

ARTICLE IX

9. Damage and Condemnation. Damage to or destruction of all or any portion of the Association Property and condemnation of all or any portion of the Association Property shall be handled in the following manner:

(a) If the Association Property is damaged or destroyed, the Association shall cause the Association Property to be repaired and reconstructed substantially in accordance with the original plans and specifications, and any restoration or repair of the Association Property shall be performed substantially in accordance with the original plans and specifications. If the cost of effecting total restoration of the Association Property exceeds the amount of insurance proceeds, then the Association shall levy a Reconstruction Assessment against the Lots and their respective Owners equal to the difference between the total restoration cost and the insurance proceeds.

(b) Each Owner is liable to the Association for any damage to the Association Property not fully reimbursed to the Association by insurance proceeds (including without limitation any deductible amounts under any insurance policies against which the Association files a claim for such damage) which may be sustained due to the negligence or willful misconduct of said Owner or the persons deriving their right and easement of use and enjoyment of the Association Property from said Owner, or of such Owner's family and guests. The Association may, after Notice and Hearing, (i) determine whether any claim shall be made upon the insurance maintained by the Association and (ii) levy against such Owner a Special Assessment equal to any deductible paid and the increase, if any, in the insurance premium directly attributable to the damage caused by such Owner or the persons for whom such Owner may be liable as described herein. If a Lot is jointly owned, the liability of its Owners is joint and several, except to the extent that the Association has previously contracted in writing with such joint Owners to the contrary. After Notice and Hearing, the cost of correcting such damage, to the extent not reimbursed to the Association by insurance, shall be a Special Assessment against such Owner.

(c) If all or any portion of the Association Property is taken by right of eminent domain or by private purchase in lieu of eminent domain, the award in condemnation shall be paid to the Association and deposited in the Operating Fund. No Owner may participate as a party, or otherwise, in any proceedings relating to such condemnation.

ARTICLE X

10. Insurance.

10.1 Casualty Insurance. The Board shall obtain and maintain fire and casualty insurance with extended coverage for loss or damage to all insurable Improvements installed by Declarant, Merchant Builders or by the Association on the Association Property for the full replacement cost thereof without deduction for depreciation or coinsurance, and may obtain insurance against such other hazards and casualties as the Association may deem desirable. The casualty insurance shall include earthquake coverage unless the Board is directed not to obtain earthquake coverage by a majority of the Association's voting power. The Association may also insure any other real or personal property it owns against loss or damage by fire and such other hazards as the Association may deem desirable, with the Association as the owner and beneficiary of such insurance. The policies insuring the Association Property must be written in

the name of, and the proceeds thereof must be payable to the Association. Unless the applicable insurance policy provides for a different procedure for the filing of claims, all claims made under such policy must be sent to the insurance carrier or agent, as applicable, by certified mail and be clearly identified as a claim. The Association shall keep a record of all claims made. Subject to Article IX(b) and XI(d) hereof, the Association shall use insurance proceeds to repair or replace the property for which the insurance was carried. Premiums for all insurance carried by the Association are a Common Expense.

10.2 Insurance Obligations of Owners. Each Owner is responsible for insuring his personal property and all other property and Improvements within his Dwelling Unit. Each Owner is also responsible for carrying public liability insurance in the amount such Owner deems desirable to cover such Owner's individual liability for damage to person or property occurring inside such Owner's Dwelling Unit or elsewhere upon such Owner's Lot. Such policies shall not adversely affect or diminish any liability under any insurance obtained by or on behalf of the Association, and duplicate copies of such other policies shall be deposited with the Board upon the Board's request. If any loss intended to be covered by insurance carried by or on behalf of the Association occurs and the proceeds payable thereunder are reduced due to insurance carried by any Owner, such Owner shall assign the proceeds of such insurance to the Association, to the extent of such reduction, for application by the Board to the same purposes as the reduced proceeds are to be applied.

10.3 Waiver of Subrogation. All policies of physical damage insurance the Association maintains must provide, if reasonably possible, for waiver of: (a) any defense based on coinsurance; (b) any right of setoff, counterclaim, apportionment, proration or contribution due to other insurance not carried by the Association; (c) any invalidity, other adverse effect or defense due to any breach of warranty or condition caused by the Association, any Owner or any tenant of any Owner, or arising from any act or omission of any named insured or the respective agents, contractors and employees of any insured; (d) any rights of the insurer to repair, rebuild or replace, and, if any Improvement is not repaired, rebuilt or replaced following loss, any right to pay under the insurance an amount less than the replacement value of the Improvements insured; (e) notice of the assignment of any Owner of its interest in the insurance by virtue of a conveyance of any Lot; (f) any denial of an Owner's claim because of negligent acts by the Association or other Owners; or (g) prejudice of the insurance by any acts or omissions of Owners that are not under the Association's control. As to each policy of insurance the Association maintains which will not be voided or impaired thereby, the Association hereby waives and releases all claims against the Board, the Owners, the Manager, Declarant, Merchant Builders, and the agents and employees of each of the foregoing, with respect to any loss covered by such insurance, whether or not caused by negligence or breach of any agreement by such persons, but only to the extent that insurance proceeds are received in compensation for such loss.

