage of the principal amount to be redeemed, as follows:

<u>Redemption Dates (Inclusive)</u>	<u>Redemption Price</u>
January 1, 2013 through December 31, 2013	101.0%
January 1, 2014 through December 31, 2014	100.5%
January 1, 2015 and thereafter	100.0%

In the event that the Governmental Agency desires to optionally redeem a portion of its Obligations, such redemption shall be in a denomination equal to \$5,000 or any integral multiple thereof.

(b) Notice of Redemption. The Governmental Agency shall give the Issuer and the Trustee notice of any redemption by sending at least one such notice by first class United States mail not less than 45 and not more than 90 days prior to the date fixed for redemption.

All of said Obligations as to which the Governmental Agency reserves and exercises the right of redemption and as to which notice as aforesaid shall have been given, and for the retirement of which, upon the terms aforesaid, funds are duly provided, will cease to bear interest on the redemption date.

Section 5. Obligations Payable Out of Revenues on a Parity with Prior Bonds. All of the Obligations and Prior Bonds, together with the interest thereon and such additional bonds ranking on a parity therewith heretofore issued and outstanding and that may be hereafter issued and outstanding from time to time under the conditions and restrictions hereinafter set forth, shall be payable out of the Sinking Fund, as heretofore created in the Prior Bond Legislation and as hereinafter more specifically provided and shall be a valid claim of the holder thereof only against said fund and the fixed portion or amount of the income and revenues of the System of said Governmental Agency pledged to said fund.

Section 6. Compliance with Parity Coverage Requirements of the Prior Bond Legislation. It is hereby declared that in accordance with the provisions of the Prior Bond Legislation, and prior to the issuance of any of the Obligations hereby authorized, there will be procured and filed with the Governmental Agency Clerk of said Governmental Agency any and all statements or certifications for the purpose of having both principal and interest on the Prior Bonds and the Obligations hereby authorized payable on a parity from the income and revenues of said System with said outstanding Prior Bonds.

Section 7. Flow of Funds. All proceedings preliminary to and in connection with the issuance of the Prior Bonds, whereby provision was made for the receipt, custody, and application of the proceeds of the Prior Bonds; for the operation of said System on a revenue-producing basis; for the segregation, allocation, and custody of the revenues derived from the operation of the System; and for the enforcement and payment of the Prior Bonds; and all other covenants for the benefit of the bondholders set out in the Prior Bond Legislation, are hereby ratified and confirmed and shall continue in force and inure to the security and benefit of the Bonds, the same as if such provisions and proceedings were repeated in full herein; provided, further, that, hereafter, the income and revenues of the System shall be collected, segregated, accounted for, and distributed as follows:

A. Revenue Fund. The Governmental Agency covenants and agrees that it will continue to deposit in the Revenue Fund, promptly as received from time to time, all revenues of the System, as same may be extended and improved from time to time. The moneys in the Revenue Fund shall continue to be used, disbursed and applied by the Governmental Agency only for the purpose and in the manner and order of priorities specified in the Prior Bond Legislation, as hereinafter modified by this Assistance Agreement, all as permitted by the Act, and in accordance with previous contractual commitments.

B. Sinking Fund. A separate and special fund or account of the Governmental Agency, distinct and apart from all other funds and accounts, was created in and by the Prior Bond Resolution and designated and identified as the "Waterworks Bond and Interest Sinking Fund", which shall continue to be maintained so long as any of the Outstanding Bonds or any additional Parity Bonds herein permitted to be issued are outstanding; and all moneys deposited therein from time to time shall be used and disbursed and applied, and are hereby irrevocably pledged, solely for the purpose of paying the principal of and interest on the Outstanding Bonds and any Parity Bonds hereafter issued and outstanding pursuant to the provisions of this Assistance Agreement.

There shall be set aside and transferred on or before the 20th day of each month from the Revenue Fund, as a first charge thereon, and deposited in the Sinking Fund Sums sufficient to pay when due the principal and interest requirements on the Outstanding Bonds. Specifically, there shall be paid into the Sinking Fund on or before the 20th day of each month, on account of the Outstanding Bonds, not less than the following:

- (1) An amount equal to one-sixth (1/6) of the next succeeding six-month interest payment to become due on the Outstanding Bonds, plus
- (2) A sum equal to one-twelfth (1/12) of the principal of any Outstanding Bonds maturing on the next succeeding principal payment date.

