

NEW ISSUE—BOOK-ENTRY ONLY

RATINGS:
S&P: "AA" (Radian)
S&P: "BBB" (Underlying)
See "RATINGS" herein

In the opinion of Stradling Yocca Carlson & Rauth, a Professional Corporation, Newport Beach, California, Bond Counsel, under existing statutes, regulations, rulings and judicial decisions, and assuming certain representations and compliance with certain covenants and requirements described herein, interest (and original issue discount) on the Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of calculating the federal alternative minimum tax imposed on individuals and corporations. In the further opinion of Bond Counsel, interest (and original issue discount) on the Bonds is exempt from State of California personal income tax. The difference between the issue price of a Bond (the first price at which a substantial amount of the Bonds of a maturity is to be sold to the public) and the stated redemption price at maturity is original issue discount. See "TAX MATTERS" herein with respect to tax consequences of the Bonds. The Agency has designated the Bonds as "bank qualified" under the provisions of Section 265(b)(3) of the Internal Revenue Code of 1986, as amended.



\$6,330,000
LEMON GROVE COMMUNITY DEVELOPMENT AGENCY
(LEMON GROVE REDEVELOPMENT PROJECT AREA)
2004 TAX ALLOCATION BONDS
(Bank Qualified)

Dated: Date of Delivery

Due: August 1, as set forth below

Proceeds from the sale of the Lemon Grove Community Development Agency (the "Agency") (Lemon Grove Redevelopment Project Area) 2004 Tax Allocation Bonds (the "Bonds"), will be used to (i) finance redevelopment activities in its Lemon Grove Redevelopment Project Area, (ii) finance low and moderate income housing activities throughout the geographic boundaries of the City of Lemon Grove, (iii) make a deposit to a reserve account, and (iv) provide for the costs of issuing the Bonds.

Interest on the Bonds will be payable semi-annually on each February 1 and August 1, commencing February 1, 2005 (each, an "Interest Payment Date"). The Bonds will be issued in fully registered form without coupons and will be registered in the name of Cede & Co., as nominee for The Depository Trust Company, New York, New York ("DTC"). DTC will act as securities depository for the Bonds. Purchases of beneficial interests in the Bonds will be made in book-entry form only in denominations of \$5,000 or any integral multiple thereof. Purchasers of such beneficial interests will not receive physical certificates representing their interests in the Bonds. Payment of principal of, interest and premium, if any, on the Bonds will be made directly to DTC or its nominee, Cede & Co., so long as DTC or Cede & Co. is the registered owner of the Bonds. Disbursement of such payments to the DTC Participants (as defined herein) is the responsibility of DTC and disbursement of such payments to the Beneficial Owners (as defined herein) is the responsibility of the DTC Participants, as more fully described herein. See "THE BONDS—Book-Entry System" herein.

The Bonds will be issued under an Indenture of Trust, dated as of August 1, 2004 (the "Indenture"), by and between the Agency and U.S. Bank National Association, as trustee (the "Trustee"). The Bonds are special obligations of the Agency and are payable solely from and secured by a pledge of the Tax Revenues (as defined herein), subject to the provisions of the Indenture permitting the application thereof for other purposes, and by a pledge of amounts in certain funds and accounts established under the Indenture, as further discussed herein. The Bonds will be on a parity as to payment and security with the Agency's outstanding Lemon Grove Community Development Agency, Tax Allocation Bonds (1998 Refunding). The Bonds will be sold by the Agency to the Lemon Grove Financing Authority (the "Authority") for concurrent resale to the Underwriter named below.

The Bonds are subject to optional and mandatory redemption prior to maturity. See "THE BONDS—Redemption" herein.

THE BONDS ARE SPECIAL OBLIGATIONS OF THE AGENCY PAYABLE SOLELY FROM THE TAX REVENUES, AS DESCRIBED HEREIN, AND AMOUNTS IN CERTAIN FUNDS AND ACCOUNTS MAINTAINED UNDER THE INDENTURE AND, ARE NOT A DEBT OF THE AUTHORITY, THE CITY OF LEMON GROVE (THE "CITY") OR THE STATE OF CALIFORNIA (THE "STATE") OR ANY POLITICAL SUBDIVISIONS THEREOF (OTHER THAN THE AGENCY, TO THE LIMITED EXTENT SET FORTH IN THE INDENTURE), AND NEITHER THE AUTHORITY, THE CITY NOR THE STATE OR ANY POLITICAL SUBDIVISIONS THEREOF (OTHER THAN THE AGENCY), IS LIABLE THEREFOR. THE BONDS ARE NOT PAYABLE FROM, AND ARE NOT SECURED BY, ANY FUNDS OF THE AGENCY, OTHER THAN THE TAX REVENUES PLEDGED PURSUANT TO THE INDENTURE. THE BONDS DO NOT CONSTITUTE AN INDEBTEDNESS WITHIN THE MEANING OF ANY CONSTITUTIONAL OR STATUTORY DEBT LIMITATION OR RESTRICTION. NEITHER THE MEMBERS OF THE AGENCY NOR ANY PERSONS RESPONSIBLE FOR THE EXECUTION OF THE BONDS IS LIABLE PERSONALLY FOR PAYMENT OF THE BONDS BY REASON OF THEIR ISSUANCE.

Payment of principal of and interest on the Bonds will be insured in accordance with the terms of a financial guaranty insurance policy to be issued simultaneously with the delivery of the Bonds by RADIAN ASSET ASSURANCE INC.



MATURITY SCHEDULE

[See inside cover page]

This cover page contains information for quick reference only. It is not intended to be a summary of all factors relating to an investment in the Bonds. Investors should review the entire Official Statement before making any investment decision with respect to the Bonds.

The Bonds are offered when, as and if issued, subject to the approval as to their legality by Stradling Yocca Carlson & Rauth, a Professional Corporation, Newport Beach, California, Bond Counsel, and subject to certain other conditions. Certain legal matters will be passed upon for the Agency by McDougal, Love, Eckis, Smith, Boehmer & Foley, El Cajon, California, as Agency Counsel, and by Quint & Thimmig LLP, San Francisco, California, as Disclosure Counsel. It is anticipated that the Bonds will be available for delivery through DTC in New York, New York, on or about August 10, 2004.



Dated: July 28, 2004

\$6,330,000
LEMON GROVE COMMUNITY DEVELOPMENT AGENCY
(LEMON GROVE REDEVELOPMENT PROJECT AREA)
2004 TAX ALLOCATION BONDS
(Bank Qualified)

MATURITY SCHEDULE

\$740,000 Serial Bonds

CUSIP Prefix: 525638†

<u>Maturity (August 1)</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield</u>	<u>CUSIP Suffix†</u>	<u>Maturity (August 1)</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield</u>	<u>CUSIP Suffix†</u>
2005	\$150,000	3.00 %	1.90%	AS1	2013	\$20,000	4.00 %	4.30%	BB7
2006	150,000	3.00	2.15	AT9	2014	25,000	4.125	4.40	BC5
2007	150,000	3.00	2.55	AU6	2015	25,000	4.30	4.52	BE1
2008	20,000	2.75	3.05	AV4	2016	25,000	4.40	4.61	BF8
2009	20,000	3.10	3.40	AW2	2017	25,000	4.50	4.70	BG6
2010	20,000	3.375	3.65	AY8	2018	30,000	4.60	4.80	BH4
2011	25,000	3.625	3.92	AZ5	2019	30,000	4.70	4.90	BJ0
2012	25,000	3.80	4.12	BA9					

\$1,090,000 5.00% Term Bonds due August 1, 2029—Not Reoffered; CUSIP 525638 BM3†

\$2,475,000 5.00% Term Bonds due August 1, 2034—Not Reoffered; CUSIP 525638 BP6†

\$640,000 Escrowed Serial Bonds

CUSIP Prefix: 525638†

<u>Maturity (August 1)</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield</u>	<u>CUSIP Suffix†</u>	<u>Maturity (August 1)</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield</u>	<u>CUSIP Suffix†</u>
2007	\$60,000	2.25 %	2.60%	BR2	2014	\$50,000	4.125%	4.40%	BD3
2008	40,000	2.75	3.05	BS0	2015	50,000	4.30	4.52	BX9
2009	40,000	3.10	3.40	AX0	2016	55,000	4.40	4.61	BY7
2010	40,000	3.375	3.65	BT8	2017	55,000	4.50	4.70	BZ4
2011	40,000	3.625	3.92	BU5	2018	55,000	4.60	4.80	CA8
2012	45,000	3.80	4.12	BV3	2019	60,000	4.70	4.90	BK7
2013	50,000	4.00	4.30	BW1					

\$355,000 5.00% Escrowed Term Bonds due August 1, 2024—Price 98.754%, to Yield 5.10%; CUSIP 525638 BL5†

\$445,000 5.125% Escrowed Term Bonds due August 1, 2029—Price 97.590%, to Yield 5.30%; CUSIP 525638 BN1†

\$585,000 5.40% Escrowed Term Bonds due August 1, 2034—Price 100%, to Yield 5.40%; CUSIP 525638 BQ4†

†CUSIP numbers are provided for reference only. Neither the Authority nor the Underwriter assume any responsibility for the accuracy of such numbers.

LEMON GROVE COMMUNITY DEVELOPMENT AGENCY
and
CITY OF LEMON GROVE

Agency Board and City Council

Mary Teresa Sessom, *Chair/Mayor*
Jerry Jones, *Vice Chair/Mayor Pro Tem*
Tom Clabby, *Board Member/Council Member*
Mary England, *Board Member/Council Member*
Jill Greer, *Board Member/Council Member*

Agency and City Staff and Officials

Graham Mitchell, *Executive Director/City Manager*
Christine Taub, *Treasurer and Secretary/Finance Director/City Clerk*
James Lough, Esq., *City Attorney*

Special Services

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Newport Beach, California
Bond Counsel

Urban Futures, Inc.
Orange, California
Financial Advisor

Quint & Thimmig LLP
San Francisco, California
Disclosure Counsel

U.S. Bank National Association
Los Angeles, California
Trustee

No dealer, broker, salesperson or other person has been authorized by the Agency to give any information or to make any representations in connection with the offer or sale of the Bonds other than those contained herein and, if given or made, such other information or representations must not be relied upon as having been authorized by the Agency. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of the Bonds by a person in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale.

This Official Statement is not to be construed as a contract with the purchasers of the Bonds. Statements contained in this Official Statement which involve estimates, forecasts or matters of opinion, whether or not expressly so described herein, are intended solely as such and are not to be construed as representations of fact.

The information set forth herein has been obtained from sources which are believed to be reliable but such information is not guaranteed as to accuracy or completeness. The information and expressions of opinions herein are subject to change without notice and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the Agency since the date hereof. The Underwriter has provided the following sentence for inclusion in this Official Statement: The Underwriter has reviewed the information in this Official Statement in accordance with and as part of this transaction but the Underwriter does not guarantee the accuracy or completeness of such information. All summaries of the Indenture and other documents are made subject to the provisions of such documents and do not purport to be complete statements of any or all such provisions.

This Official Statement is submitted in connection with the sale of the Bonds referred to herein and may not be reproduced or used, in whole or in part, for any other purpose.

OTHER THAN WITH RESPECT TO INFORMATION CONCERNING RADIAN ASSET ASSURANCE INC. CONTAINED UNDER THE CAPTION "FINANCIAL GUARANTY INSURANCE" HEREIN AND IN APPENDIX G HERETO, NONE OF THE INFORMATION IN THIS OFFICIAL STATEMENT HAS BEEN SUPPLIED OR VERIFIED BY RADIAN ASSET ASSURANCE INC., AND RADIAN ASSET ASSURANCE INC. MAKES NO REPRESENTATION OR WARRANTY, EXPRESS OR IMPLIED, AS TO: (i) THE ACCURACY OR COMPLETENESS OF SUCH INFORMATION; (ii) THE VALIDITY OF THE BONDS; OR (iii) THE TAX STATUS OF THE INTEREST ON THE BONDS.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITER MAY OVERALLOT OR EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICE OF THE BONDS AT A LEVEL ABOVE THAT WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME. THE UNDERWRITER MAY OFFER AND SELL THE BONDS TO CERTAIN DEALERS AND DEALER BANKS AND BANKS ACTING AS AGENT AT PRICES LOWER THAN THE PUBLIC OFFERING PRICES STATED ON THE COVER PAGE HEREOF AND SAID PUBLIC OFFERING PRICES MAY BE CHANGED FROM TIME TO TIME BY THE UNDERWRITER.

This Official Statement contains forward looking statements by the Agency concerning future conditions affecting the Agency, the City, the State and the United States which may relate to its business operations and financial condition of the Agency. The Official Statement contains the words or phrases "will likely result," "are expected to," "will continue," "is anticipated," "estimate," "project," "forecast," "expect," "intend" or variations of those terms to identify "forward looking statements" within the meaning of the U.S. Private Securities Litigation Reform Act of 1995 Section 21E of the U.S. Securities and Exchange Act of 1934, as amended, and Section 27A of the U.S. Securities and Exchange Act of 1933, as amended. You should not rely on these forward-looking statements which speak only as to the Agency's expectations as of the date of this Official Statement. Such statements are subject to risks and uncertainties that could cause actual results to differ materially from those contemplated in such forward-looking statements. Except as required by law, neither the Agency, the City or the Underwriter undertake any duty to update any forward looking statements after the date of this Official Statement, either to confirm any statement to reflect actual results or to reflect the occurrence of unanticipated events.

THE BONDS HAVE NOT BEEN REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED, IN RELIANCE UPON AN EXCEPTION FROM THE REGISTRATION REQUIREMENTS CONTAINED IN SECTION 3(a)(2) OF SUCH ACT. THE BONDS HAVE NOT BEEN REGISTERED OR QUALIFIED UNDER THE SECURITIES LAWS OF ANY STATE. THE INDENTURE HAS NOT BEEN QUALIFIED UNDER THE TRUST INDENTURE ACT OF 1939, AS AMENDED, IN RELIANCE UPON AN EXEMPTION CONTAINED IN SUCH ACT.

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LOCATION MAP



OFFICIAL STATEMENT

\$6,330,000
LEMON GROVE COMMUNITY DEVELOPMENT AGENCY
(Lemon Grove Redevelopment Project Area)
2004 Tax Allocation Bonds

INTRODUCTION

General

This Official Statement of the Lemon Grove Community Development Agency (the "Agency") provides information regarding the sale by the Agency of \$6,330,000 aggregate principal amount of the Agency's Lemon Grove Community Development Agency (Lemon Grove Redevelopment Project Area) 2004 Tax Allocation Bonds (the "Bonds").

Definitions of certain capitalized terms used in this Official Statement are set forth in APPENDIX D—"SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE." This Official Statement contains brief descriptions of the Bonds, the Indenture, the Project Area and the Agency. Such descriptions do not purport to be comprehensive or definitive. All references in this Official Statement to specific documents are qualified in their entirety by reference to such documents and references to the Bonds are qualified in their entirety by reference to the form of the Bonds included in the Indenture. Copies of the Indenture and other documents described in this Official Statement may be obtained from the Agency as described under the subheading "Other Information" below.

Purpose of Issuance

The Bonds will be purchased by the Lemon Grove Financing Authority, a joint exercise of powers authority created by the City and the Agency (the "Authority"), from the Agency for immediate re-sale to Kinsell, Newcomb & De Dios, Inc. (the "Underwriter").

Proceeds from the sale of the Bonds will be used to (i) finance redevelopment activities within or to the benefit of the Agency's Lemon Grove Redevelopment Project Area (the "Project Area"), (ii) finance low and moderate income housing activities within the geographic boundaries of the City of Lemon Grove, (iii) fund an escrow fund which will, upon evidence of increased Tax Revenues, will be released to the Agency for additional redevelopment and low and moderate income housing activities, (iv) fund capitalized interest with respect to the Escrowed Bonds through August 1, 2006, (v) make a deposit to the Reserve Account; and (vi) provide for the costs of issuing the Bonds. See "ESTIMATED SOURCES AND USES OF FUNDS" herein.

The Agency

The Agency was established pursuant to the Redevelopment Law. The City Council of the City of Lemon Grove (the "City") activated the Agency in May, 1986. The Agency is governed by a five-member board which consists of all members of the City Council of the City. The Mayor of the City serves as Chairman of the Agency. The Mayor is elected directly and the four members of the City Council are elected at large. See "THE AGENCY" herein.

The Project Area

The Redevelopment Plan (the "Redevelopment Plan") for the Lemon Grove Redevelopment Project (the "Project Area") was approved and adopted by the City on November 17, 1986, by adoption of Ordinance No. 132. The Project Area encompasses approximately 618 acres and is located between the northerly portion of the City's eastern and western boundaries and, with its southerly extension along most of the length of Lemon Grove Avenue and a small area on Skyline Drive, includes almost all of the City's land which is zoned for commercial and industrial use. Major roadways within the Project Area are Federal Boulevard, Broadway, Lemon Grove Avenue, Lemon Grove Way and Grove Street. The total assessed valuation of taxable property in the Project Area in Fiscal Year 2003-2004 was approximately \$161,686,461 greater than the adjusted assessed valuation in the base year. See "THE PROJECT AREA" herein. Assessed valuations in the Project Area are subject to numerous risks which could result in decreases from those reported for Fiscal Year 2003-2004. See "BONDOWNERS' RISKS" herein.

The Bonds

The Bonds are being issued pursuant to the laws of the State of California (the "State"), including the provisions of the Community Redevelopment Law of the State, constituting Part 1 of Division 24 of the California Health and Safety Code (the "Law"), a resolution adopted by the Agency on July 6, 2004 (the "Resolution"), and an Indenture of Trust, dated as of August 1, 2004 (the "Indenture"), by and between the Agency and U.S. Bank National Association, as trustee (the "Trustee"). See "THE BONDS" herein and APPENDIX D—"SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE." The Bonds will be on a parity as to payment and security with the Agency's Lemon Grove Community Development Agency, Tax Allocation Bonds (1998 Refunding), currently outstanding in the principal amount of \$9,090,000 (the "1998 Bonds").

The Bonds will be issued in denominations of \$5,000 each or integral multiples thereof. Interest on the Bonds will be payable on each February 1 and August 1, commencing on February 1, 2005. Interest and principal on the Bonds are payable by the Trustee to DTC which will be responsible for remitting such principal and interest to the Participants which will in turn be responsible for remitting such principal and interest to the beneficial owners of the Bonds. No physical distribution of the Bonds will be made to the public initially. See "THE BONDS—Book-Entry System" herein.

Source of Payment for the Bonds

The Bonds are special obligations of the Agency and are payable from and secured by a pledge of Tax Revenues and amounts in certain funds and accounts held under the Indenture. The term "Tax Revenues" is defined in the Indenture as that portion of taxes levied upon taxable property in the Project Area and received by the Agency on or after the date of issue of the Bonds, for the Project Area of the Agency pursuant to Article 6 of Chapter 6 of the Law and Section 16 of Article XVI of the Constitution of the State excluding therefrom the portion of taxes which are attributable to a tax rate levied by a taxing agency for the purpose of producing revenues in an amount sufficient to make annual payments of principal of and interest on any bonded indebtedness approved by the voters of the taxing agency on or after January 1, 1989 for the acquisition or improvement of real property, which portion shall be allocated to, and when collected shall be paid into the fund of that taxing agency but, including that portion of such taxes otherwise required by Section 33334.2 of the Law to be deposited in the Low and Moderate Income Housing Fund, but only to the extent necessary to repay that portion of the Bonds and any Parity Bonds (to the extent that portion of Tax Revenues are pledged thereto) which were issued or which shall

be issued to finance amounts deposited in the Low and Moderate Income Housing Fund for use pursuant to Section 33334.2 of the Law; but excluding all other amounts of such taxes (if any) (i) required to be deposited into the Low and Moderate Income Housing Fund of the Agency pursuant to Section 33334.2 of the Law and (ii) payable or required to be set aside by the Agency under the Pass-Through Agreements.

The Tax Revenues are not subject to the pledge and lien of any indebtedness of the Agency other than the 1998 Bonds, the Bonds and any Parity Debt issued in accordance with the Indenture, and certain other obligations which have been made or are by their terms subordinate to the payment of the 1998 Bonds and the Bonds. See "LIMITATION ON TAX REVENUES" and "THE AGENCY—Outstanding Indebtedness of the Agency" herein. The Bonds are not payable from, and are not secured by, any funds of the Agency other than the Tax Revenues and amounts in certain funds and accounts pledged therefore under the Indenture. See "SECURITY FOR THE BONDS" herein.

Financial Guaranty Insurance

The scheduled payment of principal of and interest on the Bonds when due will be guaranteed under a financial guaranty insurance policy (the "Financial Guaranty Insurance Policy") to be issued concurrently with the delivery of the Bonds by Radian Asset Assurance Inc. (the "Bond Insurer"). See "FINANCIAL GUARANTY INSURANCE" herein.

Parity Debt

The Indenture provides that in addition to the 1998 Bonds and the Bonds, the Agency may, by the execution of a Supplemental Indenture, provide for the issuance of one or more series of Parity Debt secured by a lien on Tax Revenues on a parity with the Bonds and the 1998 Bonds to finance redevelopment activities in the Project Area or low and moderate income projects in such principal amount as shall be determined by the Agency. The Agency may deliver Parity Debt subject to certain specific conditions set forth in the Indenture. See "SECURITY FOR THE BONDS—Issuance of Parity Debt."

Bond Owners' Risks

Prospective investors should review this Official Statement and the Appendices hereto in their entirety and should consider certain risk factors associated with the purchase of the Bonds, some of which have been summarized in the section herein entitled "BONDOWNERS' RISKS" herein.

Continuing Disclosure

The Agency will covenant, pursuant to a Continuing Disclosure Agreement to be executed on the date of delivery of the Bonds, for the benefit of owners and beneficial owners of the Bonds, to provide certain financial information and operating data related to the Agency by not later than February 15 following the end of the Agency's Fiscal Year (the "Annual Report"), and to provide notices of the occurrence of certain enumerated events, if material. The Annual Report will be filed by the Agency with each Nationally Recognized Municipal Securities Information Repository (as defined in the Continuing Disclosure Agreement), and with the appropriate State information depository, if any. The notices of material events will be filed by the Agency with the Municipal Securities Rulemaking Board (and with the appropriate State information depository, if any). The specific nature of the information to be contained in the Annual Report and any notices of material events is summarized below under the caption "CONTINUING DISCLOSURE" herein. A copy of the Continuing Disclosure Agreement is set forth in APPENDIX F—"FORM OF

CONTINUING DISCLOSURE AGREEMENT.” The covenants of the Agency in the Continuing Disclosure Agreement have been made in order to assist the Underwriter in complying with S.E.C. Rule 15c2-12(b)(5).

Tax Matters

In the opinion of Stradling Yocca Carlson & Rauth, Newport Beach, California, Bond Counsel, under existing law, the interest on the Bonds is exempt from personal income taxes of the State and, assuming compliance with the tax covenants described herein, interest on the Bonds is excluded pursuant to section 103(a) of the Internal Revenue Code of 1986 from the gross income of the owners thereof for federal income tax purposes and is not an item of preference for purposes of the federal alternative minimum tax. See “TAX MATTERS” herein.

Professionals Involved in the Offering

The proceedings of the Agency in connection with the issuance of the Bonds are subject to the approval as to their legality of Stradling Yocca Carlson & Rauth, Newport Beach, California, Bond Counsel for the Bonds. Quint & Thimmig LLP, San Francisco, California, is serving as Disclosure Counsel to the Agency for the Bonds. Certain legal matters will be passed upon for the Agency by McDougal, Love, Eckis, Smith, Boehmer & Foley, El Cajon, California as counsel to the Agency. U.S. Bank National Association, Los Angeles, California, will act as the Trustee under the Indenture. Urban Futures, Inc., Orange, California, will act as financial advisor to the Agency in connection with the issuance of the Bonds. The fees of Stradling Yocca Carlson & Rauth, Quint & Thimmig LLP, Urban Futures, Inc. and U.S. Bank National Association are contingent upon the sale and delivery of the Bonds.