10.4 Liability and Other Insurance. The Association shall obtain comprehensive public liability insurance, including medical payments and malicious mischief, in such limits as it deems desirable (but in no event less than \$1 million covering all claims for personal injury and property damage arising out of a single occurrence), insuring against liability for bodily injury, death and property damage arising from the Association's activities or with respect to property the Association maintains or is required to maintain including, if obtainable, a cross-liability endorsement insuring each insured against liability to each other insured. The Association may also obtain Worker's Compensation insurance and other liability insurance as it may deem desirable, insuring each Owner, the Association, Board and Manager, against liability in connection with the Association Property, the premiums for which are a Common Expense. The Board shall review all insurance policies at least annually and increase the limits in its discretion. The Board may also obtain such errors and omissions insurance, indemnity bonds, fidelity bonds and other insurance as it deems advisable, insuring the Board, the Association's officers and the

Manager against any liability for any act or omission in carrying out their obligations hereunder, or resulting from their membership on the Board or on any committee thereof. However, fidelity bond coverage which names the Association as an obligee must be obtained by or on behalf of the Association for any person or entity handling Association funds, including, but not limited to, Association officers, directors, trustees, employees and agents and Manager employees, whether or not such persons are compensated for their services, in an amount not less than the estimated maximum of funds, including reserve funds, in the Association's or Manager's custody during the term of each bond. The aggregate amount of such bonds may not be less than one-fourth (1/4) of the Annual Assessments on all Lots in the Properties, plus reserve funds. In addition, the Association shall continuously maintain in effect such casualty, flood and liability insurance and fidelity bond coverage meeting the requirements for planned unit developments established by FNMA, GNMA, FHLMC, VA and FHA, so long as any of them is a Mortgagee or an Owner of a Lot in the Properties, except to the extent such coverage is not available or has been waived in writing by FNMA, GNMA, FHLMC, VA and FHA, as applicable. The Association shall, upon issuance or renewal of insurance, but no less than annually, provide the Owners with the notice required by Section 1365.9(c) of the California Civil Code.

10.5 Notice of Expiration Requirements. If available, each insurance policy the Association maintains must contain a provision that said policy may not be canceled, terminated, materially modified or allowed to expire by its terms, without ten (10) days' prior written notice to the Board, Declarant, Merchant Builders and to each Owner and Beneficiary, insurer and guarantor of a first Mortgage who has filed a written request with the carrier for such notice, and every other Person in interest who requests such notice of the insurer.

ARTICLE XI

11. Rights of Mortgagees. Notwithstanding any other provision of this Declaration, no amendment or violation of the Declaration defeats or renders invalid the rights of the Beneficiary under any Deed of Trust upon one (1) or more Lots made in good faith and for value, provided that after the foreclosure of any such Deed of Trust such Lot(s) will remain subject to this Declaration. For purposes of this Declaration, "first Mortgage" means a Mortgage with first priority over other Mortgages or Deeds of Trust on a Lot, and "first Mortgagee" means the Beneficiary of a first Mortgage. For purposes of any provisions of the Restrictions which require the vote or approval of a specified percentage of first Mortgagees, such vote or approval is determined based upon one (1) vote for each Lot encumbered by each such first Mortgage. In order to induce FHLMC, GNMA, FNMA, VA and FHA to participate in the financing of the sale of Lots, the following provisions are added hereto (and to the extent these added provisions conflict with any other provisions of the Restrictions, these added provisions control):

(a) Each Beneficiary, insurer and guarantor of a first Mortgage encumbering one or more Lots, upon filing a written request for notification with the Board, is entitled to written notification from the Association of:

(i) any condemnation or casualty loss which affects either a material portion of the Properties or the Lot(s) securing the respective first Mortgage; and

(ii) any delinquency of sixty (60) days or more in the performance of any obligation under the Restrictions, including without limitation the payment of assessments or charges owed by the Owner(s) of the Lot(s) securing the respective first Mortgage, which notice each Owner hereby consents to and authorizes; and