In the event additional Parity Bonds are issued pursuant to the conditions and restrictions hereinafter prescribed, the monthly deposits to the Sinking Fund shall be increased to provide for payment of interest thereon and the principal thereof as the same respectively become due.

If for any reason there should be a failure to pay into the Sinking Fund the full amounts above stipulated, then an amount equivalent to such deficiency shall be set apart and paid into the Sinking Fund from the first available income and revenues of the System, subject to the aforesaid priorities.

No further payments need to be made into the Sinking Fund if and when the amount held therein and in any other available fund is at least equal to the amount required to retire all Outstanding Bonds and Parity Bonds and paying all interest that will accrue thereon.

C. Depreciation Fund. Pursuant to the provisions of the Prior Bond Legislation, there shall next be transferred from the Revenue Fund a sum sufficient, each month, to maintain a balance in said Depreciation Fund of at least the sum required by the Prior Bond Legislation, which shall be deposited into the Depreciation Fund.

Moneys in the Depreciation Fund may be withdrawn and used by the Governmental Agency, upon appropriate certification of the Governing Body, in accordance with the provisions of the Prior Bond Legislation, for the purpose of paying the cost of unusual or extraordinary maintenance, repairs, renewals and replacements not included in the annual budget of current expenses and/or of paying the costs of constructing future extensions, additions and improvements to the System which will either enhance its revenue-producing capacity or will provide a higher degree of service, and when necessary, for the purpose of making payments of principal and interest on the Bonds if the amount on deposit in the Sinking Fund is not sufficient to make such payments.

D. Operation and Maintenance Fund. There shall next be transferred monthly from the Revenue Fund and deposited into said Operation and Maintenance Fund, sums sufficient to meet the current expenses of operating and maintaining the System. The balance maintained in said Operation and Maintenance Fund shall not be in excess of the amount required to cover anticipated System expenditures for a two-month period pursuant to the Governmental Agency's annual budget.

E. Surplus Funds. Subject to the provisions for the disposition of the income and revenues of the System as set forth hereinabove, which provisions are cumulative, and after paying or providing for the payment of debt service on any subordinate obligations, there shall be transferred, within sixty days after the end of each fiscal year, the balance of excess funds in the Revenue Fund on such date, to the Depreciation Fund for application in accordance with the terms of this Assistance Agreement or to the Sinking Fund to be applied to the maximum extent feasible, to the prompt purchase or redemption of Outstanding Bonds.

Provided, however, notwithstanding anything to the contrary in any Prior Bond Legislation, the Governmental Agency shall be allowed a credit to the extent of moneys on deposit in the Program Reserve Fund for the purpose of meeting any parity requirements in any Prior Bond Legislation; subject however, to the limitation that moneys in the Program Reserve Fund may only be used to make payments of the Government Agency due under this Assistance Agreement, if necessary, and; provided further, that the Trustee may not seek payment for any reserve funds held by the Governmental Agency under any Prior Bond Legislation for payment of any amounts due from the Governmental Agency under this Assistance Agreement.

Section 8. Disposition of Proceeds of the Obligations; Governmental Agency Account. Upon (i) the execution of this Assistance Agreement, (ii) the deliverance of this Assistance Agreement to the Trustee, (iii) certification of the Compliance Group that the Loan is to be accepted in the Program and (iv) upon receipt by the Governmental Agency of the proceeds of the Obligations, the proceeds shall be applied as follows:

(a) Disposition of the Proceeds. There shall first be deducted and paid from the proceeds of the Obligations the fees and costs incurred by the Governmental Agency and any other pertinent

expenses incident to the issuance, sale and delivery of the Obligations and such other appropriate expenses as may be approved by the Governmental Agency Chief Executive, including but not limited to the Governmental Agency's pro rata share of the Program's fees and expenses.