Other Information

This Official Statement speaks only as of its date and the information contained herein is subject to change without notice. Copies of documents referred to herein are available from the Agency upon written request to the Lemon Grove Community Development Agency, 3232 Main Street, Lemon Grove, CA 91945, Attention: Executive Director. The Agency may impose a charge for copying, mailing and handling expenses related to any request for documents.

ESTIMATED SOURCES AND USES OF FUNDS

The following table sets forth a summary of the estimated sources and uses of funds associated with the issuance and sale of the Bonds.

Sources of Funds

Par Amount of Bonds	\$6,330,000.00
Less: Original Issue Discount	(186,293.05)
Less: Underwriter's Discount	<u>(79,125.00)</u>
Total Sources	<u>\$6,064,581.95</u>

Uses of Funds

Deposit to Redevelopment Fund	\$1,642,162.55
Deposit to Housing Fund	1,583,009.14
Deposit to Escrowed Proceeds Fund (1)	2,216,187.41
Deposit to Reserve Account (2)	323,661.48
Deposit to Costs of Issuance Account (3)	<u>299,561.37</u>
Total Uses	<u>\$6,064,581.95</u>

-
- (1) Amounts deposited in the Escrowed Proceeds Fund will be released to the Agency periodically upon a demonstration that Tax Revenues are sufficient to pay debt service on the Escrowed Bonds allocable to such released amounts. See "SECURITY FOR THE BONDS—Escrowed Proceeds Fund" herein. Includes capitalized interest on the Escrowed Bonds through August 1, 2006.
 - (2) See "SECURITY FOR THE BONDS—Reserve Account" herein. The amount derived from Bond proceeds will be the amount required to increase the total amount on deposit in the Reserve Account to the Reserve Account Requirement.
 - (3) Includes fees and expenses of Bond Counsel, Disclosure Counsel and the Financial Advisor, premium for the Financial Guaranty Insurance Policy, printing expenses, Trustee fees and other costs of issuance.

DEBT SERVICE SCHEDULE

The following table sets forth the scheduled annual debt service for the Bonds.

Bond Year Ending (August 1)	Non-Escrowed Bonds		Escrowed Bonds		Total Debt Service
	Principal*	Interest	Principal*	Interest	
2005	\$150,000	\$198,288.19	—	\$94,383.66	\$ 442,671.85
2006	150,000	198,872.50	—	96,803.76	445,676.26
2007	150,000	194,372.50	\$ 60,000	96,803.76	501,176.26
2008	20,000	189,872.50	40,000	95,453.76	345,326.26
2009	20,000	189,322.50	40,000	94,353.76	343,676.26
2010	20,000	188,702.50	40,000	93,113.76	341,816.26
2011	25,000	188,027.50	40,000	91,763.76	344,791.26
2012	25,000	187,121.26	45,000	90,313.76	347,435.02
2013	20,000	186,171.26	50,000	88,603.76	344,775.02
2014	25,000	185,371.26	50,000	86,603.76	346,975.02
2015	25,000	184,340.00	50,000	84,541.26	343,881.26
2016	25,000	183,265.00	55,000	82,391.26	345,656.26
2017	25,000	182,165.00	55,000	79,971.26	342,136.26
2018	30,000	181,040.00	55,000	77,496.26	343,536.26
2019	30,000	179,660.00	60,000	74,966.26	344,626.26
2020	35,000	178,250.00	65,000	72,146.26	350,396.26
2021	35,000	176,500.00	70,000	68,896.26	350,396.26
2022	35,000	174,750.00	70,000	65,396.26	345,146.26
2023	40,000	173,000.00	75,000	61,896.26	349,896.26
2024	35,000	171,000.00	75,000	58,146.26	339,146.26
2025	40,000	169,250.00	80,000	54,396.26	343,646.26
2026	45,000	167,250.00	85,000	50,296.26	347,546.26
2027	40,000	165,000.00	90,000	45,940.02	340,940.02
2028	45,000	163,000.00	95,000	41,327.50	344,327.50
2029	740,000	160,750.00	95,000	36,458.76	1,032,208.76
2030	780,000	123,750.00	105,000	31,590.00	1,040,340.00
2031	820,000	84,750.00	110,000	25,920.00	1,040,670.00
2032	400,000	43,750.00	115,000	19,980.00	578,730.00
2033	230,000	23,750.00	125,000	13,770.00	392,520.00
2034	245,000	12,250.00	130,000	7,020.00	394,270.00

*Principal amounts include mandatory sinking account payments.

THE BONDS

General Provisions

The Bonds will be issued and sold in the initial aggregate principal amount of \$6,330,000. The Bonds will be delivered in fully registered form, without coupons, in the denomination of \$5,000 each or any integral multiple thereof. Interest on the Bonds will be payable semiannually on February 1 and August 1 of each year, commencing February 1, 2005 (each, an "Interest Payment Date"), to the Owner thereof as of the close of business on the fifteenth (15th) calendar day of the month preceding each Interest Payment Date, whether or not such fifteenth (15th) calendar day is a business day (each, a "Record Date"). Principal of the Bonds will be payable on August 1 in each of the years and in the amounts shown on the cover page hereof.

The Bonds will be dated as of their date of delivery. Each Bond will bear interest from the Interest Payment Date next preceding the date of authentication thereof, unless (i)

it is executed during the period from the day after the Record Date for an Interest Payment Date to and including such Interest Payment Date, in which event it will bear interest from such Interest Payment Date, or (ii) it is executed on or prior to the Record Date for the first Interest Payment Date, in which event it will bear interest from the date of its initial delivery; provided, however, that if, at the time of registration of any Bond interest with respect to such Bond is in default, such Bond will bear interest from the Interest Payment Date to which interest has been paid or made available for payment with respect to such Bond.

Interest with respect to any Bond will be payable in lawful money of the United States of America on each Interest Payment Date to the Owner thereof as of the close of business on the Record Date, such interest to be paid by check of the Trustee, mailed by first class mail no later than the Interest Payment Date to the Owner at his address as it appears, on such Record Date, on the bond registration books maintained by the Trustee; provided, however, that at the written request of the Owner of at least \$1,000,000 in aggregate principal amount of Outstanding Bonds filed with the Trustee prior to any Record Date, interest on such Bonds will be paid to such Owner on each succeeding Interest Payment Date (unless such request has been revoked in writing) by wire transfer of immediately available funds to an account in the continental United States designated in such written request. Payments of defaulted interest with respect to the Bonds will be paid by check to the registered Owners of the Bonds as of a special record date to be fixed by the Trustee, notice of which special record date shall be given to the Owners of the Bonds not less than ten days prior thereto. The principal of and premium, if any, on the Bonds are payable when due upon surrender thereof at the principal corporate trust office of the Trustee in Los Angeles, California, in lawful money of the United States of America.

Redemption

Optional Redemption of Bonds. The Bonds maturing on or after August 1, 2015 are subject to redemption prior to maturity at the option of the Agency on any date on or after August 1, 2014, as a whole or in part among maturities designated by the Agency and by lot within a maturity, from any source of available funds at a redemption price equal to the principal amount thereof to be redeemed, without premium, together with accrued interest thereon to the date fixed for redemption. The date on which Bonds are to be presented for redemption is sometimes referred to as the "redemption date."

Sinking Account Redemption of Non-Escrowed Term Bonds. The Bonds maturing on August 1, 2029, and August 1, 2034, other than the Escrowed Term Bonds maturing on August 1, 2029, and August 1, 2034 (the "Non-Escrowed Term Bonds"), are subject to mandatory redemption on each August 1, commencing on August 1, 2020, and August 1, 2030, respectively, at a redemption price equal to the principal amount thereof together with accrued interest thereon, if any, to the redemption date, without premium from minimum sinking account payments made by the Agency, in the years and amounts as follows:

2029 Non-Escrowed Term Bonds	
<u>Year</u>	<u>Principal Amount</u>
2020	\$ 35,000
2021	35,000
2022	35,000
2023	40,000
2024	35,000
2025	40,000
2026	45,000
2027	40,000
2028	45,000
2029+	740,000

†Maturity

2034 Non-Escrowed Term Bonds	
<u>Year</u>	<u>Principal Amount</u>
2030	\$780,000
2031	820,000
2032	400,000
2033	230,000
2034+	245,000

†Maturity

Sinking Account Redemption of Escrowed Term Bonds. The Escrowed Bonds maturing on August 1, 2024, August 1, 2029, and August 1, 2034 (the “Escrowed Term Bonds”), are subject to mandatory redemption on each August 1, commencing on August 1, 2020, August 1, 2025, and August 1, 2030, respectively, at a redemption price equal to the principal amount thereof together with accrued interest thereon, if any, to the redemption date, without premium from minimum sinking account payments made by the Agency, in the years and amounts as follows:

2024 Escrowed Term Bonds	
<u>Year</u>	<u>Principal Amount</u>
2020	\$65,000
2021	70,000
2022	70,000
2023	75,000
2024+	75,000

†Maturity

2029 Escrowed Term Bonds	
<u>Year</u>	<u>Principal Amount</u>
2025	\$80,000
2026	85,000
2027	90,000
2028	95,000
2029+	95,000

†Maturity

2034 Escrowed Term Bonds	
<u>Year</u>	<u>Principal Amount</u>
2030	\$105,000
2031	110,000
2032	115,000
2033	125,000
2034+	130,000

†Maturity

Mandatory Redemption of Escrowed Bonds. The Escrowed Bonds are subject to special redemption, in part, in inverse order of each maturity of the Escrowed Bonds, as directed by the Agency at a redemption price of 100% of the principal amount thereof plus accrued interest to the redemption date without premium, on August 1, 2006, to the extent of any moneys remaining in the Escrowed Proceeds Fund on June 15, 2006. See "SECURITY FOR THE BONDS—Escrowed Proceeds Fund."

Call and Redemption; Notice of Redemption. The Agency may, by resolution, direct the call and redemption prior to maturity of Bonds by the Trustee in such amounts as there are funds available for use in redemption and shall give notice to the Trustee of the redemption at least sixty (60) days prior to the redemption date (or such shorter period as may be agreed upon by the Agency and Trustee); *provided, however*, that there shall be no optional redemption of the Bonds unless all amounts owed to the Bond Insurer under the terms of the Financial Guaranty Insurance Policy or any other documents have been paid in full.

Notice of redemption prior to maturity shall be given by first class mail, postage prepaid not less than thirty (30) nor more than sixty (60) days prior to the redemption date to the registered owner of each such Bond at the address shown on the registration books of the Trustee. Neither the failure to receive such notice nor any defect in any notice mailed shall affect the sufficiency of the proceedings for the redemption of any Bonds. The notice of redemption shall: (a) state the redemption date; (b) state the redemption price; (c) state the numbers of the Bonds to be redeemed; *provided, however*, that whenever any call for redemption includes all of the Outstanding Bonds, the numbers of the Bonds need not be stated; (d) state, as to any Bonds redeemed in part only, the Bond numbers and the principal portion thereof to be redeemed; (e) state that interest on the principal portion of the Bonds designated for redemption shall cease to accrue from and after the redemption date and that on the redemption date there shall become due and payable on each of such Bonds the redemption price for each Bond; and (f) state that the redemption of the Bonds is subject to there being on deposit with the Trustee at the time of such redemption, moneys sufficient to redeem the portion of the Bonds as set forth in the notice. No notice of shall be until such time as there is on deposit moneys sufficient to redeem that portion of the Bonds as set forth in the notice.

The actual receipt by the Bondowner of notice of redemption shall not be a condition precedent to redemption, and failure to receive notice shall not affect the validity of the proceedings for the redemption of the Bonds or the cessation of interest on the redemption date. Notice of redemption of Bonds shall be given by the Trustee on behalf of the Agency and at the request and expense of the Agency.

Partial Redemption of Bonds. Upon surrender of any Bond redeemed in part only, the Agency shall execute and the Trustee shall authenticate and deliver to the registered owner, at the expense of the Agency, a new Bond or Bonds of authorized denominations equal in aggregate principal amount to the unredeemed portion of the Bond surrendered and of the same interest rate and same maturity. A partial redemption shall be valid upon payment of

the amount required to be paid to the registered owner, and the Agency and the Trustee shall be released and discharged from all liability to the extent of such payment.

Effect of Redemption. Notice of redemption having been duly given as provided above, and moneys for payment of the principal of, premium, if any, and interest payable upon redemption of the Bonds being set aside as provided above, the Bonds, or parts thereof, called for redemption shall, on the redemption date, become due and payable at the redemption price specified in the notice. Interest on the Bonds, or parts thereof, as the case may be, called for redemption shall cease to accrue and be payable from and after the redemption date. The Bonds, or parts thereof redeemed, shall cease to be entitled to any lien, benefit or security under the Indenture, and the Owners of the Bonds shall have no rights except to receive payment of the redemption price upon surrender of the Bonds, and, in the case of partial redemption of Bonds, also to receive a new Bond or Bonds for the unredeemed balance as provided above. All Bonds, or parts thereof, as the case may be, redeemed pursuant to the provisions hereof shall be cancelled upon surrender thereof and delivered to, or destroyed upon the order of the Agency.

Purchase of Bonds. In lieu of redemption or otherwise, the Agency is hereby authorized to purchase Bonds on the open market at any time and the Trustee will upon written direction of the Agency settle these purchases from moneys deposited by the Agency with the Trustee at a price not to exceed the principal amount of Bonds plus the applicable premium and accrued interest, if any, to the date of purchase plus brokerage fees, if any.

Book-Entry System

The Bonds will be subject to a book-entry system of registration, transfer and payment and each Bond will initially be registered in the name of Cede & Co, as nominee of The Depository Trust Company, New York, New York ("DTC"). As part of such book-entry system, DTC has been appointed securities depository for the Bonds, and registered ownership may not thereafter be transferred except as provided in the Indenture. The Bonds are being delivered in book-entry form only. Purchasers will not receive securities certificates representing their interests in the Bonds. Rather, in accordance with the book-entry system, purchasers of the Bonds will have beneficial ownership interest in the purchased Bonds through DTC Participants (as hereinafter defined). For more information concerning the book-entry system, see APPENDIX G—"BOOK-ENTRY SYSTEM."

SECURITY FOR THE BONDS

Tax Revenues

Tax Allocations. The Law provides a means for financing redevelopment projects based upon an allocation of taxes collected within a project area. The taxable valuation of a project area last equalized prior to adoption of the redevelopment plan, or base roll, is established as of the adoption of the redevelopment plan. Thereafter, except for any period during which the taxable valuation drops below the base year level, the taxing bodies receive the taxes produced by the levy of the then current tax rate upon the base roll. Taxes collected upon any increase in taxable valuation over the base roll (with the exception of taxes derived from increases in the tax rate imposed by Taxing Agencies (hereinafter defined) to support new bonded indebtedness) are allocated to the redevelopment agency and may be pledged to the repayment of any indebtedness incurred in financing or refinancing redevelopment. Redevelopment agencies themselves have no authority to levy property taxes and must look exclusively to such allocation of taxes.

As provided in the redevelopment plan for the project area, and pursuant to Article 6 of Chapter 6 of the Redevelopment Law and Section 16 of Article XVI of the State Constitution, taxes levied upon taxable property in the Project Area each year by or for the benefit of the State, cities, counties, districts or other public corporations (collectively, the "Taxing Agencies"), for fiscal years beginning after the effective date of the redevelopment plan, will be divided as follows:

(1) *To Taxing Agencies:* The portion equal to the amount of those taxes which would have been produced by the then current tax rate, applied to the taxable valuation of such property in the redevelopment project area as last equalized prior to the establishment of the redevelopment project, or base roll, is paid into the funds of those respective Taxing Agencies as taxes by or for said Taxing Agencies; and

(2) *To the Agency:* The portion of said levied taxes each year in excess of the amount referred to in (1) above (the "Tax Increment Revenues") is allocated to, and when collected, is paid to the agency; provided that the portion of the Tax Increment Revenues which are attributable to a tax rate levied by a taxing agency to pay indebtedness approved by the voters of that taxing agency on or after January 1, 1989, shall be allocated to, and when collected shall be paid into, the fund of such taxing agency.

Housing Set-Aside Amounts. The Law requires generally that, unless a specified finding is made, redevelopment agencies set aside 20% of all Tax Increment Revenues derived from redevelopment project areas into a low and moderate income housing fund (the "Low and Moderate Income Housing Fund"), to be used for the purpose of increasing, improving and or preserving the supply of low and moderate income housing. Section 33334.2 of the Redevelopment Law dictates the low and moderate income housing set-aside requirement for each project area. See "LIMITATIONS ON TAX REVENUES—Low and Moderate Income Housing" herein. The Agency has made no such finding and is, therefore, obligated to make such set-aside.

Tax Sharing Agreements

Prior to 1994, under the Redevelopment Law, a redevelopment agency could enter into an agreement to pay increment revenues to any taxing agency that has territory located within a redevelopment project in an amount which in the agency's determination is appropriate to alleviate any financial burden or detriment caused by the redevelopment project. These agreements normally provide for a pass-through of tax increment revenue directed to the affected taxing agency, and, therefore, are commonly referred to as pass-through agreements or tax sharing agreements. Pursuant to the Redevelopment Law, the Agency entered into a tax sharing agreement with San Diego County (the "County") and a tax sharing agreement with the Lemon Grove School District (the "School District") with respect to tax increment revenues relating to the Project Area. In addition, certain amounts of tax increment revenue otherwise payable to the Agency with respect to the Project Area are paid to the Grossmont Union High School District and the Grossmont-Cuyamaca Community College District pursuant to a finding of the San Diego County Auditor Controller. The tax sharing agreements with the County and with School District, as well as the amounts due to the Grossmont Union High School District and the Grossmont-Cuyamaca Community College District are referred to herein as the "Tax Sharing Obligations." Except for the amounts due under the tax sharing agreement with the School District, which are subordinate to the Bonds, amounts of tax increment revenues payable under the Tax Sharing Obligations are excluded from the calculations of Tax Revenues herein. See "THE PROJECT AREA—Tax Sharing Obligations."

Pledge of Tax Revenues

The Bonds and all payments required of the Agency under the Indenture are not general obligations of the Agency but are limited special obligations of the Agency and, excluding therefrom, the Escrowed Bonds, are secured by an irrevocable pledge of, and are payable on a parity with the 1998 Bonds as to principal and interest, from Tax Revenues and other funds as hereinafter described. The Escrowed Bonds are secured by and payable solely from moneys on deposit in the Escrowed Proceeds Fund. The Bonds and interest thereon are not a debt of the City, the State or any of its political subdivisions, and neither the City, the State nor any of its political subdivisions is liable on them. In no event shall the Bonds or interest thereon be payable out of any funds or properties other than those of the Agency as set forth in the Indenture. The Bonds do not constitute an indebtedness within the meaning of any constitutional or statutory debt limitation or restriction. Neither the members of the Agency nor any persons executing the Bonds are liable personally on the Bonds by reason of their issuance.

The Bonds, excluding therefrom, the Escrowed Bonds, are secured on a parity with the 1998 Bonds by an irrevocable pledge of the Tax Revenues and other funds as hereinafter provided, without priority for number, date of sale, date of execution or date of delivery, except as expressly provided herein.

The Tax Revenues and all moneys held in the Special Fund or any of the Accounts thereunder and the Redemption Fund are conveyed, pledged and assigned absolutely and as a first lien pledge as security for the equal and ratable benefit of the owners of the Bonds and shall be used for no other purpose than payment of the principal of, premium (if any) and interest on the Bonds, except as may be otherwise expressly authorized in the Indenture.

The Indenture shall be deemed to be and shall constitute a contract between the Agency and the Owners from time to time of the Bonds, and the covenants and agreements therein set forth to be performed on behalf of the Agency shall be for the equal and proportionate benefit, security and protection of all Owners of the Bonds without preference, priority or distinction as to security or otherwise of any of the Bonds over any of the others by reason of the number or date thereof or the time of sale, execution and delivery thereof, or otherwise for any cause whatsoever, except as expressly provided therein.

The Agency has no power to levy and collect property taxes, and any property tax limitation, legislative measure, voter initiative or provision of additional sources of income to Taxing Agencies having the effect of reducing the property tax rate or collections, could reduce the amount of Tax Revenues that would otherwise be available to pay the principal of, and interest on, the Bonds. Likewise, broadened property tax exemptions could have a similar effect. See "BONDOWNERS' RISKS" herein.

Application of Tax Revenues

As provided in the Redevelopment Plan, pursuant to Article 6 of the Redevelopment Law and Section 16 of Article XVI of the Constitution of the State, taxes levied upon taxable property in the Project Area each year by or for the benefit of the State, any city, county, city and county, district, or other public corporation (herein sometimes collectively called "taxing agencies") after the effective date of the Ordinance approving the Redevelopment Plan, being Ordinance No. 132 of the City, adopted on November 17, 1986

(effective on December 17, 1986 for the Redevelopment Plan), as amended, shall be divided as follows:

(a) That portion of the taxes which would be produced by the rate upon which the tax is levied each year by or for each of the taxing agencies upon the total sum of the assessed value of the taxable property in the Project Area as shown upon the assessment roll used in connection with the taxation of such property by such taxing agency last equalized prior to August 15, 1991 (being the effective date of Ordinance No. 132, referred to above), shall be allocated to and when collected shall be paid into the funds of the respective taxing agencies as taxes by or for the taxing agencies on all other property are paid; and

(b) That portion of the taxes in excess of the amount identified in (a) above, except the amount of taxes which are attributable to a tax rate levied by a taxing agency for the purpose of producing revenues in an amount sufficient to make annual repayments of the principal of, and the interest on, any bonded indebtedness approved by the voters of the taxing agency on or after January 1, 1989, for the acquisition or improvement of real property, which portion shall be allocated to, and when collected shall be paid into, the fund of that taxing agency; including that portion of such taxes otherwise required by Section 33334.2 of the Law to be deposited in the Low and Moderate Income Housing Fund, but only to the extent necessary to repay that portion of the Bonds and any Parity Bonds (to the extent that portion of Tax Revenues are pledged thereto) which were issued or which shall be issued to finance amounts deposited in the Low and Moderate Income Housing Fund for use pursuant to Section 33334.2 of the Law; but excluding all other amounts of such taxes (if any) (i) required to be deposited into the Housing Fund of the Agency pursuant to Section 33334.2 of the Law and (ii) payable or required to be set aside by the Agency under the Pass-Through Agreements, shall be allocated and paid to the Agency and are herein referred to as "Tax Revenues."

The Tax Revenues received on or after the date of issue of the Bonds shall be deposited in the Special Fund of the Agency and are hereby irrevocably pledged on a parity with the 1998 Bonds to the payment of the principal of, premium, if any, and interest on the Bonds and any Parity Debt, and until all of the 1998 Bonds, the Bonds and any Parity Debt and all interest thereon, have been paid (or until moneys for that purpose have been irrevocably set aside), the Tax Revenues shall be applied solely to the payment of the 1998 Bonds, the Bonds and any Parity Debt plus premium, if any, and the interest thereon as provided in the Indenture. This allocation and pledge is for the exclusive benefit of the Owners of the 1998 Bonds, the Bonds and any Parity Debt and shall be irrevocable.

Section 33645 of the Health and Safety Code provides, in applicable part as follows: "The resolution, trust indenture, or mortgage shall provide that tax increment funds allocated to an agency pursuant to section 33670 shall not be payable to a trustee on account of any issued bonds when sufficient funds have been placed with the Trustee to redeem all Outstanding Bonds of the issue." The Indenture is intended to comply with the above-quoted provision and shall be so construed.

Special Fund

The Special Fund shall be held by the Agency in trust. Until such time as the amount on deposit in the Special Fund, including interest earnings thereon, together with available funds in the LMI Tax Revenue Bond Payment Account equals the aggregate amounts required to be transferred to the Trustee for such Bond Year, the Agency shall deposit all Tax Revenues, other than LMI Tax Revenue, received in any Bond Year into the Special Fund promptly upon receipt.

