

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

(iii) a lapse, cancellation, or material modification of any policy of insurance or fidelity bond maintained by the Association; and

(iv) any proposed action of the Association which requires consent by a specified percentage of first Mortgagees.

(b) Each Owner, including each first Mortgagee of a Mortgage encumbering any Lot which obtains title to such Lot pursuant to the remedies provided in such Mortgage, or by foreclosure of such Mortgage, or by deed or assignment in lieu of foreclosure, shall be exempt from any "right of first refusal" created or purported to be created by the Restrictions.

(c) Each first Mortgagee of a first Mortgage encumbering any Lot which obtains title to such Lot pursuant to the remedies provided in such Mortgage or by foreclosure of such Mortgage, shall take title to such Lot free and clear of any claims for unpaid assessments or charges against such Lot which accrued prior to the time such Mortgagee acquires title to such Lot in accordance with Section 6.15.

(d) Unless at least sixty-seven percent (67%) of the first Mortgagees or sixty-seven percent (67%) of the Owners (other than Declarant and Merchant Builders) have given their prior written approval, the Association may not:

(i) by act or omission seek to abandon, partition, subdivide, encumber, sell or transfer the Association Property and the Improvements thereon which are owned by the Association; provided that the following acts shall not be limited by the terms of this clause: The granting of easements for public utilities or for other purposes consistent with the intended use of such property by the Association as provided in this Declaration; or the granting to an Owner or Owners of exclusive easements over portions of the Association Property or of fee interests in portions of the Association Property pursuant to a Recorded lot line adjustment approved by the requisite governmental entity, so long as each such grant to an Owner is reasonably required for purposes of conformity with the as-built location of authorized Improvements;

(ii) change the method of determining the obligations, assessments, dues or other charges which may be levied against a Lot Owner, or the method of allocating distributions of hazard insurance proceeds or condemnation awards;

(iii) by act or omission change, waive or abandon any scheme of regulations, or enforcement thereof, pertaining to the architectural design or the exterior appearance of the Dwelling Units and other Improvements on the Lots, the exterior maintenance of the Dwelling Units, the maintenance of the party walls, the maintenance of the common fences and driveways, or the upkeep of lawns and plantings in the Properties;

(iv) fail to maintain Fire and Extended Coverage insurance on insurable Association Property on a current replacement cost basis in an amount as near as possible to one

hundred percent (100%) of the insurance value (based on current replacement cost); or

(v) use hazard insurance proceeds for losses to any Association Property for other than the repair, replacement or reconstruction of such property.

(e) All Beneficiaries, insurers and guarantors of first Mortgages, upon written request to the Association, shall have the right to:

(i) examine current copies of the Association's books, records and financial statements and the Restrictions during normal business hours; and

(ii) require the Association to submit an annual audited financial statement for the preceding Fiscal Year if one is available, or have one prepared at the expense of the requesting entity if such statement is not otherwise prepared by the Association; provided that, upon annexation of additional Lots to the Properties such that fifty (50) or more Lots are subject to this Declaration, the Association may be required to submit such a statement without expense to the requesting entity within one hundred twenty (120) days of the end of the Fiscal Year; and

(iii) receive written notice of all meetings of Owners; and

(iv) designate in writing a representative who shall be authorized to attend all meetings of Owners.

(f) All Beneficiaries, insurers and guarantors of first Mortgages, who have filed a written request for such notice with the Board shall be given thirty (30) days' written notice prior to (1) any abandonment or termination of the Association, (2) the effective date of any proposed, material amendment to this Declaration or the Articles of Incorporation or Bylaws of the Association, and (3) the effective date of any termination of any agreement for professional management of the Properties following a decision of the Owners to assume self-management of the Properties. Such first Mortgagees shall be given immediate notice (1) following any damage to the Common Area whenever the cost of reconstruction exceeds Ten Thousand Dollars (\$10,000.00), and (2) when the Board learns of any threatened condemnation proceeding or proposed acquisition of any portion of the Properties.

(g) First Mortgagees may, jointly or singly, pay taxes or other charges which are in default and which may have become a charge against any Association Property and may pay any overdue premiums on hazard insurance policies, or secure new hazard insurance coverage on the lapse of a policy, for Association Property, and first Mortgagees making such payments shall be owed immediate reimbursement therefor from the Association.

(h) The Reserve Fund described in Article VI of this Declaration must be funded by regular scheduled monthly, quarterly, semiannual or annual payments rather than by large special assessments.

(i) The Board shall secure and cause to be maintained in force at all times a fidelity bond for any Person handling funds of the Association, including, but not limited to, employees of the professional Manager.

(j) When professional management has been previously required by a Beneficiary, insurer or guarantor of a first Mortgage, any decision to establish self-management by the Association shall require the approval of sixty-seven percent (67%) of the voting power of the Association and the Beneficiaries of fifty-one percent (51%) of the first Mortgages of Lots in the Properties.

(k) The Board may enter into such contracts or agreements on behalf of the Association as are required in order to satisfy the guidelines of FHLMC, FNMA, GNMA, VA or FHA or any similar entity, so as to allow for the purchase, insurance or guaranty, as the case may be, by such entities of first Mortgages encumbering Lots with Dwelling Units thereon. Each Owner hereby agrees that it will benefit the Association and its Owners, as a class of potential Mortgage borrowers and potential sellers of their Lots, if such agencies approve the Properties as a qualifying subdivision under their respective policies, rules and regulations. Each Owner hereby authorizes his Mortgagees to furnish information to the Board concerning the status of any Mortgage encumbering a Lot.

ARTICLE XII

12. Declarant and Merchant Builders Exemption. Declarant and Merchant Builders or their successors or assigns intend, but are not obligated, to construct Dwelling Units and develop all of the Lots in the Properties. The completion of that work and sale, resale, rental and other disposal of Lots is essential to the establishment and welfare of the Properties as a quality residential community. As used in this Article and its subparagraphs, the words "its successors or assigns" specifically do not include purchasers of Lots pursuant to transactions requiring the issuance of a Final Subdivision Public Report. In order that such work may be completed and the Properties be established as a fully occupied residential community as rapidly as possible, no Owner nor the Association may do anything to interfere with, and nothing in this Declaration may be understood or construed to:

(a) Prevent Declarant, Merchant Builders, their successors or assigns, or any of their contractors or subcontractors, from doing on any Lot owned by them whatever they determine to be necessary or advisable in connection with the completion of such work, including without limitation altering of construction plans and designs as Declarant or a Merchant Builder deems advisable in the course of development; or

(b) Prevent Declarant, Merchant Builders, their successors or assigns, or any of their representatives, from erecting and maintaining on any portion of the Properties owned or controlled by Declarant or a Merchant Builder, or their successors or assigns or any of their contractors or subcontractors, such structures as may be reasonably necessary to conduct the business of completing such work and establishing the Properties as a residential community and disposing of the same by sale, resale, lease or otherwise; or

(c) Prevent Declarant, Merchant Builders, their successors or assigns, or any of their contractors or subcontractors, from conducting on any Lot, or any portion thereof, owned or controlled by Declarant, Merchant Builders, their successors or assigns, the business of developing, altering, subdividing, grading