The balance shall be deposited to the Governmental Agency Account to be used to construct the Project.

(b) *Governmental Agency Account.* It is hereby acknowledged that a fund entitled "Henry County Water District No. 2 Governmental Agency Account" (the "Governmental Agency Account") has been created and maintained by the Trustee pursuant to the Indenture; and the amount on deposit in said Governmental Agency Account shall be applied to the extent necessary, to pay the cost of additions and improvements to and the construction of the Project.

Investment income derived from investment of the Governmental Agency Account, which shall be invested in Permitted Investments in accordance with this Assistance Agreement, shall, as received, be deposited in the Governmental Agency Account.

The Trustee shall be obligated to send written notice to the Governmental Agency of the need for investment directions if and whenever funds in excess of \$50,000 shall remain uninvested for a period of more than five days. In the absence of written direction from the Governmental Agency with respect to investment of moneys held in the Governmental Agency Account, the Trustee is hereby directed to invest funds in money market mutual funds of the Trustee or its affiliates that qualify as Permitted Investments under this Assistance Agreement.

Payment from the Governmental Agency Account for costs in connection with the Project shall be made only upon a Requisition Certificate delivered to the Trustee which has been approved by the Engineers having charge of supervising such acquisition, improvement and construction, and countersigned by the Governmental Agency Chief Executive, said Engineers to certify in each instance that the Requisition Certificate represents a sum actually earned by and due to the proposed payee under a contract with said Governmental Agency for work performed and/or materials furnished in connection with the Project, or represents a sum necessary to be expended for land and/or rights of way necessary to be acquired by the Governmental Agency in connection with said Project.

No expenditure shall be made from the Governmental Agency Account except for proper and authorized expenses relating to the acquisition, improvement and construction of the Project in accordance with the contracts, plans and specifications approved by the Governmental Agency.

After completion of the Project, as certified by the Engineers, any balance then remaining on deposit in the Governmental Agency Account shall, subject to any and all applicable legal provisions and applicable arbitrage regulations necessary to assure the exemption of interest on the Obligations from Federal income taxation, upon orders of the Governing Body, be transferred to the Sinking Fund, to be used for the purposes thereof.

Section 9. Arbitrage Limitations. (1) The Governmental Agency covenants that neither the proceeds of the Obligations, nor "Non-Exempt Revenues" of the System, as defined below, will be invested in investments which will produce a net adjusted yield in excess of the net interest cost (effective yield) of the Obligations, if such investment would cause such Obligations to be treated as "arbitrage bonds" within the meaning of Section 148 of the Internal Revenue Code, as amended, and the applicable regulations thereunder; provided, however, that such proceeds and/or revenues may be invested to whatever extent and whenever the Code and/or applicable regulations permit same to be invested without causing the Obligations to be treated as "arbitrage bonds."

(2) "Non-Exempt Revenues" within the meaning of the foregoing shall be deemed to refer to revenues of the System deposited in any of the funds earmarked for or reasonably expected to be used for the payment of debt service on the Obligations, in excess of "Exempt Revenues," which Exempt Revenues are:

- (a) amounts deposited in the Sinking Fund for the purpose of paying debt service on any Obligations against the System within thirteen (13) months from the date of deposit; and
- (b) amounts deposited in the Depreciation Fund or any similar reserve for replacements, reasonably expected to be used for extensions, additions, improvements or replacements to the System, and not reasonably expected to be used to pay debt service (even if pledged to be used to pay debt service in the event of the unexpected inadequacy of other funds pledged for that purpose).

(3) If, and to the extent that any Non-Exempt Revenues are on deposit and are available for investment by reason of the foregoing, such funds shall be subject to the investment limitations set out in Section 9(1) above.