Until such time as the amount on deposit in the LMI Tax Revenue Bond Payment Account, including interest earnings thereon, together with available funds in the Special Fund equals the aggregate amounts required to be transferred to the for such Bond Year, the Agency shall deposit all LMI Tax Revenues received in any Bond Year into the LMI Tax Revenue Bond Payment Account promptly upon receipt. Notwithstanding the immediately preceding sentence, (1) the amount deposited into the LMI Tax Revenue Bond Payment Account each Bond Year shall not exceed (i) the corresponding debt service requirement for the Bond Year with respect to the LMI Tax Revenue Portion of the Bonds and (ii) any redemption permitted by the Indenture, and (2) from and after the date on which LMI Tax Revenue has been expended in an amount sufficient, on a present value basis based on the schedule of payments shown in the Indenture as adjusted for any prepayments, to have fully paid the principal of and accrued interest on the LMI Tax Revenue Portion of the Bonds, no further LMI Tax Revenue shall be deposited into the LMI Tax Revenue Bond Payment Account. LMI Tax Revenue received by the Agency and not deposited into the LMI Tax Revenue Bond Payment Account shall be deposited into the Agency's Low and Moderate Income Housing Fund.

On or before the Business Day immediately preceding any Interest Payment Date (or, in the event that a Surety Instrument (as defined below) has been substituted for amounts required to be on deposit in the Reserve Account, on or before the third Business Day immediately preceding any Interest Payment Date), the Agency shall withdraw from the LMI Tax Revenue Bond Payment Account and the Special Fund and deposit with the Trustee the amount of money necessary to make the deposits required to pay scheduled principal and interest.

Upon notice from the Trustee, the Agency shall withdraw from the LMI Tax Revenue Bond Payment Account and the Special Fund and deposit with the Trustee the amount of money necessary to make any deposit required by the Indenture.

All Tax Revenues received by the Agency at any time during any Bond Year in excess of the amount required to be deposited into the LMI Tax Revenue Bond Payment Account and the Special Fund, respectively, during such Bond Year shall be released from the pledge and lien hereunder for the security of the Bonds and the Agency may apply such excess Tax Revenues for any lawful purpose of the Agency. Prior to the payment in full of the principal of, premium (if any) and interest on the Bonds and the payment in full of all other amounts payable hereunder and under any Parity Debt Instrument, the Agency shall not have any beneficial right or interest in the moneys on deposit in the Special Fund, except as may be provided in the Indenture and in any Parity Debt Instrument.

Transfer of Amounts to the Trustee; Allocation of Revenues

The Debt Service Fund shall be held by the Trustee in trust. The Trustee shall deposit moneys transferred by the Agency to the Trustee from the LMI Tax Revenue Bond Payment Account and the Special Fund into the following accounts in the amounts and order of priority as follows:

Interest Account. Deposits shall be made into the Interest Account so that the balance in the Interest Account at least five (5) days prior to each Interest Payment Date shall be equal to interest due and payable on the then outstanding Bonds on such Interest Payment Date. Moneys in the Interest Account shall be used solely for the payment of interest on the Bonds as interest becomes due, including accrued interest on any Bonds purchased or redeemed prior to maturity.

Principal Account. After the deposits have been made pursuant to subparagraph (a) above, deposits shall next be made into the Principal Account so that the balance in the Principal Account at least five (5) days prior to each August 1 is equal to the principal coming due on such date on the then outstanding serial Bonds or the amount of the minimum sinking account payments due on the term Bonds on such date. All monies in the Principal Account shall be used and withdrawn by the Trustee solely for the purpose of paying principal and minimum sinking account payments on the Bonds as they shall become due and payable.

Reserve Account. After deposits have been made as described above, deposits shall be made to the Reserve Account, if necessary, in order to cause the amount on deposit therein to equal the Reserve Requirement. Moneys in the Reserve Account shall be transferred to the Interest Account or the Principal Account to pay interest on and principal of the Bonds either (i) as it becomes due to the extent moneys on deposit are insufficient therefor or (ii) at the final maturity of the Bonds. Any portion of the Reserve Account which is in excess of the Reserve Requirement shall be transferred at least semiannually to the Interest Account. Amounts on deposit in the Escrowed Bond Proceeds Fund shall not be included in calculating the Reserve Requirement, until such time as monies are released from the Escrowed Bond Proceeds Fund to the Redevelopment Fund and the Housing Fund as described in the Indenture. The Trustee shall transfer from the Escrowed Bond Proceeds Fund to the Reserve Account the amount set forth in the Written Certificate of the Agency required pursuant to such release.

Surplus Account. It is the intent of the Indenture: (i) that the deposits to the Interest Account and the Principal Account, respectively, shall be made as scheduled, and (ii) that the deposits in to the Reserve Account shall be made as necessary to maintain a balance equal to the Reserve Requirement, if and only if the Tax Revenues are sufficient therefor. Should it be necessary to defer all or part of any deposits to the Reserve Account, such deferred deposits shall be cumulative and shall be made when the Tax Revenues are sufficient to the deposits to the Interest Account and the Principal Account and thereafter make the to the Reserve Account.

If: (i) the above transfers have been made so that the required amounts as of that time are in the above mentioned Accounts and the required transfer has been made to the Excess Investment Earnings Fund as set forth below, (ii) the Tax Revenues to be received by the Agency in the current Fiscal Year, based upon the most recent assessed valuation of taxable property in Redevelopment Project Area, furnished by the appropriate officer of the County are at least equal to 125% of the Maximum Annual Debt Service on all Bonds and Parity Debt and any loans, advances or indebtedness payable from Tax Revenues on a parity with the Bonds pursuant to section 33670 of the Redevelopment Law, as shown by the certificate or opinion of an Independent Financial Consultant employed by the Agency, said opinion or certificate having been filed with the Trustee, and (iii) there has been no material change in the status of the Redevelopment Project which in the opinion of an Independent Redevelopment Consultant, said opinion having been filed with the Trustee, would be likely to result in diminution of increment in the succeeding Fiscal Year, upon direction of the Agency, any balances in the Special Fund shall be deposited in the Surplus Account and may be used and applied by the Agency for any lawful purpose, including without limitation, the purchase and/or call and redemption of Bonds and Parity Debt.

Reserve Account

Pursuant to the Indenture, the Reserve Account has been established and is held by the Trustee in trust for the benefit of the registered owners of the Bonds. The amount on deposit in the Reserve Account is required to be maintained at an amount equal to the

Reserve Requirement. The term "Reserve Requirement" means, as of the date of computation of the Bonds, an amount equal to the least of (i) Maximum Annual Debt Service, (ii) 10% of the net Bond proceeds, or (iii) 125% of average Annual Debt Service on all Bonds. The computation shall be made with respect to all Bonds and Parity Debt Outstanding at the time of such computation. The Reserve Requirement as of the Closing Date is \$323,661.48. Amounts on deposit in the Escrowed Bond Proceeds Fund shall not be included in calculating the Reserve Requirement, until such time as monies are released from the Escrowed Bond Proceeds Fund to the Redevelopment Fund and the Housing Fund as described in the Indenture. The Trustee shall transfer from the Escrowed Bond Proceeds Fund to the Reserve Account the amount set forth in the Written Certificate of the Agency required pursuant to such release.

The Indenture provides that the Agency may at any time substitute an Alternate Reserve Account Security (herein "Security"), with the consent of the Bond Insurer, and upon such substitution, the Agency shall be entitled to receive all moneys then held in the Reserve Account and the Agency shall deposit such moneys in the Redevelopment Fund for application to the costs of the Redevelopment Project. In the event the Agency delivers an Alternate Reserve Account Security, the Trustee shall hold and apply such instrument pursuant to the Indenture so as to have moneys available thereunder for the purposes and at the times required under the Indenture. The Trustee shall deliver to the provider of the Security a demand for payment under the Alternate Reserve Account Security not less than three days prior to the date upon which moneys are required hereunder. The Trustee shall apply all cash amounts in the Reserve Account to the purposes herein provided prior to making any demand for payment upon the provider of the Security. The Trustee shall maintain adequate records, verified with the provider of the Security, as to the amount available to be drawn at any given time under the Alternate Reserve Account Security and as to the amounts paid and owing to the provider of the Security.

Escrowed Proceeds Fund

The moneys set aside in the Escrowed Proceeds Fund will be applied as follows:

(a) On any date prior to June 15, 2006, the Agency may deliver to the Trustee a Written Certificate of the Agency accompanied by a certificate or opinion of an Independent Financial Consultant which identifies (i) the amount of Tax Revenues received or estimated to be received by the Agency in the then current Fiscal Year and each succeeding Fiscal Year until maturity of the Bonds, based upon the most recent assessed valuation of taxable property in the Project Area, furnished by the appropriate officer of the County of San Diego, taking into account the scheduled increases and/or decreases in payments due and owing by the Agency under pass-Through Agreements previously entered into by the Agency, assuming no growth in Tax Revenues (ii) the amount proposed to be released from the Escrowed Bond Proceeds Fund for deposit in the Redevelopment Fund and the Housing Fund, (iii) the annual debt service resulting from such release to maturity, and (iv) the amount to be transferred to the Reserve Account from the Escrowed Bond Proceeds Fund. Such Written Certificate of the Agency and certificate or opinion shall certify that (A) Tax Revenues to be received by the Agency will be at least equal to 125% of the annual debt service to maturity of the 1998 Bonds and the Bonds, excluding that proportionate share of the Escrowed Bonds that will remain secured by the Escrowed Bond Proceeds Fund immediately following such transfer, and any Parity Bonds and (B) the amount to remain on deposit in the Escrowed Bond Proceeds Fund, following the proposed transfer will be sufficient to pay principal and interest due on the principal amount of Escrowed Bonds after the proposed transfer to and including August 1, 2006. Following receipt of such Written Certificate of the Agency and certificate or opinion, on which the Trustee may conclusively rely, the Trustee may withdraw from the Escrowed

Bond Proceeds Fund the amount identified in such Written Certificate of the Agency and certificate or opinion and transfer such amount to the Agency and Trustee, respectively for deposit to the Redevelopment Fund, Housing Fund and the Reserve Account.

(b) At least five (5) days prior to each Interest Payment Date on and prior to August 1, 2006, the Trustee shall transfer, from the Capitalized Interest Account of the Escrowed Bond Proceeds Fund to the Interest Account, an amount equal to the interest then due on the Escrowed Bonds.

(c) Any moneys remaining in the Escrowed Bond Proceeds Fund, on June 15, 2006 shall be transferred by the Trustee to the Redemption Fund and applied to the redemption of Escrowed Bonds on August 1, 2006.

Issuance of Parity Debt

The Agency may at any time issue Parity Debt payable from the Tax Revenues and secured by a lien and charge upon the Tax Revenues equal to the lien and charge securing the Outstanding Bonds and any other Parity Debt theretofore issued under any Parity Debt Instrument, but only subject to the following specific conditions, which are hereby made conditions precedent to the issuance of any such Parity Debt:

(a) The Agency shall be in compliance with all covenants set forth in the Indenture, any Supplemental Indenture and any Parity Debt Instrument and no Event of Default shall have occurred and be continuing and a Written certificate of the Agency to that effect shall have been filed with the Trustee; provided, however, that Parity Debt may be issued notwithstanding that the Agency is not in compliance with all such covenants so long as immediately following the issuance of such Parity Debt the Agency will be in compliance with all such covenants.

(b) The issuance of such Parity Debt shall have been duly authorized pursuant to the Redevelopment Law and all other applicable laws, and the issuance of such Parity Debt shall have been provided for by a Parity Debt Instrument which shall specify the following: (1) the authorized principal amount of such Parity Debt; (2) the date and the maturity date or dates of such Parity Debt; provided that (i) each maturity date shall fall on an August 1 and interest shall be payable on Interest Payment Dates, (ii) all such Parity Debt of like maturity shall be identical in all respects, except as a number, and (iii) fixed serial maturities or mandatory sinking fund payments, or any combination thereof, shall be established to provide for the retirement of all such Parity Debt on or before their respective maturity dates; (3) the description of the Parity Debt, the place of payments thereof and the procedure for execution and authentication; (4) the redemption premiums, if any, and the redemption terms, if any, for such Parity Debt; (5) the amount to be deposited on the date of delivery of the Parity Debt from the Agency to the original purchaser thereof from the proceeds of such Parity Debt in the Reserve Account to increase the amount therein to the Reserve Requirement; (6) that the Parity Debt shall be subject to the provisions of Articles V and VII of the Indenture; (7) that the trustee with respect to the Parity Debt shall be the Trustee with respect to the Bonds; (8) the form of such Parity Debt; and (9) such other provisions as are necessary or appropriate and not inconsistent with the Indenture.

(c) A certificate of an independent certified public accountant certifying that the sum of Tax Revenues received or to be received by the Agency from the most recent assessed valuation of taxable property in the Redevelopment Project based upon the most recently established tax rates will, plus, to the extent permitted below, Additional Revenues, for each Fiscal Year following the issuance of such Parity Debt, be at least equal

to 125% of the Maximum Annual Debt Service on all Bonds and Parity Debt which will be Outstanding following the issuance of such Parity Debt, but, with the prior written consent of the Bond Insurer, not including debt service on any portion of the Escrowed Bonds or the proceeds of Parity Bonds deposited in an escrow fund. Such certification shall take into account scheduled increases and/or decreases in payments due and owing by the Agency under pass through agreements previously entered into by the Agency pursuant to section 33401 of the California Health and Safety Code.

“Additional Revenues” means, as of the date of calculation, the amount of Tax Revenues which, as shown in the report of a Redevelopment Consultant, are estimated to be receivable by the Agency within the Fiscal Year following the Fiscal Year in which such calculation is made as a result of an increase in the assessed valuation of taxable property in the Project Area due to (a) the application of a growth factor equal to the lesser of 2.00% or the Consumer Price Index adjustment applicable in the then current Fiscal Year and (b) completion of construction which is not yet reflected on the tax rolls, or due to transfers of ownership or any other interest in real property which has been recorded but which is not yet reflected in the tax roll.

For purposes of calculating Tax Revenues in connection with the issuance of Parity Bonds, Additional Revenues may be taken into account to the extent that the 1998 Bonds are no longer Outstanding or to the extent permitted by the 1998 Bonds Indenture.

(d) The Trustee shall have received the following documents, all of such documents dated or certified, as the case may be, as of the date of delivery of such Parity Debt by the Trustee: (i) a certified copy of the Parity Debt Instrument authorizing the issuance of such Parity Debt; (2) a Written Request of the Agency as to the authentication and delivery of such Parity Debt; (3) an opinion of Bond Counsel to the effect that (a) the Agency has the right and power under the Redevelopment Law to execute and deliver the Indenture and the Parity Debt Instrument relating to such Parity Debt, the Indenture and all Parity Debt Instruments have been duly executed and delivered by the Agency, are in full force and effect and are valid and binding upon the Agency and enforceable in accordance with their terms (except as enforcement may be limited by bankruptcy, insolvency, reorganization and other similar laws relating to the enforcement of creditors' rights); (b) such Parity Debt is a valid and binding limited obligation of the Agency, enforceable in accordance with its terms (except as enforcement may be limited by bankruptcy, insolvency, reorganization and other similar laws relating to the enforcement of creditors' rights); (c) such Parity Debt has been duly and validly executed and delivered in accordance with the Redevelopment Law, the Redevelopment Plan, the Indenture and the applicable Parity Debt will not adversely affect the exclusion from gross income for federal income tax purposes of interest on any Outstanding Bonds or Parity Debt theretofore issued or the exemption from State personal income taxation of interest on any Outstanding Bonds or Parity Debt theretofore issued; (4) a Written Certificate of the Agency containing such statements as may be reasonably necessary to show compliance with the requirements of the Indenture; (5) such further documents, money and securities as are required by the provisions of the Indenture and the Parity Debt Instrument providing for the issuance of such Parity Debt

(e) Refunding Bonds which do not defease all of the insured Bonds may be issued without the consent of the Bond Insurer provided there is no increase in maximum annual debt service. Variable rate indebtedness (indebtedness which does not bear a fixed rate of interest to maturity) and balloon indebtedness (indebtedness of which 25% or more of the principal amount comes or may come due in any one fiscal year by maturity, mandatory sinking fund redemption or optional or mandatory tender by the holder thereof) of the Agency shall be subject to the prior approval of the Bond Insurer.

(f) The indebtedness evidenced by the subordinated debt and any renewals or extensions thereof (herein called "Subordinated Indebtedness"), shall at all times be wholly subordinate and junior in right of payment to any and all indebtedness of the Agency under the Indenture or the Bonds (herein called "Superior Indebtedness"). Following an Event of Default under the Indenture, no Subordinate Indebtedness shall be paid prior to any Superior Indebtedness in any fiscal year of the Agency.

If the holder of the Subordinated Indebtedness is a commercial bank, savings bank, savings and loan association or other financial institution which is authorized by law to accept and hold deposits of money or issue certificates of deposit, such holder must agree to waive any common law or statutory right of setoff with respect to any deposits of the Agency maintained with or held by such holder.

FINANCIAL GUARANTY INSURANCE

The full text of a specimen Financial Guaranty Insurance Policy is set forth in APPENDIX G—"SPECIMEN FINANCIAL GUARANTY INSURANCE POLICY."

Description of Financial Guaranty Insurance Policy

The Financial Guaranty Insurance Policy will be issued by the Bond Insurer simultaneously with the issuance and delivery of the Bonds. The Financial Guaranty Insurance Policy is non-cancelable during its term and provides for the prompt payment of principal of and interest on the Bonds to the extent that the Trustee has not received sufficient funds from the Authority for payment of the Bonds on the "due date." The Bond Insurer is obligated to make the required payment on the later of the due date or the first business day after which the Bond Insurer has received notice from The Bank of New York, as Insurance Trustee (the "Insurance Trustee"), that the Authority has failed to pay amounts due on the Bonds. Under the Financial Guaranty Insurance Policy, the "due date" of the Bonds, when referring to the payment of principal, means the stated maturity date thereof or the date on which payment of principal is due by reason of mandatory sinking fund payments and does not mean any earlier date on which payment is due by reason of any call for redemption, acceleration, or other advancement of maturity, other than in the discretion of the Insurer. With respect to interest on the Bonds, the "due date" means the stated date for payment of interest. The Financial Guaranty Insurance Policy guarantees reimbursement of any recovery of any such payment from an Owner or the Trustee pursuant to a final judgment by any court of competent jurisdiction holding that such payment constituted a voidable preference within the meaning of any applicable bankruptcy law.

Upon the occurrence and continuance of an Event of Default, the Bond Insurer, may, in its discretion, direct the acceleration of the Bonds at a price equal to the principal amount thereof plus accrued interest, or the Bond Insurer may elect to continue to pay principal and interest on the originally scheduled due dates of the Bonds. For specific information on the coverage provided, reference should be made to the Financial Guaranty Insurance Policy that has been reproduced in specimen form in Appendix G hereto. The Financial Guaranty Insurance Policy does not insure against nonpayment of principal or interest on the Bonds due to the insolvency, misconduct or negligence of the Trustee. The Financial Guaranty Insurance Policy does not insure the payment of any redemption premium.

Radian Asset Assurance Inc.

The Bond Insurer is a financial guaranty insurance company, regulated by the Insurance Department of the State of New York and licensed to do business in all 50 states and the District of Columbia. The Bond Insurer was formerly known as "Asset Guaranty Insurance Company". The Bond Insurer changed its corporate name to Radian Asset Assurance Inc. The Bond Insurer has received approval to use its new corporate name in all jurisdictions where it is licensed to do business. As of March 31, 2004, the Bond Insurer had total shareholders' equity of approximately \$581,007,000 (unaudited) and total assets of approximately \$1,144,167,000 (unaudited). The financial information relating to the Bond Insurer presented in this Official Statement was prepared internally by the Bond Insurer, based on generally accepted accounting principles, and has not been audited by independent certified public accountants. The address of the Bond Insurer's administrative office is 335 Madison Avenue, New York, New York 10017, and its telephone number is 212-983-5859.

The Bond Insurer has filed the following information with entities designated as Nationally Recognized Municipal Securities Information Repositories ("NRMSIRs") pursuant to Rule 15c2-12 of the Securities Exchange Act of 1934:

(i) the Bond Insurer's consolidated financial statements as of December 31, 2003 and 2002 and for each of the three years in the period ended December 31, 2003 prepared in accordance with generally accepted accounting principles with the accompanying report of the Bond Insurer's independent auditors, which expresses an unqualified opinion and includes an explanatory paragraph referring to a significant insurance loss recognized subsequent to the balance sheet date; and

(ii) the Bond Insurer's quarterly unaudited consolidated balance sheet as of March 31, 2004 and unaudited consolidated statement of operations for the three month period then ended, prepared in accordance with generally accepted accounting principles.

The Bond Insurer has an insurance financial strength rating of "AA" from Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc. ("S&P"), "Aa3" from Moody's Investors Service, Inc. ("Moody's") and "AA" by Fitch Ratings Services ("Fitch"). Such ratings reflect only the views of S&P, Moody's and Fitch, respectively, do not constitute a recommendation to buy, sell or hold securities and are subject to revision or withdrawal at any time by such rating agencies.

The Bond Insurer is a wholly-owned indirect subsidiary of Radian Group Inc. ("Radian"), a publicly-owned corporation with its shares listed on the New York Stock Exchange (symbol "RDN"). Radian is a leading credit enhancement provider to the global financial and capital markets, headquartered in Philadelphia. Radian's subsidiaries provide products and services through three business lines: financial guaranty, mortgage insurance and mortgage services. None of Radian, Radian's other subsidiaries or any of Radian's investors is obligated to pay the debts of or claims against the Bond Insurer. A complete copy of the December 31, 2003 audited consolidated financial statements, which expresses an unqualified opinion and includes an explanatory paragraph referring to a significant insurance loss recognized subsequent to the balance sheet date and additional information of Radian, together with the accompanying report of independent auditors, is available from the Bond Insurer upon written request.

Additional information regarding the Bond Insurer can be found in the following documents filed by Radian with the Securities and Exchange Commission: (a) in the Annual

Report on Form 10-K of Radian for the year ended December 31, 2003 and the Quarterly Report on Form 10-Q for the period ended March 31, 2004 under the headings (i) "Safe Harbor Statement under the Private Securities Limitation Reform Act of 1995" (but insofar as it relates to the financial guaranty insurance businesses); (ii) 10-K only, Item 1. Business: "Financial Guaranty Business" "Risk Management – Financial Guaranty Business" "Ratings" (but only insofar as it relates to the Bond Insurer or Radian Reinsurance Inc.), "Defaults and Claims" (but only insofar as it relates to the financial guaranty business) and "Regulation – Direct Regulation" (but only insofar as it relates to the financial guaranty business); (iii) 10-K only, "Item 6 – Selected Financial Data –" "Selected Ratios – Financial Guaranty" and "Other Data – Financial Guaranty," and (iv) Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations "Financial Guaranty – Results of Operations, and "Liquidity and Capital Resources" (but only to the extent it relates to Radian Asset Assurance or Radian Reinsurance), and "Critical Accounting Policies;" and (b) the Reports on Form 8-K dated January 15, 2004, February 11, 2004, April 8, 2004 and June 1, 2004.

On January 14, 2004, Radian announced that the Bond Insurer will add \$96.0 million to its loss reserves in anticipation of \$111.0 million in claims from a single manufactured housing transaction in which the Bond Insurer reinsured from an affiliate. The Bond Insurer held a \$15.0 million loss reserve for this transaction as of September 30, 2003 and the increased reserve totaling \$111.0 million, represents the Bond Insurer's par exposure on the transaction. The Bond Insurer expects losses to be paid out over the next several years. After Radian's announcement, S&P and Fitch affirmed their respective current "AA" insurance financial strength ratings of the Bond Insurer, but S&P revised its outlook on the Bond Insurer and Radian from "stable" to "negative." On May 25, 2004, Moody's assigned a financial strength rating of "Aa3" to the Bond Insurer with an outlook of "stable". In January 2004, Radian contributed \$65.0 million in capital to the Bond Insurer through an intermediary holding company from funds currently held at Radian to offset (on an after-tax basis) the effect of this loss on the Bond Insurer.