On the basis of information furnished to the Governmental Agency, on known facts, circumstances and reasonable expectations on the date of enactment of this Assistance Agreement, the Governmental Agency certifies as follows:

- (a) That it is not expected or contemplated that the proceeds of the Obligations will be used or invested in any manner which will cause any of the Obligations to be treated as "arbitrage bonds" within the meaning of Section 148 of the Code and the applicable regulations thereunder.
- (b) That it is not expected or contemplated that the Governmental Agency will make any use of the proceeds of the Obligations, which, if such use had been reasonably anticipated on the date of issuance of the Obligations, would have caused the Obligations to be arbitrage bonds.
- (c) That it is expected and contemplated that the Governmental Agency will comply with (i) all of the requirements of Section 148 of the Code; and (ii) all of the requirements of the applicable regulations thereunder, to whatever extent is necessary to assure that the Obligations will not be treated as arbitrage bonds.

- (d) That it is anticipated that amounts on deposit in the Sinking Fund will be used within 13 months from the date of deposit for the payment of debt service on the outstanding Obligations and all Prior Bonds payable from said Sinking Fund.
- (e) That amounts accumulated in the Sinking Fund shall not exceed the limitations set forth in this Assistance Agreement.
- (f) That it is not reasonably anticipated that amounts accumulated in the Depreciation Fund will be used for payment of debt service on any bonds payable from the revenues of the System, even though such Depreciation Fund will be so available if necessary to prevent a default in the payment of principal and interest on such bonds.

Prior to or at the time of delivery of the Obligations, the Governmental Agency Chief Executive and/or the Governmental Agency Treasurer are authorized to execute the appropriate certification with reference to the matters referred to above, setting out all known and contemplated facts concerning such anticipated investment of the proceeds of the Obligations, including the execution of necessary and/or desirable certifications of the type contemplated by the Code and applicable regulations, as amended, in order to assure that interest on the Obligations will be exempt from all federal income taxes and that the Obligations will not constitute or be treated as arbitrage bonds.

Section 10. Parity Bonds. The Obligations shall not be entitled to priority one over the other in the application of the income and revenues of the System, regardless of the time or times of their issuance, it being the intention that there shall be no priority among the Obligations, regardless of the fact they may be actually issued and delivered at different times, and provided further that the lien and security of and for any bonds or obligations hereafter issued that are payable from the income and revenues of the System, shall, except as set out herein, be subject to the priority of the Prior Bonds and the Obligations as may from time to time be outstanding; provided the Governmental Agency has in said Prior Bond Legislation reserved the right and privilege, and does hereby reserve the right and privilege, of issuing additional bonds from time to time payable from the income and revenues of the System ranking on a parity with the Prior Bonds and with the Obligations, but only under the conditions specified in the Prior Bond Legislation, which conditions are hereinafter repeated, taking into account the issuance of the Obligations.

The Governmental Agency reserves the right to finance future extensions, additions, and/or improvements to the System by the issuance of one or more additional series of bonds to be secured by a parity lien on and ratably payable from, the revenues of the System pledged to the Prior Bonds and the Obligations, provided;

(a) The facility or facilities to be constructed from the proceeds of the additional parity bonds is or are made a part of the System and its or their revenues are pledged as additional security for the additional parity bonds and the outstanding Prior Bonds and Obligations.

(b) The Governmental Agency is in compliance with all covenants and undertakings in connection with all of the bonds then outstanding and payable from the revenues of the System or any part thereof.

(c) The annual net revenues (defined as gross revenues less operation expenses), of the then existing System for the Fiscal Year preceding the year in which such Parity Bonds are to be issued, adjusted as hereinafter provided, shall be certified by an independent Certified Public Accountant to be equal at least one hundred twenty percent (120%) of the average annual debt service requirements for principal and interest on all Outstanding Bonds payable from the revenues of the System, including such requirements of the Obligations, any Parity Bonds then outstanding plus the anticipated debt service requirements of any Parity Bonds then proposed to be issued. The calculation of average annual debt service requirements of principal and interest on the additional Parity Bonds to be issued shall, regardless of whether such additional Parity Bonds are to be serial or term bonds, be determined on the basis of the principal of and interest on such Parity Bonds being payable in approximately equal annual installments.

(d) The "annual net revenues" referred to above may be adjusted for the purpose of the foregoing computations to reflect:

(i) any revision in the schedule of rates or charges being imposed at the time of the issuance of any such additional Parity Bonds, and

(ii) any increase in the "annual net revenues" to be realized, within 12 months of the completion of the Project, from the proposed extensions, additions, and/or improvements being financed (in whole or in part) by such additional Parity Bonds; provided all such adjustments shall be based upon and included in a certification of a Certified Public Accountant.

(e) Reference is made to the necessity of obtaining the written consent of the United States Department of Agriculture Rural Development or its successor [the "RD"] for the issuance of future bonds encumbering the System while the RD holds any bonds payable from the revenues of the System.

The Governmental Agency hereby covenants and agrees that in the event any additional Parity Bonds are issued, the Governmental Agency shall:

(1) Adjust the monthly amount to be deposited into the Sinking Fund on the same basis as that prescribed in the provisions establishing such Sinking Fund, to reflect the annual debt service requirements of the additional Parity Bonds; and

(2) Adjust the minimum annual amount to be deposited monthly into the Sinking Fund on the same basis as that prescribed in the provisions establishing such Sinking Fund, taking into account the future debt service requirements of all first lien bonds which will then be outstanding against the System.

The Governmental Agency reserves the right to issue parity bonds to refund or refinance any part or all of the Prior Bonds and the Obligations, provided that prior to the issuance of such additional parity bonds for that purpose, there shall have been procured and filed with the Governmental Agency Clerk of the Governmental Agency a statement by a Certified Public Accountant, as defined herein, reciting the opinion based upon necessary investigation that:

(a) after the issuance of such parity bonds, the annual net revenues, as adjusted and defined above, of the then existing system for the fiscal year preceding the date of issuance of such Parity Bonds, after taking into account the revised debt service requirements resulting from the issuance of such Parity Bonds and from the elimination of the Bonds being refunded or refinanced thereby, are equal to not less than 120% of the average annual debt service requirements then scheduled to fall due in any fiscal year thereafter for principal of and interest on all of the then outstanding Bonds payable from the revenues of the System, calculated in the manner specified above; or

(b) in the alternative, that the average annual debt service requirements for the Prior Bonds, the Obligations, any previously issued Parity Bonds and the proposed refunding Parity Bonds, in any year of maturities thereof after the redemption of the Bonds scheduled to be refunded through the issuance of such proposed refunding Parity Bonds, shall not exceed the average annual debt service requirements applicable to the then outstanding Prior Bonds, the Obligations and any previously issued Parity Bonds for any year prior to the issuance of such proposed Parity Bonds and the redemption of the Bonds to be refunded.

Section 11. Rates and Charges for Services of the System. While any Bonds are outstanding and unpaid, the rates for all services of the System rendered by the Governmental Agency to its citizens, corporations, or others requiring the same, shall be reasonable and just, taking into account and consideration the cost and value of said System, the cost of maintaining and operating the same, the proper and necessary allowances for depreciation thereof, and the amounts necessary for the retirement of the outstanding Bonds and the accruing interest on all such Bonds as may be outstanding under the provisions of this Assistance Agreement and the Prior Bond Legislation, and there shall be charged such rates and amounts as shall be adequate to meet all requirements of the provisions of this Assistance Agreement. Prior to the issuance of the Obligations a schedule of rates and charges for the services rendered by the System to all users adequate to meet all requirements of this Assistance Agreement has been established and adopted.

The Governmental Agency covenants that it will not reduce the rates and charges for the services rendered by the System without first filing with the Governmental Agency Clerk a certification of an Independent Consulting Engineer or a Certified Public Accountant that the "annual net revenues" (defined as gross revenues less operation expenses) of the then existing System for the fiscal year preceding the year in which such reduction is proposed, as such annual net revenues are adjusted, after taking into account the projected reduction in annual net revenues anticipated to result from any such proposed rate decrease, are equal to not less than 120% of the average annual debt service requirements for principal and interest on all of the then outstanding bonds payable from the revenues of the System, calculated in the manner specified in Section 10 hereof.