In April 2004, the Board of Directors of the Bond Insurer and its financial guaranty affiliate Radian Reinsurance Inc. approved the merger of the financial guaranty reinsurance business of Radian Reinsurance Inc. into the Bond Insurer (the "Merger"). The Merger was approved by each company's sole shareholder and the Merger was consummated on June 1, 2004. As a result of the Merger, the financial guaranty reinsurance business currently conducted by Radian Reinsurance Inc. and the direct financial guaranty business conducted by the Bond Insurer will be conducted by the Bond Insurer, and the Bond Insurer has greater assets, liabilities and shareholder's equity than it currently has on a stand-alone basis.

The Bond Insurer has filed with the NRMSIRs a table presenting selected unaudited balance sheet and income sheet data of the Bond Insurer as of December 31, 2001 (with respect to non-balance sheet information only), 2002 and 2003 and March 31, 2004 on a proforma combined basis as if Radian Reinsurance were merged with the Bond Insurer as of the dates indicated, in accordance with accounting principles generally accepted in the United States of America. Though unaudited, the information so filed was derived from the respective audited financial statements of the Bond Insurer and Radian Reinsurance Inc. as of December 31, 2003 and 2002, and for each for the three years in the period ended December 31, 2003, together with the respective accompanying reports of the Bond Insurer's independent auditors. For informational purposes, the Bond Insurer has also filed the Radian Reinsurance Inc. audited financial statements with the NRMSIRs referred to above, as well as Radian Reinsurance Inc.'s quarterly unaudited consolidated balance sheet as of March 31, 2004 and unaudited consolidated statement of Income for the three month period then ended, prepared in accordance with generally accepted accounting principles.

Effective January 31, 2004, one primary insurer of Radian Reinsurance exercised its right to recapture the financial guaranty reinsurance business assumed by Radian Reinsurance. In connection with the recapture, Radian Reinsurance returned approximately \$16.4 billion of par in force and approximately \$96.4 million of statutory unearned premium with a carrying value of approximately \$71.5 determined in accordance with accounting principles generally accepted in the United State of America (can defined as US GAAP). In addition, Radian Reinsurance was reimbursed for policy acquisition costs of approximately \$31.0 million with a carrying value of approximately \$21.3 determined in accordance with accounting principles generally accepted in the United State of America. Radian Reinsurance has also reimbursed the primary insurer approximately \$7.5 million for case reserves, net of \$4.0 million salvage. The impact of the recapture resulted in a reduction of pre-tax income of \$15.9 million determined in accordance with accounting principles generally accepted in the United States of America. Such recapture also resulted in negative net premiums written for the quarter ended March 31, 2004.

Neither the Bond Insurer nor any of its affiliates makes any representation regarding the Bonds or the advisability of purchasing the Bonds and makes no representation regarding this Official Statement other than as to the information supplied by the Bond Insurer and presented under the heading "FINANCIAL GUARANTY INSURANCE" and as set forth in APPENDIX G—"SPECIMEN FINANCIAL GUARANTY INSURANCE POLICY." The Bond Insurer's role is limited to providing the coverage set forth in the Financial Guaranty Insurance Policy. In accordance with applicable law, in the event the Bond Insurer becomes insolvent, any claims arising under the Financial Guaranty Insurance Policy are excluded from coverage by the California Insurance Guaranty Association, established pursuant to Article 15.2 (commencing with Section 1063) of Chapter 1 of Part 2 of Division 1 of the California Insurance Code.

THE AUTHORITY

The Lemon Grove Financing Authority (the "Authority") was created by a Joint Exercise of Powers Agreement, dated May 1, 1992, by and between the City and the Agency. Such agreement was entered into pursuant to the provisions of Articles 1, 2 and 4 of Chapter 5 of Division 7 of Title 1 of the California Government Code. The Authority was created for the purpose of assisting the financing or refinancing of certain public capital facilities within the City. The Authority has the power to purchase bonds issued by any local agency at public or negotiated sale and may sell such bonds to public or private purchasers at public or negotiated sale. The Authority is governed by a five-member board which consists of the members of the City Council of the City. The Mayor acts as the Chair of the Authority, the City Manager as its Executive Director, the City Clerk as its Secretary and the City Treasurer as its Treasurer.

THE CITY

The City is located directly east of the City of San Diego adjacent to state Route 94. The City was first organized as a community and incorporated as a general law city in July 1977. The City's population was first estimated by the California Department of Finance in January 1978 and indicated that 19,700 persons resided in the community. In January 2004, the City's population was 25,592. See APPENDIX B—"GENERAL INFORMATION REGARDING THE CITY."

THE AGENCY

Agency Members

The Agency was activated pursuant to the Redevelopment Law in May, 1986. The Agency is governed by a five-member board which consists of all members of the City Council of the City. The Mayor of the City serves as Chairman of the Agency. The Mayor is elected directly and the four members of the City Council are elected at large. City Council/Agency Board members, their occupations and term expiration dates, are as follows:

<u>MEMBER</u>	<u>OCCUPATION</u>	<u>TERM EXPIRES</u>
Mary Teresa Sessom, <i>Chair/Mayor</i>	Educator	June 2008
Jerry Jones, <i>Vice Chair/Mayor Pro Tem</i>	Businessman	June 2006
Tom Clabby, <i>Board Member/Council</i>	Retired/Aircraft Mfg.	June 2008
Mary England, <i>Board Member/Council Member</i>	Public Relations/Event Planner	June 2008
Jill Greer, <i>Board Member/Council Member</i>	Graphic Arts	June 2006

Agency Administration

The Agency has an arrangement with the City for financial assistance and services, facilities and personnel support. As moneys become available, the Agency reimburses the City for all such services performed in amounts equal to a portion of the gross salary and employee fringe benefits for certain City employees utilized by the Agency plus other miscellaneous operating and equipment costs and capital expenditures. All such payments are subordinate to the payment of debt service on the Bonds.

Agency Powers

All powers of the Agency are vested in its members. Pursuant to the Redevelopment Law, the Agency is a separate public body and exercises governmental functions, including planning and implementing redevelopment projects.

The Agency may exercise the right to issue bonds for authorized purposes and to expend their proceeds, and the right to acquire, sell, rehabilitate, develop, administer or lease property. The Agency may demolish buildings, clear land and cause to be constructed certain improvements, including streets, sidewalks, and utilities, and can further prepare for use as a building site any real property which it owns or administers.

The Agency may, from any funds made available to it for such purposes, pay for all or part of the value of land and the cost of buildings, facilities or other improvements to be publicly owned and operated, provided that such improvements are of benefit to a redevelopment project and cannot be financed by any other reasonable method. The Agency may not construct or develop buildings, with the exception of public buildings and housing, and must sell or lease cleared property which it acquires within a redevelopment project for redevelopment in conformity with a particular redevelopment plan, and may further specify a period within which such redevelopment must begin and be completed.

Outstanding Indebtedness of the Agency

Certification of Agency Indebtedness. Pursuant to section 33675 of the Redevelopment Law, on or before October 1 of each year the Agency must file with the County Auditor a

statement of indebtedness certified by the chief fiscal officer of the Agency for each redevelopment project that receives tax increment. The statement of indebtedness is required to contain the date on which any bonds were delivered, the principal amount, term, purpose and interest rate of bonds and the outstanding balance and amount due on bonds. Similar information must be given for each loan, advance or indebtedness that the Agency has incurred or entered into to be payable from tax increment. The Agency has complied with the requirements of section 33675 each year since adoption of the Redevelopment Plan.

Section 33675 also provides that the County Auditor is limited in payment of tax increment to the Agency to the amounts shown on the Agency's statement of indebtedness. The section further provides that the statement of indebtedness is prima facie evidence of the indebtedness of the Agency but that the County Auditor may dispute the amount of indebtedness shown on the statement in certain cases. Provision is made for time limits under which the dispute can be made by the County Auditor as well as provisions for determination by the Superior Court in a declaratory relief action of the proper disposition of the matter. The issue in any such action must involve only the amount of the indebtedness and not the validity of any contract or debt instrument, or any expenditures pursuant thereto. An exception is made for payments to a public agency in connection with payments by such public agency pursuant to a bond issue which shall not be disputed in any action under section 33675.

Bonded Indebtedness. Other than the 1998 Bonds and the Bonds, the Agency has incurred no bonded indebtedness.

The following table sets forth the combined scheduled annual debt service for the 1998 Bonds and the Bonds.

Bond Year Ending (August 1)	1998 Bonds Debt Service	Non-Escrowed Bonds Debt Service	Escrowed Bonds Debt Service	Total Debt Service
2005	\$692,248	\$348,288	\$ 94,384	\$1,134,919
2006	692,998	348,873	96,804	1,138,674
2007	693,248	344,373	156,804	1,194,424
2008	692,793	209,873	135,454	1,038,119
2009	691,613	209,323	134,354	1,035,289
2010	693,675	208,703	133,114	1,035,491
2011	694,875	213,028	131,764	1,039,666
2012	690,213	212,121	135,314	1,037,648
2013	694,975	206,171	138,604	1,039,750
2014	693,588	210,371	136,604	1,040,563
2015	691,338	209,340	134,541	1,035,219
2016	693,225	208,265	137,391	1,038,881
2017	693,963	207,165	134,971	1,036,099
2018	693,550	211,040	132,496	1,037,086
2019	691,988	209,660	134,966	1,036,614
2020	694,275	213,250	137,146	1,044,671
2021	695,125	211,500	138,896	1,045,521
2022	694,538	209,750	135,396	1,039,684
2023	692,513	213,000	136,896	1,042,409
2024	694,050	206,000	133,146	1,033,196
2025	693,863	209,250	134,396	1,037,509
2026	691,950	212,250	135,296	1,039,496
2027	693,313	205,000	135,940	1,034,253
2028	692,663	208,000	136,328	1,036,990
2029	—	900,750	131,459	1,032,209
2030	—	903,750	136,590	1,040,340
2031	—	904,750	135,920	1,040,670
2032	—	443,750	134,980	578,730
2033	—	253,750	138,770	392,520
2034	—	257,250	137,020	394,270

Source: The Agency.

Agency Financial Statements

The Law requires redevelopment agencies to have an independent financial audit conducted each year. The financial audit is also required to include an opinion of the Agency's compliance with laws, regulations and administrative requirements governing activities of the Agency. Audited financial statements for the Agency for the Fiscal Year that ended June 30, 2003, included in Appendix A attached hereto, have been prepared Brownell & Duffey, Carlsbad California. The firm's audit was made in accordance with generally accepted auditing standards. See APPENDIX A—"AUDITED FINANCIAL STATEMENTS OF THE AGENCY FOR THE FISCAL YEAR ENDED JUNE 30, 2003."

THE PROJECT AREA

The following is a summary description of the Project Area. Included within this description are sections discussing the present and current conditions of the Project Area and the future development within the Project Area. These descriptions have been supplied by the Agency. There can

be no assurance that the future developments discussed below will be completed in the manner or in the time periods set forth.

General

The City Council and the Agency established the Project Area by Ordinance No. 132 enacted by the City Council on November 17, 1986. The Redevelopment Plan seeks to establish a pattern of land use which will best promote the health, safety, convenience and welfare of all citizens of the community. The Redevelopment Plan strives to encourage private investment in industry, commerce and housing by providing needed public facilities and improvements and promoting an environment which reflects concern for architectural and urban design principles.

The Project encompasses 618 acres of land and consists of 25.4% of the total area within the City.

Redevelopment Plan Limitations

Chapter 942, Statutes of 1993, as codified in section 33333.6 of the Redevelopment Law, limits the life of redevelopment plans adopted prior to January 1, 1994, to 40 years from the date of adoption or January 1, 2009, whichever is later. It also limits the period within which a redevelopment project area may receive tax increment to the life of the redevelopment plan plus ten years beyond the termination of redevelopment activities except to accommodate certain specific low and moderate-income housing obligations or to pay debt service on bonds, indebtedness or other financial obligations authorized prior to January 1, 1994. Such redevelopment plans are further required to include a limitation on the number of tax increment dollars that may be allocated to the redevelopment agency; a time limit on the establishing of indebtedness to be repaid with tax increment; and a limit on the amount of bonded indebtedness to be repaid with tax increment that can be outstanding at one time. These limits can be extended only by an amendment of the redevelopment plan.

For redevelopment plans adopted prior to 1994, Chapter 942 stipulates that the time limit for establishing indebtedness shall not exceed 20 years from the adoption of the redevelopment plan or January 1, 2004, whichever is later. Chapter 741, Statutes of 2001, was adopted under SB 211 and amends several sections of the Redevelopment Law that control time limitations for redevelopment project areas. Limitations, that under prior legislation could not be amended or had different amendment procedures, in accordance with this section, may be modified through project area amendments as set forth in this section of the Redevelopment Law. At this time, the Agency is not considering adoption of a Project Area amendment pursuant to this statute.

The Redevelopment Plan for the Project Area provides that the amount of tax increment revenues annually allocable to the Agency is no more than \$10,000,000 which is adjusted annually by the Consumer Price Index. The maximum amount of bonded indebtedness which may be incurred by the Agency is \$100,000,000 adjusted annually by the Consumer Price Index. The Agency may not establish any bonded indebtedness after October 2016 (30 years from the date the plan was adopted). Tax increment revenues will only be allocated and paid to the Agency if the Agency has incurred indebtedness relating to the Project Area.

On December 20, 1994, the City adopted Ordinance No. 228 establishing Redevelopment Plan limits required by Assembly Bill 1290 (Statutes of 1993, Chapter 942) ("AB 1290") for the Project Area as follows:

1. A time limit to issue or incur debt of November 17, 2006, except that such a limit does not apply to the agency’s ability to incur or issue debt for housing purposes payable from housing set-aside funds, or refinancing existing debt issued prior to January 1, 1994 as long as the amount of debt is not increased and the repayment of such debt does not extend beyond the date the original debt would have been repaid.

2. The term of the effectiveness of the Redevelopment Plan of November 17, 2026.

3. The time limit to receive tax increment generated from the Project Area at ten (10) years beyond the termination of the effectiveness of the Redevelopment Plan, which is November 17, 2036, except that the Agency may continue to receive such necessary tax increment to pay indebtedness or other obligations issued or incurred prior to January 1, 1994 and for the financing of required housing and the elimination of deficits created pursuant to section 33334.6 of the Redevelopment Law.

On November 17, 1998, the City adopted Ordinance No. 286, the Agency amended the Redevelopment Plan to extend its eminent domain powers beyond the originally scheduled expiration date.

The plan limitations for the Project Area are summarized below.

**Table 1
Redevelopment Plan Limitations**

Plan Life:	November 17, 2026
Last Date to Establish Debt:	November 17, 2006
Last Date to Repay Debt:	November 17, 2036
Annual Limit Amount of Tax Increment	\$10,000,000*
Bonded Indebtedness Limit	\$100,000,000*

*Adjusted annually by the Consumer Price Index.

The California legislature recently enacted SB 1045, Chapter 260, Statutes of 2003 (“SB 1045”), as an urgency statute, relating to a requirement that all redevelopment agencies allocate specified amounts of tax increment to the County Controller for deposit into the Education Revenue Augmentation Fund (“ERAF”). See “BONDOWNERS’ RISKS—State Budget Deficit—ERAF” herein. In recognition of the loss of revenue to the agencies, SB 1045 authorizes amendments to redevelopment plans to extend by one year the life of the redevelopment plan and the time period in which to collect tax increment revenues. The legislative body of a redevelopment agency can adopt an ordinance without having to follow normal lengthy procedures to amend its redevelopment plans. The Agency has not adopted an ordinance to extend by one year the life of the Redevelopment Plan and the time period in which to collect Tax Revenues but may elect to do so in the future.

Project Area Description

The 618-acre Project Area stretches between the northerly portion of the City’s eastern and western boundaries and, with its southerly extension along most of the length of Lemon Grove Avenue and a small area on Skyline Drive, includes almost all of the City’s land which is zoned for commercial and industrial use. Major roadways within the Project Area are Federal Boulevard, Broadway, Lemon Grove Avenue, Lemon Grove Way and Grove Street.

Goals of the Project Area

The following goals have been established to guide the Agency when implementing the Redevelopment Plan:

- To eliminate and prevent the spread of blight and deterioration, and to conserve, rehabilitate and redevelop the Project in accordance with the Redevelopment Plan.
- To assemble land for productive use.
- To put underutilized land to productive use.
- To encourage private sector investment in the development of the Project. To promote private sector investment in the development of the Project.
- To provide for the development of distinct commercial districts, to attain a consistent image and character and to enhance their economic viability.
- To provide for the expansion, renovation and relocation of businesses within the Project to enhance their economic viability.

Developments Within the Project Area

New construction projects recently completed in the Project Area are set forth below and consist of an estimated addition of \$1,182,916 of assessed valuation for the fiscal year 2004-05 tax roll.

<u>Development</u>	<u>Estimated Fiscal Year 2004-05 Assessed Valuation</u>
Various Commercial Tenant Improvements	\$ 451,047
New 6,500 sq. ft. Commercial Building	370,500
New Gas Station/Mini Mart	186,760
1,159 sq. ft. Residential Addition	114,609
Cellular Communications Improvements	<u>60,000</u>
Total	<u>\$1,182,916</u>

Current and Projected Development

Current development activity in the Project Area includes facade and dining area improvements for El Pollo Grill and the Lemon Grove Deli, and an expansion of Bob Baker Toyota, which will include 63,939 square feet of new service bays and office space on a 5.6 acre lot, adjacent to the existing facility.

The Agency is currently developing a specific plan for the core of the Project Area, to increase commercial densities and encourage affordable and market-rate housing in the form of mixed use projects.

The Agency has been working to create a more pedestrian oriented commercial area to bring activity to the Project Area. The Agency recently invested more than \$350,000 in facade loans and street improvements (sidewalk repair, street trees, outdoor furniture and landscaping) in the downtown area. The Agency has encouraged outdoor dining by working with downtown area restaurants to create and expand outdoor dining areas.

Anticipated future development projects in the Project Area include the expansion of an existing motorcycle sales and service shop, the development of a power center project in the downtown area and the development of a mixed use commercial/residential project in the downtown area.

Assessed Valuation

The Base Year assessed valuation was established in fiscal year 1986-87 in the amount of \$106,440,805. A breakdown of the fiscal year 2003-04 assessed valuation in the Project Area by category of use is as follows:

Table 2
Breakdown of Assessed Valuation by Category of Use

<u>Land Use</u>	<u>Number of Parcels</u>	<u>2003-04 Secured Assessed Valuation</u>	<u>Percent of Secured Assessed Valuation</u>
Commercial	271	\$133,505,859	55.95%
Industrial	89	32,216,305	13.50
Institutional	7	3,421,838	1.43
Recreational	5	251,137	0.11
Res-Multi-Family	156	50,694,566	21.24
Res-Single Family	97	10,322,590	4.33
Unknown	55	0	0.00
Vacant	<u>71</u>	<u>8,218,902</u>	<u>3.44</u>
Total	<u>751</u>	<u>\$238,631,197</u>	<u>100.00%</u>

Source: San Diego County Assessor 2003-04 Secured Tax Rolls

Note: The figures include the value for exempt parcels such as those owned by the City, the Agency, the State or other governmental agencies.

According to the figures provided on the assessor's tax rolls, the 71 vacant, privately owned parcels within the Project Area total 14.24 acres. This vacant land is 2% of all acreage within the Project Area.

The following table shows the actual assessed values for fiscal years 2000 to 2004 based upon the County Auditor/Controller's equalized rolls and incremental values of property within the Project Area based on an exclusion of assessed values from the unsecured roll.

**Table 3
Historical Taxable Values and Tax Increment Revenues
Fiscal Years Ended June 30,**

	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
Assessed Values					
Secured	\$210,065,725	\$219,383,817	\$231,236,503	\$227,088,690	\$238,631,197
Unsecured	<u>22,552,480</u>	<u>26,664,355</u>	<u>23,321,317</u>	<u>28,124,736</u>	<u>29,496,069</u>
Total Assessed Values	\$232,618,205	\$246,048,172	\$254,557,820	\$255,213,426	\$268,127,266
Base Year Values	<u>106,440,805</u>	<u>106,440,805</u>	<u>106,440,805</u>	<u>106,440,805</u>	<u>106,440,805</u>
Incremental Assessed Values	\$126,177,400	\$139,607,367	\$148,117,015	\$148,772,621	\$161,686,461
Gross Tax Revenues	\$1,261,774	\$1,396,074	\$1,481,170	\$1,487,726	\$1,616,865
Less:					
SB 2557 Admin & Service Fee	\$12,075	\$12,792	\$11,989	\$14,238	\$16,169
Pass-Through Agreements	<u>203,911</u>	<u>229,678</u>	<u>243,359</u>	<u>269,749</u>	<u>294,892</u>
Net Revenues	<u>\$1,045,788</u>	<u>\$1,153,604</u>	<u>\$1,225,822</u>	<u>\$1,203,739</u>	<u>\$1,305,804</u>

Source: San Diego Auditor - Controller and Urban Futures, Inc.

The following table shows the ten largest property taxpayers, by assessed value, in the Project Area.

**Table 4
Largest Fiscal Year 2003-04 Property Taxpayers, by Assessed Value**

<u>Property Owner</u>	<u>Primary Land Use</u>	<u>2003-04 Assessed Valuation</u>	<u>% of Total (1)</u>
Home Depot	Commercial / Store	\$13,000,000	5.45%
G M S Five LLC	Community Shopping	11,652,059	4.88
V G Holdings LLC	Senior Apartments	8,641,643	3.62
Commercial Net Lease Realty	Grocery/Drug Store	7,210,825	3.02
Terrace Gardens LLC	Senior Apartments	6,937,315	2.91
American Stores Properties Inc.	Grocery/Drug Store	6,130,733	2.57
Rekab Properties Ltd.	Large Com Auto Sales	5,631,230	2.36
Golden Grove Terrace Apartment	Senior Apartments	5,030,708	2.11
Armer/Armer Investments	Commercial / Store	4,751,875	1.99
Murray C. Greengrass	Industrial	<u>3,946,218</u>	<u>1.65</u>
Total		<u>\$72,932,606</u>	<u>30.56%</u>

Source: San Diego County Assessor 2003-04 Secured Tax Rolls

(1) The Project Area total secured value for fiscal year 2003-04 is \$238,631,197.

Annual Tax Receipts to Tax Levy

The County apportions tax revenues to redevelopment agencies based upon the amount of the tax levy that is received from the taxpayers. The following table illustrates the tax revenue collections for the previous five fiscal years.

Table 5
Tax Revenue Collections

<u>Fiscal Year</u>	<u>Original Tax Levy</u>	<u>Current Year Apportioned</u>	<u>Prior Year Collections</u>	<u>Total Apportioned</u>	<u>Current Collections Percentage</u>	<u>Percentage Total Collections</u>
1998-99	1,044,132	1,019,957	28,531	1,048,488	97.68%	100.42%
1999-00	1,108,602	1,080,877	24,073	1,104,950	97.50%	99.67%
2000-01	1,260,733	1,231,032	24,626	1,255,659	97.64%	99.60%
2001-02	1,335,382	1,303,361	25,085	1,328,447	97.60%	99.48%
2002-03	1,498,968	1,467,693	23,334	1,491,027	97.91%	99.47%

Source: San Diego County Auditor-Controller's Office.

Appeals of Assessed Values

Pursuant to California law, property owners may apply for a reduction of their property tax assessment by filing a written application, in the form prescribed by the State Board of Equalization, with the appropriate county board of equalization or assessment appeals board. After the applicant and the assessor have presented their arguments, the Appeals Board makes a final decision on the proper assessed value. The Appeals Board may rule in the assessor's favor, in the applicant's favor or the Appeals Board may set its own opinion of the proper assessed value, which may be more or less than either the assessor's opinion or the applicant's opinion.

Any reduction in the assessment ultimately granted applies to the year for which application is made and during which the written application was filed. After a reduction is allowed, the property is reviewed on an annual basis to determine its full cash value and the valuation may be adjusted accordingly. This may result in further reductions or increases in value. Such increases are in accordance with the actual cash value of the property and may exceed the maximum annual inflationary growth rate allowed on other properties under Article XIII A of the State Constitution. Once the property has regained its prior value, adjusted for inflation, it is once again subject to the annual inflationary growth rate allowed under Article XIII A.

Appeals for reduction in the "base year" value of an assessment, if successful, reduce the assessment for the year in which the appeal is taken and prospectively after that. The "base year" is determined by the completion date of new construction or the date of change of ownership. Any base year appeal must be made within four years of the change of ownership or new construction date.

Refunds for taxpayer overpayment of property taxes may include refunds for overpayment of taxes in years after that which was appealed. Any taxpayer payment of property taxes that is based on a value that is subsequently adjusted downward will require a refund for overpayment.

There are three pending appeals within the Project Area. None of the Project Area's top ten taxpayers have pending appeals of their assessed value. The following table shows the appeal history since Fiscal Year 1998-99.

**Table 6
Appeal History**

<u>Lien Year</u>	<u>Total Appeals</u>	<u>Resolved Appeals</u>	<u>Successful Appeals</u>	<u>Successful Original Value</u>	<u>Successful Appeal Value Loss</u>
1998-99	0	13	10	\$10,979,382	\$1,247,201
1999-00	9	9	6	934,870	109,683
2000-01	4	4	0	0	0
2001-02	4	4	3	1,900,463	146,870
2002-03	2	2	1	1,110,788	110,788

Source: San Diego County Clerk of the Board of Supervisors

Tax Sharing Agreements

County Tax Sharing Agreement. On December 7, 1987, the County and the Agency entered into a tax sharing agreement pursuant to which the Agency is to pass through to the County 50% of the County's share of general levy tax increment revenue through fiscal year 2006/07, and 100% of the County's share of general levy tax increment revenue and inflationary growth beginning in fiscal year 2007/08. The County's share of general levy tax increment revenue is stipulated in the agreement as 24.98% of the general levy. In addition, the County will be entitled to the full amount of any increase in tax override that may be levied on its behalf.

School District Tax Sharing Agreement. On May 16, 1988, the Agency entered into an agreement entitled "Agreement for Cooperation Between Lemon Grove School District, City of Lemon Grove and the Redevelopment (sic) Agency of the City of Lemon Grove" (the "School District Agreement"). Pursuant to the School District Agreement, the school district is to be allocated \$1,000,000 over a ten year period beginning in fiscal year 1996/97. Some or all of this amount may be provided by the Agency in the form of new construction that benefits the school district. The Agency will annually pay \$83,333 through 2006/07. The payment of this obligation from Tax Revenues is subordinate to the payment of debt service on the Bonds.

Grossmont Union High School District and Grossmont-Cuyamaca Community College District--Base Year Adjustments. Under the Redevelopment Law, school districts and community college districts may elect to receive their share of tax increment revenues in the event that no pass-through agreement is entered. Although the high school district and the community college district have not made such an election, County policy automatically allocates each district's share to each respective district. The Agency has not challenged this practice. Accordingly, such allocation by the County is excluded from the Agency's computation of tax increment revenue.

Bob Baker Enterprises Disposition and Development Agreement. The Agency entered into a Disposition and Development Agreement with Bob Baker Enterprises in December, 1993 to provide general redevelopment assistance in the development of a new car dealership facility. Agency agrees to pay the developer quarterly an amount equal to percentages of sales tax revenue generated by the dealership in each of the first five years of operation. The percentage increases each year to a maximum of 30% on the first \$100,000; 40% on the second \$100,000 and 50% on amounts over \$200,000 in the fifth year of operation. The first payment

was made in 1995-96. The payment of this obligation from Tax Revenues is subordinate to the payment of debt service on the Bonds.

Tax Increment Revenue Projections and Debt Service Coverage

The following tables sets forth the projected growth in tax increment revenues in the Project Area. The projected growth in real property taxable values includes anticipated value added from the identified new developments identified under the subheading "Developments Within the Project Area" above.

Table 7
Projected Tax Revenues

<u>Fiscal Year</u>	<u>Assessed Valuation (1)</u>	<u>Incremental Assessed Valuation (2)</u>	<u>Gross Tax Increment (3)</u>	<u>Pass-Through Amount (4)</u>	<u>County Admin. Fees</u>	<u>Projected Tax Revenues</u>
2004-05	\$284,467,384	\$178,026,579	\$1,780,266	(\$320,770)	(\$17,803)	\$1,441,693
2005-06	293,001,405	186,560,600	1,865,606	(338,681)	(18,656)	1,508,269
2006-07	301,791,448	195,350,643	1,953,506	(357,038)	(19,535)	1,576,933
2007-08	310,845,191	204,404,386	2,044,044	(589,130)	(20,440)	1,434,473
2008-09	320,170,547	213,729,742	2,137,297	(618,148)	(21,373)	1,497,777
2009-10	329,775,663	223,334,858	2,233,349	(647,940)	(22,333)	1,563,075

Source: Urban Futures Incorporated

- (1) FY 2003-04 assessed valuation provided by San Diego County Auditor-Controller. Assessed valuation growth is based on a 3% annual growth factor for the period FY 2004-05 to FY 2009-10, with \$8,296,300 of assessed valuation added in FY 04-05 for resale activity and building permits issued for new construction projects in the Project Area.
- (2) Incremental assessed valuation for a given year is current valuation for such year, less base year assessed valuation in the amount of \$106,440,805.
- (3) Gross tax increment is incremental assessed valuation multiplied by the tax rate of 1.00%.
- (4) Pass through amounts pursuant to the terms of Pass Through Agreements.

**Table 8
Projected Debt Service Coverage
Housing Portion of the Bonds**

Bond Year Ending (August 1)	Estimated Housing Portion of Tax Revenues	Debt Service on Housing Portion of Tax Revenues				Estimated Coverage on Housing Portion of Tax Revenue
		<u>1998 Bonds</u>	<u>Non-Escrowed 2004 Bonds</u>	<u>Escrowed 2004 Bonds</u>	<u>Total</u>	
2005	\$356,053.16	\$144,117.50	\$113,280.69	\$25,616.91	\$283,015.10	1.26
2006	373,121.20	142,117.50	115,072.50	26,273.76	283,463.76	1.32
2007	390,701.29	140,117.50	114,472.50	36,273.76	290,863.76	1.34
2008	408,808.77	143,077.50	113,872.50	36,048.76	292,998.76	1.40
2009	427,459.48	140,737.50	113,322.50	35,773.76	289,833.76	1.47
2010	446,669.72	143,150.00	112,702.50	35,463.76	291,316.26	1.53
2011	466,456.26	140,275.00	117,027.50	35,126.26	292,428.76	1.60
2012	486,836.39	142,400.00	116,121.26	34,763.76	293,285.02	1.66
2013	507,827.93	144,237.50	110,171.26	39,383.76	293,792.52	1.73
2014	529,449.22	140,787.50	114,371.26	38,783.76	293,942.52	1.80
2015	551,719.14	142,337.50	113,340.00	38,165.00	293,842.50	1.88
2016	574,657.17	143,600.00	112,265.00	37,520.00	293,385.00	1.96
2017	598,283.33	144,575.00	111,165.00	36,860.00	292,600.00	2.04
2018	622,618.28	140,262.50	115,040.00	36,185.00	291,487.50	2.14
2019	647,683.27	140,950.00	113,660.00	35,495.00	290,105.00	2.23
2020	673,500.22	141,350.00	117,250.00	39,790.00	298,390.00	2.26
2021	700,091.68	141,462.50	115,500.00	38,790.00	295,752.50	2.37
2022	727,480.87	141,287.50	113,750.00	37,790.00	292,827.50	2.48
2023	755,691.75	140,825.00	117,000.00	36,790.00	294,615.00	2.57
2024	784,748.95	145,075.00	110,000.00	35,790.00	290,865.00	2.70
2025	814,677.87	143,750.00	113,250.00	34,790.00	291,790.00	2.79
2026	845,504.65	142,137.50	116,250.00	38,765.00	297,152.50	2.85
2027	877,256.24	145,237.50	109,000.00	37,483.76	291,721.26	3.01
2028	909,960.37	142,762.50	112,000.00	36,202.50	290,965.00	3.13
2029	943,645.63	—	254,750.00	34,921.26	289,671.26	3.26
2030	978,341.45	—	255,250.00	38,640.00	293,890.00	3.33
2031	1,014,078.14	—	255,250.00	37,020.00	292,270.00	3.47
2032	1,050,886.93	—	254,750.00	35,400.00	290,150.00	3.62
2033	1,088,799.99	—	253,750.00	38,780.00	292,530.00	3.72
2034	1,127,850.44	—	257,250.00	36,890.00	294,140.00	3.83

Source: Urban Futures Incorporated

Table 9
Projected Debt Service Coverage
Non- Housing Portion of the Bonds

Bond Year Ending (August 1)	Estimated Non- Housing Portion of Tax Revenues	Debt Service on Non-Housing Portion of Tax Revenues				Estimated Coverage on Non- Housing Portion of Tax Revenue
		1998 Bonds	Non-Escrowed 2004 Bonds	Escrowed 2004 Bonds	Total	
2005	\$1,085,639.64	\$548,130.00	\$235,007.50	\$ 68,766.75	\$851,904.25	1.27
2006	1,135,148.07	550,880.00	233,800.00	70,530.00	855,210.00	1.33
2007	1,186,231.81	553,130.00	229,900.00	120,530.00	903,560.00	1.31
2008	1,025,664.38	549,715.00	96,000.00	99,405.00	745,120.00	1.38
2009	1,070,317.36	550,875.00	96,000.00	98,580.00	745,455.00	1.44
2010	1,116,405.50	550,525.00	96,000.00	97,650.00	744,175.00	1.50
2011	1,163,973.77	554,600.00	96,000.00	96,637.50	747,237.50	1.56
2012	1,213,068.51	547,812.50	96,000.00	100,550.00	744,362.50	1.63
2013	1,263,737.53	550,737.50	96,000.00	99,220.00	745,957.50	1.69
2014	1,316,030.06	552,800.00	96,000.00	97,820.00	746,620.00	1.76
2015	1,369,996.88	549,000.00	96,000.00	96,376.26	741,376.26	1.85
2016	1,425,690.35	549,625.00	96,000.00	99,871.26	745,496.26	1.91
2017	1,483,164.39	549,387.50	96,000.00	98,111.26	743,498.76	1.99
2018	1,542,474.64	553,287.50	96,000.00	96,311.26	745,598.76	2.07
2019	1,603,678.41	551,037.50	96,000.00	99,471.26	746,508.76	2.15
2020	1,666,834.79	552,925.00	96,000.00	97,356.26	746,281.26	2.23
2021	1,732,004.70	553,662.50	96,000.00	100,106.26	749,768.76	2.31
2022	1,799,250.92	553,250.00	96,000.00	97,606.26	746,856.26	2.41
2023	1,868,638.15	551,687.50	96,000.00	100,106.26	747,793.76	2.50
2024	1,940,233.10	548,975.00	96,000.00	97,356.26	742,331.26	2.61
2025	2,014,104.53	550,112.50	96,000.00	99,606.26	745,718.76	2.70
2026	2,090,323.30	549,812.50	96,000.00	96,531.26	742,343.76	2.82
2027	2,168,962.46	548,075.00	96,000.00	98,456.26	742,531.26	2.92
2028	2,250,097.30	549,900.00	96,000.00	100,125.00	746,025.00	3.02
2029	2,333,805.41	—	646,000.00	96,537.50	742,537.50	3.14
2030	2,420,166.77	—	648,500.00	97,950.00	746,450.00	3.24
2031	2,509,263.84	—	649,500.00	98,900.00	748,400.00	3.35
2032	2,601,181.56	—	189,000.00	99,580.00	288,580.00	9.01
2033	2,696,007.53	—	—	99,990.00	99,990.00	26.96
2034	2,793,831.99	—	—	100,130.00	100,130.00	27.90

Source: Urban Futures Incorporated

The foregoing projections reflects the Agency's understanding of the assessment and tax apportionment procedures employed by the County. The County procedures are subject to change as a reflection of policy revisions or legislative mandate. While the Agency believes the estimates to be reasonable, taxable values resulting from actual appraisals may vary from the amounts assumed in the projections.

No assurances are provided by the Agency as to the certainty of the projected tax increment revenues shown on the foregoing table. Actual revenues may be higher or lower than what has been projected and are subject to valuation changes resulting from new developments or transfers of ownership not specifically identified herein, actual resolution of outstanding appeals, future filing of appeals, or the non-payment of taxes due.

Adjustments to Tax Increment Revenues

Property Tax Administrative Costs. The County currently reduces the amount of total tax increment revenue allocated to the Agency from the Project Area to cover property tax administrative costs. Legislation enacted in 1990 (SB 2557), and in 1992 (SB 1559) authorizes county auditors to determine property tax administrative costs proportionately attributable to local jurisdictions and, for the 1990-91 and 1991-92 Fiscal Years, to invoice the jurisdictions for such costs. Commencing in the 1992-93 Fiscal Year, the amounts due as local agencies' contribution to covering county administrative costs are to be allocated to the county as part of the overall system for the redistribution of property taxes (as opposed to being paid pursuant to invoices).

SB 2557 expressly includes redevelopment agencies as jurisdictions that are to be charged for property tax administrative costs. The County's administrative and collection fee for fiscal year 2003-04 is \$16,169, or approximately 1 percent of the projected 2003-04 gross Project Area revenue. As a result, the property tax administrative charge for future fiscal years is estimated at 1 percent of gross Project Area revenue.

Low and Moderate Income Housing. The Agency must set aside 20 percent of its allocated tax increment for low and moderate income housing purposes, except under certain specified conditions. It is the current policy of the Agency to make deposits into its Low and Moderate Income Housing Fund either through direct deposits to the Low and Moderate Income Housing Fund or by using Low and Moderate Income Housing Fund revenues for eligible debt service payments.

See "Tax Sharing Agreements" above.

BONDOWNERS' RISKS

The following information should be considered by prospective investors in evaluating whether to invest in the Bonds. However, the following does not purport to be an exhaustive listing of risks and other considerations which may be relevant to investing in the Bonds and the order in which the following information is presented is not intended to reflect the relative importance of any such risks.

Tax Revenues

The Tax Revenues allocated to the Agency, which constitute the primary security for the Bonds, are determined by the incremental assessed value of taxable property in the Project Area, the current rate or rates at which property in the Project Area is taxed and the percentage of taxes collected in the Project Area. Several types of events which are beyond the control of the Agency could occur and cause a reduction in available Tax Revenues. A reduction of taxable assessed values of property in the Project Area caused by economic or other factors beyond the Agency's control could occur (such as successful appeals by a property owner for a reduction in a property's assessed value, a reduction of the general inflationary rate, a reduction in transfers of property, construction activity or other events that permit reassessment of property at higher values, or the destruction of property caused by natural or other disasters), and have occurred in recent years thereby causing a reduction in Tax Revenues. Such a reduction in Tax Revenues could have an adverse impact on the Agency's ability to make timely payment of principal of and interest on the Bonds.

As described in greater detail under "LIMITATIONS ON TAX REVENUES—Property Tax Rate Limitations—Article XIII A," Article XIII A of the California

Constitution provides that the full cash value base of real property used in determining taxable value may be adjusted from year to year to reflect the inflation rate, not to exceed a two percent increase for any given year; or may be reduced to reflect a reduction in the consumer price index, comparable local data or any reduction in the event of declining property value caused by damage, destruction or other factors (as described above). Such measure is computed on a calendar year basis. Any resulting reduction in the full cash value over the term of the Bonds could reduce Tax Revenues securing the Bonds. See "LIMITATIONS ON TAX REVENUES—Property Tax Rate Limitations—Article XIII A."

Historically, some property owners within the Project Area have appealed for reductions in the assessed value of their properties. Reductions in the assessed value of secured property in the Project Area in recent years can be attributed in part to such appeals and reductions in property values generally. Tax Revenues may be reduced from current levels as a result of such appeals and reductions in property values generally. See "THE PROJECT AREA—Appeals of Assessed Values" herein.

In addition to the other existing limitations on Tax Revenues described below under "LIMITATIONS ON TAX REVENUES," the California electorate or Legislature could adopt a constitutional or legislative property tax decrease with the effect of reducing Tax Revenues payable to the Agency. There is no assurance that the California electorate or Legislature will not at some future time approve additional limitations that could reduce the Tax Revenues and adversely affect the security of the Bonds.

The Agency has no power to levy and collect property taxes. Any substantial delinquencies in the payment of property taxes by property owners in the Project Area could have an adverse effect on the Agency's ability to make timely debt service payments on the Bonds. Tax Revenues allocated to the Agency are distributed in November, April and July of each Fiscal Year. The payments are adjusted to reflect actual collections. See "LIMITATIONS ON TAX REVENUES—Property Tax Collection Procedures" herein.

Estimated Tax Revenues

The Agency believes that its estimates of future Tax Revenues to be reasonable, but to the extent the assessed valuation, the tax rates or the percentage of taxes collected are less than projected, the Tax Revenues available to pay debt service on the Bonds would be reduced. See "THE PROJECT AREA—Tax Increment Revenue Projections and Debt Service Coverage" herein.

No representations are being made as to the future Tax Revenues, or as to whether the estimated Tax Revenues as shown under the heading "THE PROJECT AREA—Tax Increment Revenue Projections and Debt Service Coverage" will be realized.

In estimating that the total Tax Revenues to be received by the Agency will be sufficient to pay debt service on the Bonds, the Agency has relied on the actual historical Tax Revenues and made certain assumptions with regard to future assessed valuation in the Project Area, future tax rates and the percentage of taxes collected. The Agency believes these assumptions to be reasonable, but there is no assurance these assumptions will be realized and to the extent that the assessed valuation and the tax rates are less than expected, the total Tax Revenues available to pay debt service on the Bonds will be reduced. Such reduced Tax Revenues may be insufficient to provide for the payment of debt service on the Bonds. See "SECURITY FOR THE BONDS" herein.

Parity Debt

The Agency may issue or incur obligations payable from Tax Revenues on a parity with its pledge of Tax Revenues to payment of the Bonds, but only to the extent permitted in the Indenture. See “SECURITY FOR THE BONDS—Issuance of Parity Debt.” The existence of and the potential for such obligations increases the risks associated with the Agency’s payment on the Bonds in the event of a decrease in the Agency’s collection of Tax Revenues.

Bankruptcy

The various legal opinions to be delivered concurrently with delivery of the Bonds will be qualified as to the enforceability of the various legal documents by limitations imposed by bankruptcy, reorganization, insolvency, fraudulent conveyance or other laws affecting rights of creditors generally. If any of such limitations are imposed, they may adversely affect the ability of the Trustee and the Bond owners to enforce their claims and assert their rights under the Indenture or the Agency Indentures.

Loss of Tax Exemption

In order to maintain the exclusion from gross income for federal income tax purposes of the interest on the Bonds, the Agency has covenanted in the Indenture to comply with each applicable requirement of section 103 and sections 141 through 150 of the Internal Revenue Code of 1986, as amended. The interest on the Bonds could become includable in gross income for purposes of federal income taxation retroactive to the date of issuance of the Bonds as a result of acts or omissions of the Agency in violation of this or other covenants in the Indenture. The Bonds are not subject to redemption or any increase in interest rates should an event of taxability occur and will remain outstanding until maturity or prior redemption under one of the redemption provisions contained in the Indenture. See “TAX MATTERS” herein.

Reduction in Taxable Value

Tax increment revenues allocated to the Agency are determined by the amount of incremental taxable assessed value in the Project Area and the current rate or rates at which property in the Project Area is taxed. The reduction of taxable values of property caused by economic factors beyond the Agency’s control, such as a relocation out of the Project Area by one or more major property owners, or the complete or partial destruction of such property caused by, among other eventualities, an earthquake, flood (see “Seismic Factors and Flooding” below), or other natural disaster, could cause a reduction in the Tax Revenues securing the Bonds. Property owners may also appeal to the County Assessor for a reduction of their assessed valuations. Such a reduction of assessed valuations, either on a case-by-case basis or as a blanket reduction due to a general decline in property values, and the resulting decline in Tax Revenues or the resulting refund of property taxes could have an adverse effect on the Agency’s ability to make timely payments of debt service on the Bonds. See “THE PROJECT AREA—Appeals of Assessed Values” herein.

Application of the provisions of Article XIII A(2)(d) of the California Constitution and section 68 of the California Revenue and Taxation Code may also result in a significant reduction of the assessed valuation of a property within the Project Area. These provisions permit a person who is displaced from property by eminent domain proceedings or by governmental action resulting in a judgment of inverse condemnation to transfer the adjusted base year value of the property from which the person is displaced to another comparable property anywhere within the State. Persons acquiring replacement property

must request assessment pursuant to these provisions within four (4) years of the date the property was acquired by eminent domain or purchase or the date the judgment of inverse condemnation becomes final. Any such assessment pursuant to these provisions of Article XIII A(2)(d) and section 68 of the California Revenue and Taxation Code could result in an unexpected reduction in the assessed valuation of a property within the Project Area.

Overlapping Debt Burdens

Certain properties within the Project Area are located within special assessment or community facilities districts previously created by the County to finance street, drainage, utility and other public facilities. Such properties are subject to relatively higher tax or special assessment levies than many other parcels in the County. These higher tax or special assessment burdens may increase the possibility of higher delinquency rates and may be a factor which slows development of such parcels.

Reduction in Inflationary Rate

As described in greater detail below, Article XIII A of the California Constitution provides that the full cash value of real property used in determining taxable value may be adjusted from year to year to reflect the inflationary rate, not to exceed a 2% increase for any given year, or may be reduced to reflect a reduction in the consumer price index or comparable local data. Such measure is computed on a calendar year basis. Because Article XIII A limits inflationary assessed value adjustments to the lesser of the actual inflationary rate or 2%, there have been years in which the assessed values were adjusted by actual inflationary rates, which were less than 2 percent. Since Article XIII A was approved, the annual adjustment for inflation has fallen below the 2% limitation four times: for 1993-94, 1%; for 1995-96, 1.19%; for 1996-97, 1.11%; and for 1999-00, 1.853%. In addition, the State Board of Equalization has directed county assessors to use an inflation adjustment of 1.867% in preparing the 2004-05 assessment rolls. The Agency is unable to predict if any adjustments to the full cash value of real property within the Project Area, whether an increase or a reduction, will be realized in the future.

Litigation Regarding 2% Limitation

On December 27, 2001, the Orange County Superior Court issued an order declaring the practice of "recapturing" to be unconstitutional. That order only applies to one property in Seal Beach. A second issue of "class action" was requested to be reviewed by the court and on December 12, 2002, the Superior Court certified class action status for this case, which could have the effect of extending this ruling to other similar cases. A third issue addressed by the court is related to notification to the taxpayers by the tax collector. On January 20, 2003, the Superior Court granted the motion for the tax collector to give some type of notice to taxpayers. The court put on hold this order pending final appellate review and a ruling on the "recapture" issue. The court entered a Final Judgment on April 18, 2003. In 2002 two local courts (Los Angeles and San Diego) ruled differently on the "recapture" issue.

On March 26, 2004, a state appeals court upheld Orange County's method of assessing property taxes. In its *County of Orange v. Bezaire* decision (commonly referred to as the "Pool decision"), the 4th District Court of Appeal held that the technique used by Orange County in assessing taxes, called "recapturing," is constitutional pursuant to Proposition 13, the property tax limit approved by voters in 1978. "Recapturing" means that the 2% annual inflation factor is calculated against the property's original purchase price regardless of any intervening decreases in property value. This process allows a tax assessor to increase the value of property above Proposition 13's annual 2% limit after property has

lost value or failed to increase in value in previous years, in order to recover revenues lost because of the temporary market decline. The plaintiff has appealed to the California Supreme Court. On July 22, 2004, the Supreme Court determined not to hear the appeal.

The Pool decision validates the “recapturing method” in which the base on which Proposition 13’s inflation factor is considered remains that of the original purchase price (or assessment at time of new construction) and not a reduced base resulting from a reassessment as the result of a decline in property values.