The Governmental Agency also covenants to cause a report to be filed with the Governing Body within four months after the end of each fiscal year by a Certified Public Accountant, setting forth the precise debt service coverage percentage of the average annual debt service requirements falling due in any fiscal year thereafter for principal of and interest on all of the then Outstanding Bonds payable from the revenues of the System, produced or provided by the net revenues of the System in that fiscal year, calculated in the manner specified in Section 10 hereof; and the Governmental Agency covenants that if and whenever such report so filed shall establish that such coverage of net revenues for such year was less than 120% of the average annual debt service requirements, the Governmental Agency shall increase the rates by an amount sufficient, in the opinion of such Certified Public Accountant, to establish the existence of or immediate projection of, such minimum 120% coverage.

Section 12. All Obligations of this Issue Are Equal. The Obligations authorized and permitted to be issued hereunder, and from time to time outstanding, shall not be entitled to priority one over the other in the application of the income and revenues of the System regardless of the time or times of their issuance, it being the intention that there shall be no priority among the Obligations, the Prior Bonds and any Parity Bonds authorized or permitted to be issued under the provisions of this Assistance Agreement, regardless of the fact that they may be actually issued and delivered at different times.

Section 13. Defeasance and/or Refunding of Obligations. The Governmental Agency reserves the right, at any time, to cause the pledge of the revenues securing the outstanding Obligations to be defeased and released by paying an amount into an escrow fund sufficient, when invested (or sufficient without such investment, as the case may be) in direct obligations of or obligations guaranteed by the United States of America, including book entry obligations and trust receipts representing an ownership in direct obligations of the United States of America, to assure the availability in such escrow fund of an adequate amount (a) to call for redemption and to redeem and retire all of such outstanding Obligations, both as to principal and as to interest, on the next or any optional redemption date, including all costs and expenses in connection therewith, and to pay all principal and interest falling due on the outstanding Obligations to and on said date, or (b) to pay all principal and interest requirements on the outstanding Obligations as same mature, without redemption in advance of maturity, the determination of whether to defease under (a) or (b) or both to be made by the Governing Body. Such Permitted Investments shall have such maturities as to assure that there will be sufficient funds for such purpose. If such defeasance is to be accomplished pursuant to (a), the Governmental Agency shall take all steps necessary to publish the required notice of the redemption of the outstanding Obligations and the applicable redemption date. Upon the proper amount of such investments being placed in escrow and so secured, such revenue pledge shall be automatically fully defeased and released without any further action being necessary.

Section 14. Contractual Nature of Assistance Agreement. The provisions of this Assistance Agreement shall constitute a contract between the Governmental Agency and the Issuer; and after the issuance of any of such Obligations, no change, variation or alteration of any kind in the provisions of this Assistance Agreement, nor of the Prior Bond Legislation, shall be made in any manner except as herein or therein provided until such time as all of the Bonds authorized thereby and the interest thereon have been paid or provided for in full, or as otherwise provided herein; provided (a) that the Governing Body may enact legislation for any other purpose not inconsistent

with the terms of this Assistance Agreement, and which shall not impair the security of the Issuer and/or for the purpose of curing any ambiguity, or of curing, correcting or supplementing any defective or inconsistent provisions contained herein or in any ordinance or other proceedings pertaining hereto.

Section 15. Appointment and Duties of Bond Registrar and Paying Agent. The Trustee is hereby designated as the bond registrar and paying agent with respect to the Obligations.

Its duties as Trustee shall be as follows:

- (1) To register all of the Obligations in the names of the Issuer;
- (2) To cancel and destroy (or remit to the Governmental Agency for destruction, if so requested by the Governmental Agency) all exchanged, matured, retired and redeemed Obligations, and to maintain adequate records relevant thereto;
- (3) To remit, but only to the extent that all required funds are made available to the Trustee by the Governmental Agency, semiannual interest payments directly to the Issuer's accounts for the Program;
- (4) To notify the Issuer of any Obligations to be redeemed and to redeem Obligations prior to their stated maturity upon receiving sufficient funds; and
- (5) To supply the Governmental Agency with a written accounting evidencing the payment of interest on and principal of the Obligations within thirty (30) days following each respective due date.