Levy and Collection of Taxes

The Agency has no independent power to levy and collect property taxes. Any reduction in the tax rate or the implementation of any constitutional or legislative property tax decrease could reduce the Tax Revenues, and accordingly, could have an adverse impact on the ability of the Agency to repay the Bonds. Likewise, delinquencies in the payment of property taxes and the impact of bankruptcy proceedings on the legal ability of taxing agencies to collect property taxes could have an adverse effect on the Agency’s ability to make timely Bond payments.

Real Estate and General Economic Risks

As hereinbefore stated in the above paragraph captioned “Reductions in Inflationary Rate,” Tax Revenues as presented herein as available for payment of any indebtedness of the Agency are based upon the latest actual amounts for the 2003-04 fiscal year. Redevelopment of real property within the Project Area by the Agency, as well as private development in the Project Area, may be adversely affected by changes in general economic conditions, fluctuations in the real estate markets and interest rates, unexpected increases in development costs, changes in or new governmental policies, including governmental policies to restrict or control certain kinds of development and by other similar factors. If development and redevelopment activities in the Project Area encounter significant obstacles of the kind described herein or other impediments, the economy of the Project Area could be adversely affected, causing reduced taxable valuation of property in the Project Area, a reduction of the Tax Revenues and a consequent reduction in Tax Revenues available to repay the Bonds. If there is a decline in the general economy of the Project Area, the owners of property within the Project Area may be less able or less willing to make timely payments of property taxes, causing a delay or stoppage of Tax Revenues received by the Agency from the Project Area.

Concentration of Land Ownership

Ownership of property within the Project Area is concentrated with a small number of owners, some of which are responsible for a significant percentage of the property taxes allocated to the Agency from the Project Area. **The top ten taxpayers account for approximately 45.1% of the Project Area incremental value and 30.6% of the total Project Area assessed value. A default by one or more of these owners in the payment of their property taxes would materially and adversely affect the ability of the Agency to pay debt service on the Bonds. Such a result could be affected by events not related to the operation of the businesses of such taxpayers, including earthquakes or other natural disasters or other economic or environmental events occurring outside of their control. See “THE PROJECT AREA—Description of the Project Area.”**

Hazardous Substances

An additional environmental condition that may result in the reduction in the assessed value of parcels in the Project Area would be the discovery of a hazardous substance that would limit the beneficial use of the property. In general, the owners and operators of an assessed parcel may be required by law to remedy conditions of the parcel relating to releases or threatened releases of hazardous substances. The federal Comprehensive Environmental Response, Compensation and Liability Act of 1980, sometimes referred to as CERCLA or the Superfund Act, is the most well known and widely applicable of these laws but California laws with regard to hazardous substances are also stringent and similar. Under many of these laws, the owner (or operator) is obligated to remedy a hazardous substance condition on the property whether or not the owner (or operator) has anything to do with creating or handling the hazardous substance. The effect, therefore, should any of the assessed parcels be affected by a hazardous substance would be to reduce the marketability and value of the parcel by the costs of remedying the condition, since the purchaser, upon becoming owner, will become obligated to remedy the condition just as is the seller.

Seismic Factors and Flooding

The occurrence of severe seismic activity and/or flooding in the Project Area could result in substantial damage to property located in the Project Area, and could lead to successful appeals for reduction of assessed values of such property. Such a reduction could result in a decrease in Tax Revenues collected by the Agency.

State Budget Deficit—ERAF

In connection with its approval of the budget for the State for the 1992-93, 1993-94 and 1994-95 fiscal years, the State Legislature enacted legislation which, among other things, reallocated funds from redevelopment agencies to school districts by shifting a portion of each agency's tax increment (net of amounts due to other taxing agencies), to school districts for such fiscal years for deposit in ERAF. The amount required to be paid by a redevelopment agency to ERAF under such legislation was apportioned to all of its redevelopment project areas on a collective basis, and was not allocated separately to individual project areas.

Faced with a projected \$23.6 billion State budget gap for Fiscal Year 2002-03, the State Legislature adopted and sent to the Governor of the State as urgency legislation AB 1768, requiring redevelopment agencies to pay into ERAF in Fiscal Year 2002-03 an aggregate amount of \$75 million. The Agency paid into ERAF in Fiscal Year 2002-03 the amount of \$46,215 as its share of such \$75 million. See "LIMITATIONS ON TAX REVENUES."

As part of the overall legislation to enact the 2003-04 State Budget, the State enacted, as urgency legislation, SB 1045, being Chapter 260 of the Statutes of 2003 ("Chapter 260"), as part of the 2003-04 State Budget requiring redevelopment agencies to pay into ERAF in fiscal year 2003-04 an aggregate amount of \$135 million. Chapter 260 requires payments into ERAF in fiscal year 2003-04 only. Chapter 260 provides that one-half of an agency's ERAF obligation is calculated based on the gross tax increment received by the agency and the other one-half of the agency's ERAF obligation is calculated based on the net tax increment revenues (after any pass-through payments to other taxing entities). The Agency paid into ERAF in Fiscal Year 2003-04 the amount of \$127,301 as its share of such \$135 million (which amount is approximately 1.8 times the amount that the Agency was required to transfer to ERAF in Fiscal Year 2002-03).

On January 9, 2004, the Governor submitted the 2004-05 Governor's budget proposal to the California Legislature. The 2004-05 Governor's budget proposal identified \$22.1 billion worth of debt inherited from the prior gubernatorial administration and indicated that, absent any changes in policies, State budget deficits would continue, estimated at \$14 billion for fiscal year 2004-05. The 2004-05 Governor's budget proposal contemplated a shift of \$1.3 billion of revenues from local government to the State; but the manner in which this would be allocated among local governmental agencies (including redevelopment agencies) was not specified. The shift, as to redevelopment agencies, was proposed to be in the form of an increased ERAF shift beginning in 2004-05.

On March 2, 2004, voters in California approved Propositions 57 and 58 which were designed by the Governor to assist with the State budget shortfall. Proposition 57 authorized bond issues of up to \$15,000,000,000 to fund budget deficits and Proposition 58 requires the enactment of a balanced State budget.

On May 13, 2004, the Governor released his May Revision to the Proposed 2004-05 Budget (the "May Revision"). The May Revision relies on about \$3.6 billion in new resources relative to the January budget proposal. The May Revision reflects recent proposed multiyear agreements between the Governor and various parties relating to future funding for higher education and local governments. The May Revision includes the following related to redevelopment agencies: (a) redevelopment agencies would contribute \$250 million in each of the next two fiscal years to ERAF using the same formula as in current law, (b) county, city, special district and redevelopment agency property tax, sales tax, and vehicle license fee revenue would be permanently protected from State ERAF reallocations in future years through a constitutional amendment to be placed on the November general election ballot by the Legislature with the full support and leadership of the Governor, and (c) the second year of local government budget cuts will be repealed if the constitutional amendment does not pass at the November 2004 election.

If the ERAF provisions of the May Revision are incorporated into the 2004-05 budget, the Agency will be required to pay an amount equal to \$127,301 as its share of such \$250 million (which amount is approximately 1.9 times the amount that the Agency was required to transfer to ERAF in Fiscal Year 2003-04). However, as of the date of this Official Statement, the State Legislature has not approved a State budget for Fiscal Year 2004-05, and the Agency cannot predict if the budget for Fiscal Year 2004-05 will include all of the proposals of the May Revision's proposals. The budget for Fiscal Year 2004-05 could contain ERAF provisions that are more or less severe than those proposed in the May Revision.

In addition to potential ERAF provisions, the Agency cannot predict whether the State Legislature will enact any other legislation requiring additional or increased future shifts of tax increment revenues to the State and/or to schools, whether through an arrangement similar to ERAF or by other arrangements, and, if so, the effect on future Tax Revenues. Given the level of the State's budget deficit problems, tax increment available for payment of the Bonds may be substantially reduced in the future by actions of the State Legislature.

Information about the State budget and State spending is available at various State-maintained websites. Text of the budget may be found at the website of the Department of Finance, www.dof.ca.gov, under the heading "California Budget." An impartial analysis of the budget is posted by the Office of the Legislative Analyst at www.lao.ca.gov. In addition, various State official statements for its various debt obligations, many of which contain a summary of the current and past State budgets, may be found at the website of the State Treasurer, www.treasurer.ca.gov. All of such websites are provided for general

informational purposes only and the material on such sites is in no way incorporated into this Official Statement.

Book-Entry System

Beneficial Owners of the Bonds may experience some delay in their receipt of distributions of principal of, and interest on, the Bonds since distributions will be forwarded by the Trustee to DTC and DTC will credit such distributions to the accounts of the DTC Participants which will thereafter credit them to the accounts of the Beneficial Owners either directly or indirectly through indirect participants. See "THE Bonds—Book-Entry System" herein. Issuance of the Bonds in book-entry form may reduce the liquidity of the Bonds in the secondary trading market since investors may be unwilling to purchase Bonds for which they cannot obtain physical certificates. In addition, since transactions in the Bonds can be effected only through DTC, DTC Participants, indirect participants and certain banks, the ability of a Beneficial Owner to pledge Bonds to persons or entities that do not participate in the DTC system, or otherwise to take actions in respect of such Bonds, may be limited due to lack of a physical certificate. Beneficial Owners will not be recognized by the Trustee as registered owners for purposes of the Indenture, and Beneficial Owners will be permitted to exercise the rights of registered owners only indirectly through DTC and the DTC Participants. See "THE BONDS—Book-Entry System" herein and APPENDIX G—"BOOK-ENTRY SYSTEM."

LIMITATIONS ON TAX REVENUES

Property Tax Limitations—Article XIII A

California voters, on June 6, 1978, approved an amendment (commonly known as both Proposition 13 and the Jarvis-Gann Initiative) to the California Constitution. This amendment, which added Article XIII A to the California Constitution, among other things, affects the valuation of real property for the purpose of taxation in that it defines the full cash value of property to mean "the county assessor's valuation of real property as shown on the fiscal year 1975-76 tax bill under full cash value, or thereafter, the appraised value of real property when purchased, newly constructed, or a change in ownership has occurred after the 1975 assessment." The full cash value may be adjusted annually to reflect inflation at a rate not to exceed two percent per year, or any reduction in the consumer price index or comparable local data, or any reduction in the event of declining property value caused by damage, destruction or other factors. The amendment further limits the amount of any ad valorem tax on real property to one percent of the full cash value except that additional taxes may be levied to pay debt service on indebtedness approved by the voters prior to July 1, 1978. In addition, an amendment to Article XIII was adopted in October 1986 by initiative which exempts any bonded indebtedness approved by two-thirds (55% in certain instances) of the votes cast by the voters for the acquisition or improvement of real property from the one percent limitation.

On September 22, 1978, the California Supreme Court upheld the amendment over challenges on several state and federal constitutional grounds (*Amador Valley Joint Union School District v. State Board of Equalization*). The Court reserved certain constitutional issues and the validity of legislation implementing the amendment for future determination in proper cases.

In the general elections of 1986, 1988 and 1990, the voters of the State approved various measures which further amended Article XIII A. One such amendment generally provides that the purchase or transfer of (i) real property between spouses or (ii) the

principal residence and the first \$1,000,000 of the full cash value of other real property between parents and children, do not constitute a “purchase” or “change of ownership” triggering reassessment under Article XIII A. This amendment has reduced local property tax revenues. Other amendments permitted the Legislature to allow persons over 55 who sell their residence on or after November 5, 1986, to buy or build another of equal or lesser value within two years in the same county, to transfer the old residence’s assessed value to the new residence, and permitted the Legislature to authorize each county under certain circumstances to adopt an ordinance making such transfers of assessed value applicable to situations in which the replacement dwelling purchased or constructed after November 8, 1988, is located within the county and the original property is located in another county within California.

In the October 1990 election, the voters approved additional amendments to Article XIII A permitting the State Legislature to extend the replacement dwelling provisions applicable to persons over 55 to severely disabled homeowners for replacement dwellings purchased or newly constructed on or after June 5, 1990, and to exclude from the definition of “new construction,” triggering reassessment, improvements to certain dwellings for the purpose of making the dwelling more accessible to severely disabled persons. In the November 1990 election, the voters approved the amendment of Article XIII A to permit the State Legislature to exclude from the definition of “new construction” seismic retrofitting improvements or improvements utilizing earthquake hazard mitigation technologies constructed or installed in existing buildings after November 6, 1990.

Challenges to Article XIII A

The U.S. Supreme Court struck down as a violation of equal protection certain property tax assessment practices in West Virginia, which had resulted in vastly different assessments of similar properties. Since Proposition 13 provides that property may only be reassessed up to two percent per year, except upon change of ownership or new construction, recent purchasers may pay substantially higher property taxes than long-time owners of comparable property in a community. The Supreme Court in the West Virginia case expressly declined to comment in any way on the constitutionality of Proposition 13.

Based on the decision in the West Virginia case, property owners in California brought three suits challenging the acquisition value assessment provisions of Article XIII A. Two cases involved residential property, and one case involved commercial property. In all three cases, State trial and appellate courts have upheld the constitutionality of Article XIII A’s assessment rules and concluded that the West Virginia case did not apply to California’s laws. On June 3, 1991, the U.S. Supreme Court agreed to hear the appeal in the challenge relating to commercial property, but the plaintiff subsequently withdrew its case. On June 18, 1992, the U.S. Supreme Court upheld the decision in *Nordlinger v. Hahn*, one of the challenges relating to residential property.

Implementing Legislation

Legislation enacted by the California Legislature to implement Article XIII A (Statutes of 1978, Chapter 292, as amended) provides that, notwithstanding any other law, local agencies may not levy any property tax, except to pay debt service on indebtedness approved by the voters prior to July 1, 1978, and that each county will levy the maximum tax permitted by Article XIII A.

The apportionment of property taxes in fiscal years after 1978-79 has been revised pursuant to Statutes of 1979, Chapter 282 which provides relief funds from State moneys beginning in fiscal year 1978-79 and is designed to provide a permanent system for sharing

State taxes and budget surplus funds with local agencies. Under Chapter 282, cities and counties receive about one-third more of the remaining property tax revenues collected under Proposition 13 instead of direct State aid. School districts receive a correspondingly reduced amount of property taxes, but receive compensation directly from the State and are given additional relief.

Future assessed valuation growth allowed under Article XIII A (new construction, change of ownership, 2% annual value growth) will be allocated on the basis of "situs" among the jurisdictions that serve the tax rate area within which the growth occurs except for certain utility property assessed by the State Board of Equalization which is allocated by a different method discussed herein.

Unitary Property

Assembly Bill 454 Statutes of 1987, Chapter 921 ("AB 454"), provided that revenues derived from Unitary Property (consisting mostly of operations property owned by utility companies), commencing with fiscal year 1988-89, will be allocated as follows: (1) for revenues generated from the one percent tax rate, (a) each jurisdiction, including redevelopment project areas, will receive a percentage up to 102 percent of its prior year State-assessed unitary revenue; and (b) if county-wide revenues generated from Unitary Property are greater than 102 percent of the previous year's revenues, each jurisdiction will receive a percentage share of the excess unitary revenues by a specified formula, and (2) for revenue generated from the application of the debt service tax rate to county-wide unitary taxable value, each jurisdiction's annual debt service requirements and the percentage of property taxes received by each jurisdiction from unitary property taxes. This provision applies to all Unitary Property except railroads whose valuation will continue to be allocated to individual tax rate areas.

The provisions of AB 454 do not constitute an elimination of assessment of any State-assessed properties nor a revision of the method of assessing utilities by the State Board of Equalization. Generally, AB 454 allows valuation growth or decline of Unitary Property to be shared by all jurisdictions within a county.

On February 1, 1991, the Superior Court for the County of Sacramento issued a Statement of Decision in *AT&T Communications of California, et al. v. State Board of Equalization* which reduced the valuation of certain unitary property owned by AT&T for property tax purposes. Under the decision, the valuation method used by the State Board of Equalization to assess unitary public utility property was declared illegal and a new method of valuation, resulting in significantly lower values and therefore significantly lower potential property tax revenues, was imposed. The effect on AT&T's statewide assessed value was to reduce it from approximately \$1,750,000,000 to approximately \$1,100,000,000. As a result of this case, on May 1, 1992, 57 of California's 58 counties, the State Board of Equalization and a number of other utility companies whose unitary property valuations could be affected by the principles announced in the Superior Court decision entered into a settlement agreement. On July 14, 1993, the Superior Court for the County of Sacramento entered a judgment validating the settlement agreement.

Although the settlement agreement is complex and extensive, its substance is represented by the signatory public utilities' agreement (except AT&T) to abandon their right to refunds since 1983 in return for lowered assessed valuations for the next eight fiscal years pursuant to an agreed formula.

To administer the allocation of unitary tax revenues to redevelopment agencies, the County no longer includes the taxable value of utilities as part of the reported taxable

values of project areas, therefore, the base year values of project areas have been reduced by the amount of utility value that existed originally in the base year. Within the Project Area, the Auditor Controller has allocated \$2,036.31 in unitary tax revenue to the Agency for fiscal year 2002-03. This amount is reasonably consistent with the unitary revenue allocations made to the Agency in prior years. The Agency has assumed no increase in the amounts of unitary tax revenues for purposes of projecting Tax Revenues.

Property Tax Collection Procedures

Classifications. In California, property which is subject to ad valorem taxes is classified as "secured" or "unsecured." Secured and unsecured property are entered on separate parts of the assessment roll maintained by the county assessor. The secured classification includes property on which any property tax levied by the County becomes a lien on that property sufficient, in the opinion of the county assessor, to secure payment of the taxes. Every tax which becomes a lien on secured property has priority over all other liens on the secured property, regardless of the time of the creation of other liens. A tax levied on unsecured property does not become a lien against unsecured property, but may become a lien on certain other property owned by the taxpayer.

Collections. The method of collecting delinquent taxes is substantially different for the two classifications of property. The taxing authority has four ways of collecting unsecured property taxes in the absence of timely payment by the taxpayer: (1) a civil action against the taxpayer; (2) filing a certificate in the office of the county clerk specifying certain facts in order to obtain a judgment lien on certain property of the taxpayer; (3) filing a certificate of delinquency for record in the county recorder's office, in order to obtain a lien on certain property of the taxpayer; and (4) seizure and sale of the personal property, improvements or possessory interests belonging or assessed to the assessee.

The exclusive means of enforcing the payment of delinquent taxes with respect to property on the secured roll is the sale of property securing the taxes to the State for the amount of taxes which are delinquent.

Penalties. A 10% penalty is added to delinquent taxes which have been levied with respect to property on the secured roll. In addition, property on the secured roll on which taxes are delinquent is declared in default on or about June 30 of the fiscal year. Such property may thereafter be redeemed by payment of the delinquent taxes and a delinquency penalty, plus a redemption penalty of 1.5% per month to the time of redemption and a \$15 Redemption Fee. If taxes are unpaid for a period of five years or more, the property is recorded in a "Power to Sell" status and is subject to sale by the county tax collector. A 10% penalty also applies to the delinquent taxes on property on the unsecured roll, and further, an additional penalty of 1.5% per month accrues with respect to such taxes beginning the first day of the third month following the delinquency date.

Delinquencies. The valuation of property is determined as of January 1 each year and equal installments of taxes levied upon secured property become delinquent on the following December 10 and April 10. Taxes on unsecured property are due January 1. Unsecured taxes enrolled by July 31, if unpaid, are delinquent August 31 at 5:00 p.m. and are subject to penalty; unsecured taxes added to the roll after July 31, if unpaid, are delinquent on the last day of the month succeeding the month of enrollment.

Supplemental Assessments. Legislation enacted in 1983 (Chapter 498, Statutes of 1983) provides for the supplemental assessment and taxation of property as of the occurrence of a change of ownership or completion of new construction.

Chapter 498 provided increased revenue to redevelopment agencies to the extent that supplemental assessments of new construction or changes of ownership occur within the boundaries of redevelopment projects subsequent to the January 1 lien date. To the extent such State supplemental assessments occur within the Project Area, the Tax Revenues for the Project Area may increase.

Tax Collection Fees. In 1990, the State Legislature enacted Senate Bill 2557 (Chapter 466, Statutes of 1990) (“SB 2557”) which allows counties to charge for the cost of assessing, collecting and allocating property tax revenues to local government jurisdictions on a prorated basis. Two recent decisions have interpreted the provisions of SB 2557 and have upheld the inclusion of redevelopment agencies as a local government Agency which must share the cost of property tax administration. The 1992 enactment of Senate Bill 1559 (Chapter 697) and the decision of the California Court of Appeal in *Arcadia Redevelopment Agency v. Ikemoto* have clarified that redevelopment agencies, such as the Agency, are to share in the cost of property tax administration charged by most California counties, including the County. During fiscal years 2001-02 and 2002-03, the County withheld approximately \$11,989 and \$14,238 respectively, from the Agency for such administrative costs.

Appropriations Limitations—Article XIII B

On November 6, 1979, California voters approved Proposition 4, the so-called Gann Initiative, which added Article XIII B to the California Constitution. The principal effect of Article XIII B is to limit the annual appropriations of the State and any city, county, school district, authority or other political subdivision of the State to the level of appropriations for the prior fiscal year, as adjusted for changes in the cost of living, population and services rendered by the government entity.

Effective November 30, 1980, the California Legislature added section 33678 to the Redevelopment Law which provided that the allocation of taxes to a redevelopment Agency for the purpose of paying principal of, or interest on, loans, advances, or indebtedness will not be deemed the receipt by such Agency of proceeds of taxes levied by or on behalf of the Agency within the meaning of Article XIII B, nor will such portion of taxes be deemed receipt of taxes by, or an appropriation subject to the limitation of, any other public body within the meaning or for the purpose of the Constitution and laws of the State, including section 33678 of the Redevelopment Law.

State Board of Equalization and Property Assessment Practices

On December 10, 1998, the State Board of Equalization (“SBOE”) approved revisions to its guidelines regarding the valuation of intangible business and commercial property for property tax purposes. The SBOE approved these revisions over the strong objections of the California Assessors Association (“CAA”), an organization representing all 58 County Assessors in California.

The Agency is not able to predict whether the revised SBOE guidelines will cause any reductions in tax increment revenues and, hence, in Tax Revenues. However, the Agency does not believe that the SBOE’s adoption of the revised guidelines will affect its ability to pay debt service on the Bonds.

Exclusion of Tax Revenues for General Obligation Bonds Debt Service

An initiative to amend the California Constitution entitled “Property Tax Revenues Redevelopment Agencies” was approved by California voters at the November 8, 1988

general election. Under prior law, a redevelopment agency using tax increment revenue received additional property tax revenue whenever a local government increased its property tax rate to pay off its general obligation bonds. This initiative amended the California Constitution to allow the California Legislature to prohibit redevelopment agencies from receiving any of the property tax revenues raised by increased property tax rates imposed by local governments to make payments on their bonded indebtedness.

The initiative only applies to tax rates levied to finance general obligation bonds approved by the voters on or after January 1, 1989. Any revenue reduction to redevelopment agencies would depend on the number and value of the general obligation bonds approved by voters in prior years, which tax rate will reduce due to increased valuation subject to the tax or the retirement of the indebtedness. The Agency receives no tax increment as a result of general obligation bond tax levies.

Proposition 218

On November 5, 1996, California voters approved Proposition 218-Voter Approval for Local Government Taxes—Limitation on Fees, Assessments, and Charges-Initiative Constitutional Amendment. Proposition 218 added Articles XIIC and XIID to the California Constitution, imposing certain vote requirements and other limitations on the imposition of new or increased taxes, assessments and property-related fees and charges. Tax Revenues securing the Bonds are derived from property taxes which are outside the scope of taxes, assessments and property-related fees and charges which were limited by Proposition 218.

AB 1290

In 1993, the California Legislature enacted Assembly Bill 1290 (“AB 1290”) which contained several significant changes in the Redevelopment Law. Among the changes made by AB 1290 was a provision that limits the period of time for incurring and repaying loans, advances and indebtedness payable from tax increment revenues. In general, a redevelopment plan may terminate not more than 40 years following the date of original adoption, and loans, advances and indebtedness may be repaid during a period extending not more than 10 years following the date of termination of the redevelopment plan. See “THE PROJECT AREA—Redevelopment Plan Limitations.”

The Agency’s Redevelopment Plan is fully in compliance with AB 1290.

SB 211

Senate Bill 211 (“SB 211”), which was adopted in 2001 and took effect as of January 1, 2002, allows redevelopment agencies, by ordinance, to eliminate the time limit on establishing indebtedness (meaning the redevelopment Agency could incur debt up to the end of the effectiveness of its redevelopment plan), but would in turn trigger statutory pass-throughs to all taxing entities with whom the redevelopment Agency does not have a pass-through agreement at the time the ordinance is adopted. If the Agency chooses to eliminate the Agency’s existing tax increment indebtedness limit as permitted by SB211, the statutory pass-throughs would apply starting in the year after what is now the final year to incur indebtedness. To date, the Agency has not determined to eliminate such time limit.

Future Initiatives

Article XIIA, Article XIIB and certain other propositions affecting property tax levies were each adopted as measures which qualified for the ballot pursuant to California’s

initiative process. From time to time other initiative measures could be adopted, further affecting Agency revenues or the Agency's ability to expend revenues.

Low and Moderate Income Housing

Chapter 1337, Statutes of 1976, added sections 33334.2 and 33334.3 to the law requiring redevelopment agencies to set aside 20% of all tax increment revenues allocated to redevelopment agencies from redevelopment project areas adopted after December 31, 1976, in a low- and moderate-income housing fund to be expended for authorized low- and moderate-income housing purposes. Amounts on deposit in the low- and moderate-income housing fund may also be applied to pay debt service on bonds, loans or advances of redevelopment agencies to provide financing for such low- and moderate-income housing purposes.

Statement of Indebtedness

Under the Redevelopment Law, the Agency must file with the County Auditor a statement of indebtedness for the Project Area by October 1 of each year. As described below, the statement of indebtedness controls the amount of tax increment revenue that will be paid to the Agency in each fiscal year.

Each statement of indebtedness is filed on a form prescribed by the State Controller and specifies, among other things: (i) the total amount of principal and interest payable on all loans, advances or indebtedness (including the Bonds) (the "Debt"), both over the life of the Debt and for the current fiscal year, and (ii) the amount of "available revenue" as of the end of the previous fiscal year.

"Available Revenue" is calculated by subtracting the total payments on Debt during the previous fiscal year from the total revenues (both tax increment revenues and other revenues) received during the previous fiscal year, plus any carry-forward from the prior fiscal year. Available Revenue include amounts held by the Agency and irrevocably pledged to the payment of Debt other than amounts set aside for low- and moderate-income housing.

The County Auditor may only pay tax increment revenue to the Agency in any fiscal year to the extent that the total remaining principal and interest on all Debt exceeds the amount of available revenues as shown on the statement of indebtedness.

The statement of indebtedness constitutes prima facie evidence of the indebtedness of the Agency; however, the County Auditor may dispute the statement of indebtedness in certain cases. Section 33675 of the Redevelopment Law provides for certain time limits controlling any dispute of the statement of indebtedness, and allows for Superior Court determination of such dispute if it cannot be resolved by the Agency and the County. Any such action may only challenge the amount of the Debt as shown on the statement, and not the validity of any Debt or its related contract or expenditures. No challenge can be made to payments to a trustee in connection with a bond issue or payments to a public agency in connection with payments by that public agency with respect to a lease or bond issue.

CERTAIN LEGAL MATTERS

Legal Opinions

The legal opinion of Stradling Yocca Carlson & Rauth, Newport Beach, California, as Bond Counsel, approving the validity of the Bonds, will be made available to purchasers at the time of original delivery of the Bonds and the proposed form thereof appears in Appendix E hereto. Bond Counsel's employment as bond counsel is limited to a review of the legal proceedings required for the authorization of the Bonds and to rendering the opinion set forth in Appendix E hereto.

Quint & Thimmig LLP, San Francisco, California, is serving as Disclosure Counsel to the Agency. Certain legal matters will be passed upon for the Agency by McDougal, Love, Eckis, Smith, Boehmer & Foley, El Cajon, California, as counsel to the Agency.

Payment of the fees and expenses of Bond Counsel and Disclosure Counsel is contingent upon the sale and delivery of the Bonds.

Enforceability of Remedies

The remedies available to the Trustee and to the registered owners of the Bonds upon an event of default under the Indenture and any other document described herein are in many respects dependent upon regulatory and judicial actions which are often subject to discretion and delay. Under existing law and judicial decisions, the remedies provided for under such documents may not be readily available or may be limited. The various legal opinions to be delivered concurrently with the delivery of the Bonds will be qualified to the extent that the enforceability of the legal documents with respect to the Bonds are subject to limitations imposed by bankruptcy, reorganization, insolvency or other similar laws affecting the rights of creditors generally and by equitable remedies and proceedings generally.

RATINGS

Standard & Poor's Ratings Services ("S&P") has assigned its municipal bond rating of "AA" to the Bonds with the understanding that upon delivery of the Bonds, the Financial Guaranty Insurance Policy will be issued by the Bond Insurer. In addition, S&P has assigned its underlying municipal bond rating of "BBB" to the Bonds. Such ratings reflect only the views of such organization and an explanation of the significance of such ratings may be obtained from them as follows: Standard & Poor's Ratings Services, 55 Water Street, New York, New York 10004, (212) 438-2124. There is no assurance that such ratings will continue for any given period of time or that they will not be revised downward or withdrawn entirely by such rating agency, if in the judgment of such rating agency, circumstances so warrant. Any such downward revision or withdrawal of such ratings may have an adverse effect on the market price of the Bonds.

CONTINUING DISCLOSURE

The Agency has covenanted for the benefit of holders and beneficial owners of the Bonds to provide certain financial information and operating data relating to the Agency by not later than February 15 following the end of the Agency's Fiscal Year (which reporting date would be March 31), commencing with the report for the 2003-2004 Fiscal Year (the "Annual Report"), and to provide notices of the occurrence of certain enumerated events, if

material. The Annual Report will be filed by the Agency with each Nationally Recognized Municipal Securities Information Repository, and with the appropriate State information depository, if any. The notices of material events will be filed by the Agency with the Municipal Securities Rulemaking Board (and with the appropriate State information depository, if any). The specific nature of the information to be contained in the Annual Report or the notices of material events is set forth in the Form of Continuing Disclosure Agreement in Appendix F hereto. These covenants have been made in order to assist the Underwriter in complying with S.E.C. Rule 15c2-12(b)(5). The Agency is current with respect to previous undertakings with regard to said Rule to provide annual reports or notices of material events.

ABSENCE OF LITIGATION

At the time the Bonds are delivered, the Agency will certify that, to its best knowledge, there is no litigation pending with respect to which the Agency has been served with process or know to be threatened against the Agency in any court or other tribunal of competent jurisdiction, State or federal, which seeks to enjoin or challenges the authority of the Agency to participate in the transactions contemplated by this Official Statement, the Bonds or the Indenture.

TAX MATTERS

In the opinion of Stradling Yocca Carlson & Rauth, a Professional Corporation, Newport Beach, California, Bond Counsel, under existing statutes, regulations, rulings and judicial decisions, interest on the Bonds is excluded from gross income for federal income tax purposes, and is not an item of tax preference for purposes of calculating the federal alternative minimum tax imposed on individuals and corporations. In the further opinion of Bond Counsel, interest on the Bonds is exempt from State personal income tax. Bond Counsel notes that, with respect to corporations, interest on the Bonds may be included as an adjustment in the calculation of alternative minimum taxable income which may affect the alternative minimum tax liability of such corporations.

In addition, the difference between the issue price of a Bond (the first price at which a substantial amount of the Bonds of a maturity is to be sold to the public) and the stated redemption price at maturity of such Bond constitutes original issue discount. Original issue discount accrues under a constant yield method, and original issue discount will accrue to a Bondowner before receipt of cash attributable to such excludable income. The amount of original issue discount that accrues to the Owner of the Bonds is excluded from the gross income of such Owner for federal income tax purposes, is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations, and is exempt from State personal income tax.

Bond Counsel's opinion as to the exclusion from gross income for federal income tax purposes of interest (and original issue discount) on the Bonds is based upon certain representations of fact and certifications made by the City, the Agency and others and is subject to the condition that the City and the Authority comply with all requirements of the Internal Revenue Code of 1986, as amended (the "Code"), that must be satisfied subsequent to the delivery of the Bonds to assure that interest (and original issue discount) on the Bonds will not become includable in gross income for federal income tax purposes. Failure to comply with such requirements might cause interest (and original issue discount) on the Bonds to be included in gross income for federal income tax purposes retroactive to the date of delivery of the Bonds. The Agency has covenanted to comply with all such

requirements. Bond Counsel has not undertaken to determine (or to inform any person) whether any actions taken (or not taken) or events occurring after the date of delivery of the Bonds may affect the tax status of the interest on the Bonds.

Bond Counsel's opinion may be affected by action taken (or not taken) or events occurring (or not occurring) after the date hereof. Bond Counsel has not undertaken to determine, or to inform any person, whether any such actions taken or events are taken or do occur. Although Bond Counsel has rendered an opinion that interest (and original issue discount) on the Bonds is excluded from gross income for income tax purposes provided that the Agency continues to comply with certain requirements of the Code, the ownership of and the accrual or receipt of interest (and original issue discount) with respect to the Bonds may otherwise affect the tax liability of the recipient. Bond Counsel expresses no opinion regarding any such consequences. Accordingly, all potential purchasers should consult their tax advisors before purchasing any of the Bonds.

UNDERWRITING

The Bonds are being purchased for reoffering by Kinsell, Newcomb & De Dios, Inc. (the "Underwriter"). The Underwriter has entered into an agreement with the Agency to purchase the Bonds at a price of \$6,064,581.95 (being the principal amount of the Bonds of \$6,330,000, less an Underwriter's discount of \$79,125.00 and less net original issue discount of \$186,293.05). The agreement pursuant to which the Underwriter will purchase the Bonds provides that the Underwriter will purchase all of the Bonds if any of the Bonds are purchased.

The Underwriter intends to reoffer the Bonds to the public initially at the yield set forth on the cover page of this Official Statement, which yield may subsequently change without any requirement of prior notice. The Underwriter reserves the right to join with dealers and other underwriters in reoffering the Bonds to the public. The Underwriter may reoffer and sell Bonds to certain dealers (including dealers depositing Bonds into investment trusts) at prices lower than the public offering prices, and such dealers may reallocate any such discounts on sales to other dealers.

MISCELLANEOUS

The purpose of this Official Statement is to supply information to prospective buyers of the Bonds. Quotations from, and summaries and explanations of, the Indenture and other documents and statutes contained herein do not purport to be complete, and reference is made to such documents, Indenture and statutes for full and complete statements of their provisions.

Unless otherwise noted, all information contained in this Official Statement pertaining to the Agency, the County and the Project Area has been furnished by the Agency. Any statement in this Official Statement involving matters of opinion, whether or not expressly so stated, are intended as such and not as representations of fact. This Official Statement is not to be construed as a contract or agreement between the Agency and the purchasers or registered owners of any of the Bonds.

The execution and delivery of this Official Statement has been duly authorized by the Agency.

LEMON GROVE COMMUNITY
DEVELOPMENT AGENCY

By /s/ Graham Mitchell
Executive Director

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APPENDIX A

**AUDITED FINANCIAL STATEMENTS
LEMON GROVE COMMUNITY DEVELOPMENT AGENCY
FOR THE FISCAL YEAR ENDING JUNE 30, 2003**

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CITY OF LEMON GROVE
COMMUNITY DEVELOPMENT AGENCY

COMPONENT UNIT
FINANCIAL STATEMENTS

WITH REPORT ON AUDIT BY
CERTIFIED PUBLIC ACCOUNTANTS

June 30, 2003

Brownell & Duffey
certified public accountants

CITY OF LEMON GROVE – COMMUNITY DEVELOPMENT AGENCY

JUNE 30, 2003

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INDEPENDENT AUDITOR'S REPORT

Agency Members
Community Development Agency
of the City of Lemon Grove
Lemon Grove, California

We have audited the accompanying component unit financial statements of the Community Development Agency of the City of Lemon Grove, as of June 30, 2003, and for the year then ended, as listed in the foregoing table of contents. These component unit financial statements are the responsibility of the Agency's management. Our responsibility is to express an opinion on these financial statements based on our audit.

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

In our opinion, such component unit financial statements present fairly, in all material respect, the financial position of the Community Development Agency of the City of Lemon Grove as of June 30, 2003, and the results of its operations for the year then ended in conformity with generally accepted accounting principles.

In accordance with *Government Auditing Standards*, we have also issued a report dated December 22, 2003, on our consideration of the Community Development Agency of the City of Lemon Grove's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants.

December 22, 2003



CITY OF LEMON GROVE - COMMUNITY DEVELOPMENT AGENCY
 COMBINED BALANCE SHEET
 ALL FUND TYPES AND ACCOUNT GROUPS
 June 30, 2003
 (With Comparative Totals For June 30, 2002)

	GOVERNMENTAL FUND TYPES		
	Special Revenue	Debt Service	Capital Projects
ASSETS			
Cash and investments	\$ 799,832	\$ 273,892	\$ 528,353
Cash with fiscal agent	-	697,221	-
Taxes receivable	9,466	38,213	-
Interest receivable	-	-	7,151
Due from other funds	178,599	-	-
Amount available in debt service	-	-	-
Amount to be provided for retirement of general long-term debt	-	-	-
	-	-	-
TOTAL ASSETS	\$ 987,897	\$ 1,009,326	\$ 535,504
LIABILITIES AND FUND EQUITY			
LIABILITIES			
Accounts payable	\$ -	\$ -	\$ 163
Deferred revenue	4,086	16,343	-
Due to other funds	-	178,599	-
Loans payable	-	-	-
Bonds payable	-	-	-
	-	-	-
Total Liabilities	4,086	194,942	163
FUND EQUITY			
Reserved under requirements of debt service	-	690,248	-
Designated for projects and programs	983,811	-	535,341
Designated for debt service	-	124,136	-
	-	124,136	-
Total Fund Equity	983,811	814,384	535,341
TOTAL LIABILITIES AND FUND EQUITY	\$ 987,897	\$ 1,009,326	\$ 535,504

See accompanying accountant's report and notes to financial statements

CITY OF LEMON GROVE - COMMUNITY DEVELOPMENT AGENCY
 COMBINED BALANCE SHEET
 ALL FUND TYPES AND ACCOUNT GROUPS
 June 30, 2003
 (With Comparative Totals For June 30, 2002)

ACCOUNT GROUP	TOTALS (Memorandum Only)	
General Long-Term Debt	<u>June 30, 2003</u>	<u>June 30, 2002</u>
\$ -	\$ 1,602,077	\$ 1,564,067
-	697,221	700,265
-	47,679	50,943
-	7,151	10,606
-	178,599	178,599
814,384	814,384	846,351
13,120,958	13,120,958	13,601,463
\$ 13,935,342	\$ 16,468,069	\$ 16,952,294
\$ -	\$ 163	\$ 2,130
-	20,429	19,922
-	178,599	178,599
4,675,342	4,675,342	5,027,814
9,260,000	9,260,000	9,420,000
13,935,342	14,134,533	14,648,465
-	690,248	690,248
-	1,519,152	1,457,478
-	124,136	156,103
-	2,333,536	2,303,829
\$ 13,935,342	\$ 16,468,069	\$ 16,952,294

See accompanying accountant's report and notes to financial statements

CITY OF LEMON GROVE COMMUNITY DEVELOPMENT AGENCY
STATEMENT OF REVENUE, EXPENDITURES AND CHANGES IN FUND BALANCE
ALL FUND TYPES AND ACCOUNT GROUPS
For the Fiscal Year Ended June 30, 2003
(With Comparative Totals For the Fiscal Year Ended June 30, 2002)

GOVERNMENTAL FUND TYPES

	<u>Special Revenue</u>	<u>Debt Service</u>	<u>Capital Projects</u>
REVENUES:			
Tax increment	\$ 291,910	\$ 1,167,642	\$ -
Interest income	18,198	13,714	5,757
Other revenues	13,815	-	-
Total Revenues	<u>323,923</u>	<u>1,181,356</u>	<u>5,757</u>
EXPENDITURES:			
Administration	23,828	11,391	85,649
Professional services	4,175	-	19,407
Education fund allocation	-	83,000	-
Education augment fund	-	41,215	-
Housing programs	4,714	-	-
School district allocation	30,443	121,774	-
Economic development services	-	-	3,063
Central Business District Development	-	-	58,181
Interest Expense	-	662,018	-
Principal repayment	-	794,425	-
Total Expenditures	<u>63,160</u>	<u>1,713,823</u>	<u>166,300</u>
EXCESS (DEFICIT) OF REVENUES OVER EXPENDITURES	<u>260,763</u>	<u>(532,467)</u>	<u>(160,543)</u>
OTHER FINANCING SOURCES (USES):			
Loans from the City of Lemon Grove	-	-	461,953
Transfers in	-	500,500	-
Transfers out	(155,500)	-	(345,000)
Total Other Financing Sources	<u>(155,500)</u>	<u>500,500</u>	<u>116,953</u>
EXCESS OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES	105,263	(31,967)	(43,590)
FUND BALANCE - Beginning of year	<u>878,548</u>	<u>846,351</u>	<u>578,931</u>
FUND BALANCE - End of year	<u>\$ 983,811</u>	<u>\$ 814,384</u>	<u>\$ 535,341</u>

See accompanying accountant's report and notes to financial statements

CITY OF LEMON GROVE COMMUNITY DEVELOPMENT AGENCY
 STATEMENT OF REVENUE, EXPENDITURES AND CHANGES IN FUND BALANCE
 ALL FUND TYPES AND ACCOUNT GROUPS
 For the Fiscal Year Ended June 30, 2003
 (With Comparative Totals For the Fiscal Year Ended June 30, 2002)

Totals
(Memorandum Only)

<u>2003</u>	<u>2002</u>
\$ 1,459,552	\$ 1,288,010
37,669	62,741
13,815	1,550
<u>1,511,036</u>	<u>1,352,301</u>
120,868	118,896
23,582	21,193
83,000	83,000
41,215	
4,714	6,186
152,217	134,314
3,063	26,902
58,181	425,674
662,018	701,018
794,425	677,600
<u>1,943,283</u>	<u>2,194,783</u>
<u>(432,247)</u>	<u>(842,483)</u>
461,953	842,600
500,500	304,100
<u>(500,500)</u>	<u>(304,100)</u>
<u>461,953</u>	<u>842,600</u>
29,706	117
<u>2,303,830</u>	<u>2,303,713</u>
<u>\$ 2,333,536</u>	<u>\$ 2,303,830</u>

See accompanying accountant's report and notes to financial statements

CITY OF LEMON GROVE – COMMUNITY DEVELOPMENT AGENCY

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

1. REPORTING ENTITY AND SIGNIFICANT ACCOUNTING POLICIES

a. Reporting Entity

The reporting entity ‘City of Lemon Grove Community Development Agency’ includes the accounts of the City of Lemon Grove (CDA) and certain funds of the Lemon Grove Financing Authority (LGFA) pertaining to the CDA debt issuances.

The Community Development Agency was activated in May of 1986 pursuant to section 33101 of the California Health and Safety Code. The purpose of the CDA is to eliminate deteriorating conditions and conserve, rehabilitate and revitalize project areas in accordance with the community development plan. The Agency is designed to encourage cooperation and participation of residents, business persons, community organizations and public agencies in the revitalization of the area. The CDA has established a project area composed of the northern portion of the City of Lemon Grove, properties adjacent to the central and southerly portion of Lemon Grove Avenue, and a small section of parcels in the southeast quadrant of the City. Since the primary purpose of the Redevelopment Agency is to promote the revitalization and development of the commercial and industrial areas of the City, the project area includes all of these areas and little if any residential areas.

The Lemon Grove Financing Authority is a joint power authority, organized pursuant to a Joint Exercise of Powers Agreement, dated as of May 1, 1992 (the ‘Joint Powers Agreement’) by and between its members, the Lemon Grove Community Development Agency and the City of Lemon Grove. The Joint Powers Agreement was entered into pursuant to the provisions of the California Government Code. The Authority is a separate entity constituting a public instrumentality of the State of California and was formed for the public purpose of assisting in financing and refinancing public capital improvements for a member through the purchase by the Authority of bonds pursuant to bond purchase agreements, and/or the loan of funds to a member. The Authority is governed by a board consisting of the members of the Agency Board. Separate financial statements for LGFA are not issued and therefore, each member includes in its financial statements the accounts and transactions pertaining to its debt issuances through the Authority.

See accompanying independent auditors’ report.

CITY OF LEMON GROVE – COMMUNITY DEVELOPMENT AGENCY

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

1. REPORTING ENTITY AND SIGNIFICANT ACCOUNTING POLICIES

a. Reporting Entity:

The criteria used in determining the scope of the reporting entity are based on the provisions of GASB Statement No. 14. The city of Lemon Grove (City) is the primary governmental unit. The CDA is a component unit of the City and the CFA is a component unit of the City. Component units are those entities which are financially accountable to the primary government either because the primary unit appoints a voting majority of the component unit Board, or because the component unit will provide financial benefit or impose a financial burden on the primary government. The specific criteria used in determining that the CDA and CFA component units of the City are that the members of the City Council are the same as the members of the CDA and CFA Boards of Directors.

b. Description of Funds and Account Groups:

The accounts of the Lemon Grove Community Development Agency (the "Agency") are organized on the basis of funds and account groups, each of which is considered a separate accounting entity with a self balancing set of accounts. The funds and account groups used in the accompanying financial statements and described below are those specified for governmental units in Statement No. 1 of the National Council on Governmental Accounting, as adopted by the Governmental Accounting Standards Board.

Special Revenue Funds

The Agency is required to set aside 20% of tax increment revenues for low and moderate income housing. Under provisions of the California Health and Safety Code, such funds can be accounted for as either Capital Project Funds or Special Revenue Funds. The Agency uses the housing funds to provide housing subsidies to low-income households and appropriately uses a special revenue fund for financial reporting purposes.

Debt Service Funds

Debt Service Funds are established to account for tax increment revenues, bond proceeds required to be set aside for future debt service and related interest income. The funds are used to repay principal and interest on indebtedness of the Agency. Under provisions of the Health and Safety Code such funds are referred to as "Special Funds".

See accompanying accountants' report

CITY OF LEMON GROVE – COMMUNITY DEVELOPMENT AGENCY

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

1. REPORTING ENTITY AND SIGNIFICANT ACCOUNTING POLICIES (Continued):

b. Description of Funds and Account Groups (Continued):

Capital Project Funds

Capital Project Funds are established to account for loans and advances from the City of Lemon Grove, bond proceeds, interest income on invested funds and certain miscellaneous income. The funds are expended primarily for administrative expenses and redevelopment project costs. Under provisions of the Health and Safety Code such funds are referred to a "Redevelopment Funds".

Long-Term Debt Group of Accounts

The Long-Term Debt Group of Accounts is used to account for long-term loans and advances from the City and bonds payable.

c. Basis of Accounting:

The Special Revenue, Debt Service and Capital Project Funds are accounted for using the modified accrual basis of accounting. Revenues are recognized when they become measurable and available to finance expenditures of the current period. Accrued revenue includes earnings on investments. Expenditures are recorded when the related liability is incurred.

d. Measurement Focus:

All Governmental funds are accounted for on a spending or "financial flow" measurement focus. This means that generally only current assets and current liabilities are included on their balance sheets, with the exception that the non-current portion of long-term receivables due to Governmental funds are reported on their balance sheets, offset by fund balance reserve accounts. Statement of revenues, expenditures and changes in fund balances for governmental funds generally present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) in net current assets.

e. Claims and Judgments:

When it is probable that a claim liability has been incurred at year-end, and the amount of the loss can be reasonably estimated, the Agency records the estimated loss, net of any insurance coverage under its self-insurance program. At June 30, 2003, in the opinion of Management, the Agency had no material claims which would require loss provision in the financial statements. Small dollar claims and judgements are recorded as expenditures when paid.