The Trustee shall be entitled to the advice of counsel and shall be protected for any acts taken by it in good faith in reliance upon such advice. The Trustee shall not be liable for any actions taken in good faith and believed by it to be within its discretion or the power conferred upon it by this Assistance Agreement, or the responsibility for the consequences of any oversight or error in judgment.

The Trustee may at any time resign from its duties set forth in this Assistance Agreement by filing its resignation with the Governmental Agency Clerk and notifying the Issuer. Thereupon, the Issuer shall notify the Governmental Agency of a successor Trustee which shall be an incorporated bank or trust company authorized to transact business in the United States of America. Notwithstanding the foregoing, in the event of the resignation of the Trustee, provision shall be made for the orderly transition of the books, records and accounts relating to the Obligations to the successor Trustee in order that there will be no delinquencies in the payment of interest or principal due on the Obligations.

Section 16. Provisions in Conflict Repealed. All ordinances, resolutions and orders, or parts thereof, in conflict herewith are, to the extent of such conflict, hereby repealed; and it is hereby specifically ordered and provided that any proceedings heretofore taken for the issuance of other bonds payable or secured in any manner by all or any part of the income and revenues of the

System, or any part thereof, and which have not heretofore been issued and delivered, are hereby revoked and rescinded, and none of such other bonds shall be issued and delivered.

Section 17. Covenant of Governmental Agency to Take All Action Necessary to Assure Compliance with the Internal Revenue Code of 1986. In order to assure purchasers of the Obligations that interest thereon will continue to be exempt from federal and Kentucky income taxation (subject to certain exceptions set out below), the Governmental Agency covenants to and with the Issuer that (1) the Governmental Agency will take all actions necessary to comply with the provisions of the Code, (2) the Governmental Agency will take no actions which will violate any of the provisions of the Code, or would cause the Obligations to become "private activity bonds" within the meaning of the Code, (3) none of the proceeds of the Obligations will be used for any purpose which would cause the interest on the Obligations to become subject to federal income taxation, and the Governmental Agency will comply with any and all requirements as to rebate (and reports with reference thereto) to the United States of America of certain investment earnings on the proceeds of the Obligations.

The Governmental Agency hereby certifies that it does not reasonably expect to issue bonds or other obligations considered under the Code to be "tax-exempt obligations" in the aggregate principal amount in excess of \$5,000,000 during the calendar year in which the Obligations are being issued, and has irrevocably allocated that portion of its \$5,000,000 small issuer exemption equal to the principal amount of the Obligations, and for that reason the Governmental Agency has been advised by Bond Counsel that pursuant to Section 148(f)(4)(C) of the Code, neither the debt service fund nor any other fund or account established under the provisions of this Assistance Agreement is subject to the "rebate requirements" on excess earnings in favor of the United States of America imposed by the Code. The Governmental Agency covenants and agrees that in the event it is subsequently determined, upon advice of nationally recognized bond counsel, that any fund or account established under this Assistance Agreement, is subject to said rebate requirements and do, in fact, generate earnings from "non-purpose investments" in excess of the amount which said investments would have earned at a rate equal to the "yield" on the Obligations, plus any income attributable to such excess, it shall rebate to the United States of America any such excess generated from such investments and remit such excess to the United States of America on or before five (5) years from the date of issuance of the Obligations, and once every five years thereafter until the final retirement of the Obligations; the last installment, to the extent required, to be made no later than sixty (60) days following the date on which funds sufficient for the complete retirement of the Obligations are deposited with the Paying Agent or any escrow agent.

The Governmental Agency reserves the right to amend this Assistance Agreement but only with the consent of the Issuer (i) to whatever extent shall, in the opinion of Bond Counsel, be deemed necessary to assure that interest on the Obligations shall be exempt from federal income taxation, and (ii) to whatever extent shall be permissible (without jeopardizing such tax exemption or the security of such owners) to eliminate or reduce any restrictions concerning the investment of the proceeds of these Obligations, or the application of such proceeds or of the revenues of the System. The purchasers of these Obligations are deemed to have relied fully upon these covenants and undertakings on the part of the Governmental Agency as part of the consideration for the purchase of the Obligations. To the extent that the Governmental Agency obtains an opinion of