See accompanying accountants' report

CITY OF LEMON GROVE – COMMUNITY DEVELOPMENT AGENCY

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

1. REPORTING ENTITY AND SIGNIFICANT ACCOUNTING POLICIES (Continued):

f. Budgetary Reporting

The budgets of the Agency are primarily “long-term” budgets which emphasize major programs and capital outlay plans extending over a number of years. Because of the long-term nature of projects, “annual” budget comparisons are not considered meaningful, and accordingly, no budgetary information is included in the accompanying financial statements except for the special revenue fund.

g. Total Columns:

Total columns are captioned “Memorandum Only” to indicate that they are presented only to facilitate financial analysis. Data in these columns do not present consolidated financial information. Inter-fund elimination has not been made in the aggregation of this data.

2. TAX INCREMENT FINANCING:

The Agency’s primary source of revenue, other than the sale of bonds and advances from the City will come from property taxes, referred to as “tax increment revenue”. Property taxes allocated to the Agency will be computed in the following manner:

- a. The assessed valuation of all property within the project area is determined on the date of adoption of the Redevelopment Plan.
- b. Property taxes related to the incremental increase in assessed values after the adoption of the Redevelopment Plan are allocated to the Agency; all taxes on the “frozen” assessed valuation of the property are allocated to the City and other districts.

The Agency has no power to levy and collect taxes, and any legislative property tax de-emphasis might necessarily reduce the amount of tax revenues that would otherwise be available to pay the principal of, and interest on bonds or loans from the City. Broadened property tax exemptions could have a similar effect. Conversely, any increase in the tax rate or assessed valuation, or any reduction or elimination of present exemptions would necessarily increase the amount of tax revenues that would be available to pay principal and interest on bonds or loans from the City.

3. EQUITY IN POOLED CASH AND INVESTMENTS:

The Agency maintains a cash investment pool that is available for use by all funds. Each fund type’s portion of this pool is displayed on the combined balance sheet as “cash and investments”. The investment pools used by the Agency are equivalent to demand accounts and are therefore considered cash equivalents.

See accompanying accountants’ report.

CITY OF LEMON GROVE – COMMUNITY DEVELOPMENT AGENCY

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

3. EQUITY IN POOLED AND CASH INVESTMENTS (Continued):

Deposits

At year-end, the carrying amount of the deposits with financial institutions and the bank balance was \$1,300. The bank balance was covered by federal depository insurance.

Authority for Deposits and Investments

The Agency's investment policy and state statutes authorized the Agency to invest in obligations of the U.S. Treasury, its agencies and instrumentalities, repurchase agreements, certificates of deposit with national and state licensed or chartered banks or federal or state savings and loan associations, money market and mutual funds whose portfolios consist of one or more of the foregoing investments, and the State and County Treasurer's investment pools.

State statutes require that all deposits be insured or collateralized. Depositories holding public funds on deposit are required to maintain collateral in the form of a pool of securities with the agent of the depository having a market value of at least 10 to 50 percent in excess of the total amount of all public funds on deposit.

The Agency's investments are categorized below in accordance with GASB Statement #3 to give an indication of the level of risk assumed by the entity at year-end. Category 1 includes investments that are insured or collateralized with securities held by the Agency or its agent in the Agency name. Category 2 are securities held by the counterparty's trust department or agent in the Agency name. Category 3 includes uninsured and unregistered investments for which the securities are held by the financial institutions, broker, dealer or its agent but not in the Agency name.

	<u>Category</u>			<u>Total</u>
	<u>1</u>	<u>2</u>	<u>3</u>	
U.S. Treasury Instruments	\$ -	\$ 697,221	\$ -	\$ 697,221
Total	-	697,221	-	697,221
Uncategorized investments:				
Local Agency Investment Fund				1,600,777
Total Investments	\$ -	\$ 697,221	\$ -	\$ 2,297,998

Investments are carried at cost which approximates fair value.

See accompanying accountants' report.

CITY OF LEMON GROVE – COMMUNITY DEVELOPMENT AGENCY

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

3. EQUITY IN POOLED CASH AND INVESTMENTS (Continued):

Authority for Deposits and Investments (Continued):

A reconciliation of the carrying value of deposits and investments reported above to the combined balance sheet is as follows:

Deposits	\$	1,300
Investments		<u>2,297,998</u>
	\$	<u>2,299,298</u>
Per Combined balance sheet:		
Cash and investments	\$	1,600,077
Cash with Fiscal Agent		<u>697,221</u>
	\$	<u>2,297,298</u>

Collateral for Deposits

Under provisions of the California Government Code, California banks and savings and loan associations are required to secure an Agency's deposits by pledging government securities with a value equal to 100% of the Agency's deposits. California law also allows financial institutions to secure Agency deposits by pledging first trust deed mortgage notes having a value of 150% of an Agency's total deposits.

The collateral for certificates of deposit is generally held in safekeeping by the Federal Home Loan Bank in San Francisco as the third-party trustee. The securities are physically held in an undivided pool for all California public agency depositors. The State Public Administrative office for public agencies and the Federal Home Loan Bank maintain detailed records of the security pool which are coordinated and updated weekly.

Allocation of Interest Income Among Funds

Interest Income from pooled investments is allocated to those funds which are required by law or administrative action to receive interest. Interest is allocated based on the weighted average cash balances in each fund receiving interest.

See accompanying accountant's report

CITY OF LEMON GROVE – COMMUNITY DEVELOPMENT AGENCY

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

4. LONG-TERM DEBT:

The following is a summary of long-term debt transactions for the fiscal year ended June 30, 2003:

	<u>Balance</u> <u>June 30, 2002</u>	<u>Additions</u>	<u>Payments</u>	<u>Balance</u> <u>June 30, 2003</u>
Loan Payable – City of Lemon Grove	\$ 4,847,814	\$ 461,953	\$ 634,425	\$ 4,675,342
Tax Allocation Refunding Bonds	<u>9,420,000</u>	<u>-</u>	<u>160,000</u>	<u>9,260,000</u>
Total Long-term Debt	<u>\$14,267,814</u>	<u>\$ 461,953</u>	<u>\$ 794,425</u>	<u>\$13,935,342</u>

The loan payable to the City of Lemon Grove has no stated interest rate. Interest expense is computed monthly using the rate currently being paid by the Local Agency Investment Fund. This resulted in an average rate of 2.68 % for the year resulting in a total interest expense of \$130,000. This loan will be repaid based on a schedule to be agreed upon by the City and Agency.

In May 1998 the Agency issued \$9,420,000 in tax allocation bonds with interest rates varying from 5.00% to 5.75% to advance refund \$7,895,000 of outstanding Series 1992 Lemon Grove Redevelopment Project Tax Allocation Bonds with interest rates ranging from 5.00% to 6.90%. The refunding bonds were also issued to retire Disposition and Developer Agreements with Coral Ford and Land Grant Development Company. The net proceeds (after original issue discount of \$180,805 and underwriter fees and other issue costs of \$198,402) were deposited into an escrow fund. Of the proceeds \$672,338 was set aside to immediately retire the Disposition and Development Agreements. Pursuant to the escrow agreement \$8,307,194 was deposited into the Lemon Grove Community Development Agency 1998 Escrow Fund and invested in direct obligations of the United States such that the principal amount of the securities, together with the scheduled interest thereon, is sufficient to assure that the funds available in the escrow fund will be sufficient to pay when due the scheduled payments of principal and interest on the refunded bonds through August 1, 2002 and to fully redeem all outstanding refunded bonds on August 1, 2002. As a result the Series 1992 Lemon Grove Redevelopment Project Tax Allocation Bonds are considered defeased and the liability for those bonds and the Disposition and Developer Agreement has been removed from the general long-term debt group of accounts.

See accompanying accountants' report.

CITY OF LEMON GROVE – COMMUNITY DEVELOPMENT AGENCY

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

4. LONG-TERM DEBT (Continued):

The Agency advance refunded the 1992 Series bonds to take advantage of lower current interest rates, stretch the debt service obligations on its' outstanding debt and to retire the Disposition and Developer Agreements with Coral Ford and Land Grant Development Company. The Agency increased its' total debt service payments by \$5,082,363 over 30 years but has received an economic gain (difference between the present values debt service payments on the old debt and the new debt) of approximately \$140,500.

The annual requirements to amortize the long-term debt outstanding as of June 30, 2003, including interest payments to maturity, are as follows:

<u>Year</u>	<u>Tax Allocation Bonds (1998 Refunding)</u>
2004	\$ 690,248
2005	686,623
2006	687,623
2007	688,123
2008	688,020
2009-2028	<u>14,319,184</u>
Total	17,759,821
Less amounts representing Interest	(8,499,821)
Plus amount due to City of Lemon Grove	<u>4,675,342</u>
Total Long-Term Debt	<u>\$ 13,935,342</u>

The debt service for tax allocation bonds will be made from tax increment revenues received by the Agency.

See accompanying accountants' report.

CITY OF LEMON GROVE – COMMUNITY DEVELOPMENT AGENCY

NOTES TO FINANCIAL STATEMENTS

June 30, 2003

5. DUE TO AND FROM OTHER FUNDS:

On September 2, 1992, the Governor of California signed an appropriations bill adopting the state budget. Under provisions of the bill all California redevelopment agencies are required to make a transfer of funds to California schools and community colleges. The amount of the transfer is equal to a percentage of the Agency's tax increment revenue. Accordingly, the Agency was required to transfer approximately \$236,546. The legislation provides that a portion of the funds to be transferred may be borrowed by an agency from its low and Moderate Income Housing Funds. This resulted in the following "Due To and Due From Other Funds" balances:

	<u>Due to Other Funds</u>	<u>Due From Other Funds</u>
Debt Service Fund	\$ 178,599	\$ -
Special Revenue Fund	<u>-</u>	<u>178,599</u>
Total	<u>\$ 178,599</u>	<u>\$ 178,599</u>

See accompanying accountants' report.

SUPPLEMENTAL INFORMATION

CITY OF LEMON GROVE - COMMUNITY DEVELOPMENT AGENCY
STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE - BUDGET AND ACTUAL
SPECIAL REVENUE FUND
For the Fiscal Year Ended
June 30, 2003

	<u>Budget</u>	<u>Actual</u>	Variance Favorable <u>(Unfavorable)</u>
REVENUES:			
Tax increment	\$ 224,500	\$ 291,910	\$ 67,410
Interest income	19,328	18,198	(1,130)
Other Revenue	-	13,815	13,815
Total Revenues	<u>243,828</u>	<u>323,923</u>	<u>80,095</u>
EXPENDITURES:			
Administration	23,000	23,828	(828)
Professional services	12,600	4,175	8,425
School district allocation	-	30,443	(30,443)
Neighborhood revitalization	30,000	-	30,000
Housing programs	10,000	4,714	5,286
Total Expenditures	<u>75,600</u>	<u>63,160</u>	<u>12,440</u>
EXCESS (DEFICIT) OF REVENUES OVER EXPENDITURES	<u>168,228</u>	<u>260,763</u>	<u>92,535</u>
OTHER FINANCING SOURCES:			
Transfers out	<u>(155,500)</u>	<u>(155,500)</u>	-
Total Other Financing Sources	<u>(155,500)</u>	<u>(155,500)</u>	-
EXCESS OF REVENUES AND OTHER FINANCING SOURCES OVER EXPENDITURES	12,728	105,263	92,535
FUND BALANCE - Beginning of year	<u>878,548</u>	<u>878,548</u>	-
FUND BALANCE - End of year	<u>\$ 891,276</u>	<u>\$ 983,811</u>	<u>\$ 92,535</u>

See accompanying accountant's report and notes to financial statements

BROWNELL & DUFFEY
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**REPORT ON COMPLIANCE AND ON INTERNAL CONTROL
OVER FINANCIAL REPORTING BASED ON AN AUDIT OF
COMPONENT UNIT FINANCIAL STATEMENTS PERFORMED IN
ACCORDANCE WITH GOVERNMENT AUDITING STANDARDS**

Board of Directors
Community Development Agency
of the City of Lemon Grove
Lemon Grove, California

We have audited the accompanying component unit financial statements of the Lemon Grove Community Development Agency, as of June 30, 2003, and have issued our report thereon December 22, 2003. We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

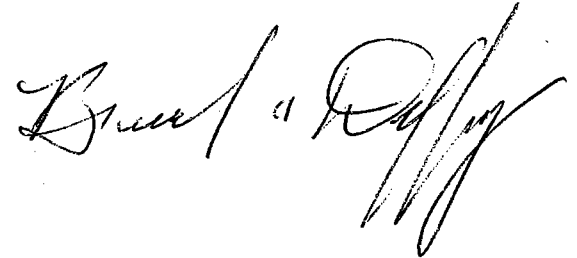
As part of obtaining reasonable assurance about whether the Lemon Grove Community Development Agency's component unit financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of component unit financial statements amounts. However, providing an opinion on compliance with those provisions was not an objective of our audits and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered Lemon Grove Community Development Agency's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the component unit financial statements and not to provide assurances on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the component unit financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving internal control over financial reporting and its operation that we consider to be material weakness.

This report is intended for the information of the Agency members, management and the State Controller. However, this report is a matter of public record and its distribution is not limited.

December 22, 2003

A handwritten signature in black ink, appearing to read "Bruce A. Poff". The signature is written in a cursive style with a large, stylized initial "B".

APPENDIX B

GENERAL INFORMATION REGARDING THE CITY

The following information relating to the City of Lemon Grove and San Diego County, California is supplied solely for purposes of information. Neither the City nor the County is obligated in any manner to pay principal of or interest on the Bonds or to cure any delinquency or default on the Bonds. The Bonds are payable solely from the Tax Revenues and other moneys as described in the Official Statement. The Project Area is located within the boundaries of the City.

Location and Background Information

The City of Lemon Grove (the "City") is located directly east of the City of San Diego adjacent to state Route 94. The City was settled in 1868 by its first known permanent resident, sheep rancher Robert Allison. From the 1860's to 1900 the predominant land use was sheep and poultry ranching and the cultivation of vegetable crops. In the early 1900's the community acquired its name when large citrus groves were planted and lemon and orange growing and shipping became the community's major industry.

By World War II, most of the citrus groves had disappeared and the suburbanization of the City had begun, but this trend did not peak until the end of the war. Between 1946 and 1960, building continued at a steady pace until most of the easily developable land had been consumed.

The City was first organized as a community and incorporated as a general law city in July 1977. The City's population was first estimated by the California Department of Finance in January 1978 and indicated that 19,700 persons resided in the community. In January 1991, the City's population was 24,310 and current estimates indicate that by the year 2010 the population will increase to 27,600.

Organization

The City is governed by a five-member City Council elected at large with four-year alternating terms. The Mayor is elected directly by the voters. Additionally, the positions of City Clerk, City Treasurer, City Manager and City Attorney are filled by appointments of the City Council. The City contracts with the San Diego County Sheriffs Office for law enforcement services.

Labor Relations

The City has 55 permanent employees. The City, pursuant to section 3500 of the California Government Code, provides for a meet-and-confer process with the City employees, individually or collectively, in order to negotiate on matters of wages, hours and working conditions. Matters involving merits, necessity or organization of any service or activity provided by law are excluded from this process.

The City has only one bargaining group comprised of its 20 firefighters. It has an Interim Memorandum of Understanding (MOU) with Lemon Grove Firefighters proposed Local 2728 of the International Association of Fire Fighters (IAFF). This MOU will become a final once the newly formed local bargaining unit becomes certified by the IAFF, its parent organization. The MOU has a term of two years from July 1, 2004.

Population

The City's population, as of January 2004, was 25,600, as reported by the California State Department of Finance. A summary of the City's population since incorporation is shown below.

CITY OF LEMON GROVE Population

<u>Year</u>	<u>Population</u>
1995	24,150
1996	24,050
1997	24,050
1998	24,450
1999	24,700
2000	24,918
2001	25,250
2002	25,400
2003	25,500
2004	25,600

(1) State Department of Finance estimate as of January 1 of each year.

Income

The following table is based on effective buying income as reported in the annual publication "Survey of Buying Power" published by Sales and Marketing Management Magazine. Effective buying income is defined as money income less personal tax and nontax payments. Money income is the aggregate of wages and salaries, net farm and nonfarm self employment income, interest, dividends, net rental and royalty income, Social Security and railroad retirement income, other retirement and disability income, public assistance income, unemployment compensation, Veterans Administration payments, alimony and child support, military family allotments, net winnings from gambling, and other periodic income. Deductions are then made for personal income taxes (federal, state and local), personal contributions for social insurance and taxes on owner-occupied nonbusiness real estate.

A yearly comparison of effective buying income and median household income totals for the County, the State and the nation is presented in the following table.

SAN DIEGO COUNTY, STATE OF CALIFORNIA AND UNITED STATES
Effective Buying Income
For Years 1998 through 2002
(in Thousands)

<u>Year</u>	<u>Area</u>	<u>Total Effective Buying Income (000's omitted)</u>	<u>Median Household Effective Buying Income</u>
1998	San Diego County	46,056,143	36,296
	California	551,999,317	37,091
	United States	4,621,491,738	35,377
1999	San Diego County	49,907,828	39,213
	California	590,376,663	39,492
	United States	4,877,786,658	37,233
2000	San Diego County	54,337,662	44,292
	California	652,190,282	44,464
	United States	5,230,824,904	39,129
2001	San Diego County	55,210,119	44,146
	California	650,521,407	43,532
	United States	5,303,481,498	38,365
2002	San Diego County	54,831,958	42,315
	California	647,879,427	42,484
	United States	5,340,682,818	38,035

Source: "Survey of Buying Power," Sales and Marketing Management.

Commerce

CITY OF LEMON GROVE
Taxable Sales Transactions

<u>Year</u>	<u>Retail Stores</u>	<u>Total All Outlets</u>
1997	227,125	263,655
1998	237,397	280,695
1999	269,056	316,733
2000	294,738	346,760
2001	317,341	367,924
2002	343,173	393,660
2003*	88,105	100,603

*Latest information available 2nd Quarter 2003
Source State Board of Equalization

CITY OF LEMON GROVE
Taxable Transactions
Calendar Years 1998-2002
(000's)

	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003*</u>
Apparel Stores	5,323	6,210	6,167	6,090	1,327
General Merchandise Stores	8,153	8,977	9,154	9,199	2,282
Food Stores	17,917	19,308	19,401	19,431	4,789
Eating and Drinking Group	20,357	21,304	22,584	23,595	5,965
Household Group	3,986	3,563	2,450	4,646	1,264
Building Material Group	73,660	76,015	85,362	86,895	20,890
Automotive Group	94,541	106,760	116,542	134,614	27,747
Service Stations	17,649	21,582	22,894	22,401	6,503
Other Retail Stores	27,470	31,019	32,787	36,302	9,466
 Retail Stores Total	 269,056	 294,738	 317,341	 343,173	 80,233
 All Other Outlets	 47,677	 52,022	 50,583	 50,487	 12,060

*Latest information available, 1st Quarter 2003
Source: California State Board of Equalization.

Employment

The service industries, notably hotels, restaurants and retail trade, account for a large proportion of the labor force. Small manufacturing firms, primarily electronics, and finance, insurance and real estate are the other major sectors of employment.

The civilian labor force, employment and unemployment for the City, the County and the State are outlined in the following table.

**CITY OF LEMON GROVE, SAN DIEGO COUNTY AND STATE OF CALIFORNIA
LABOR FORCE, EMPLOYMENT AND UNEMPLOYMENT
Yearly Average for Years 1999 through 2003**

<u>Year</u>	<u>Area</u>	<u>Civilian</u>			<u>Unemployment</u>
		<u>Labor Force</u>	<u>Employed</u>	<u>Unemployed</u>	<u>Rate</u>
1999	City of Lemon Grove	12,420	11,960	460	3.7%
	San Diego County	1,348,300	1,306,700	41,600	3.1%
	California	16,596,400	15,731,700	864,700	5.2%
	United States	139,380,000	133,501,000	5,879,000	4.2%
2000	City of Lemon Grove	12,810	12,350	460	3.6%
	San Diego County	1,391,700	1,349,400	41,700	3.0%
	California	17,090,800	16,245,600	845,200	4.9%
	United States	140,866,300	135,214,700	5,651,600	4.0%
2001	City of Lemon Grove	13,060	12,550	510	3.9%
	San Diego County	1,417,700	1,371,800	45,900	3.2%
	California	17,362,300	16,435,200	927,100	5.3%
	United States	142,122,200	135,042,900	6,779,300	4.8%
2002	City of Lemon Grove	13,460	12,770	690	5.1%
	San Diego County	1,458,000	1,395,600	62,400	4.3%
	California	17,661,000	16,574,000	1,087,000	6.2%
	United States	142,878,000	135,237,000	7,640,000	5.3%
2003	City of Lemon Grove	13,690	12,990	700	5.1%
	San Diego County	1,482,200	1,419,100	63,100	4.3%
	California	17,460,000	16,282,700	1,777,300	6.7%
	United States	146,510,000	137,736,000	8,774,000	6.0%

Source: Employment Development Department State of California Health and Welfare Agency.

Wage and salary employment by industry for San Diego County is shown below. Data are not compiled separately for the City.

SAN DIEGO COUNTY
Industry Employment & Labor Force
Annual Averages (In Thousands)

	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>
Agricultural	10.6	11.2	11.4	11.4	11.0	11.2
Natural Resources and Mining	.3	.3	.3	.3	.3	.3
Construction	60.2	67.0	69.7	75.1	76.4	79.6
Manufacturing	124.0	122.9	122.6	119.0	112.3	105.4
Durable Goods	93.6	92.4	92.2	89.3	84.7	79.0
Nondurable Goods	30.4	30.5	30.4	29.8	27.7	26.4
Service Providing	921.0	962.7	1001.2	1024.0	1041.7	1056.7
Wholesale Trade	34.7	36.8	39.1	41.5	41.3	41.3
Retail Trade	124.7	128.2	133.8	135.6	138.0	140.0
Transportation, Warehousing and Utilities	28.6	29.2	29.8	32.0	29.3	27.3
Information	34.3	36.2	39.2	38.8	37.7	37.1
Real Estate and Rental and Leasing	26.3	27.2	27.2	27.2	27.7	29.0
Finance and Insurance	39.7	43.3	44.0	44.9	47.3	51.5
Professional and Business Services	173.1	185.0	195.2	198.2	201.7	201.6
Educational and Health Services	107.1	112.2	115.3	116.0	119.7	122.0
Leisure and Hospitality	118.6	124.4	129.0	131.4	133.8	139.9
Other Services	39.5	40.9	42.2	44.9	45.6	47.2
Government	194.5	199.3	206.6	213.8	219.7	219.8
Federal Government	43.3	42.5	42.1	40.2	40.1	42.7
State and Local Government	151.2	156.8	164.6	173.6	179.6	177.2
TOTAL	1116.1	1164.1	1205.2	1229.8	1241.7	1253.2

(1) "Total" may not be precise due to independent rounding.

Source: State of California Employment Development Department Labor Market Information Division.

**SAN DIEGO COUNTY
Principal Employers**

Employer Name	Location	Industry
BF Goodrich	Chula Vista	Aircraft & Parts
County of San Diego	San Diego	Public Administration (Government)
Department of Defense	San Diego	Public Administration (Government)
Jack In The Box Inc	San Diego	Eating & Drinking Places
National Steel & Shipbuilding	San Diego	Ship Building and Repairing
Qualcomm Inc	San Diego	Telephone Communications
Science Applications Intl Corp	San Diego	Engineering & Architectural Services
Scripps Memorial Hospital	La Jolla	Hospitals
Sea World Amusement, Recreation Services	San Diego	Misc
Sempre Energy	San Diego	Combination Utility Services
Sharp Rees-Stealy Medical Group	San Diego	Hospitals
Sony Electronics Inc	San Diego	Radio, Television, & Computer Stores
University of California, San Diego	La Jolla	Colleges & Universities
University of San Diego	San Diego	Colleges & Universities
US Post Office	San Diego	U.S. Postal Service

This list of major employers was developed using the 2002 America's Labor Market Information System (ALMIS) Employer Database from infoUSA and is sorted in alphabetical order by company name. The industry shown is based upon the Standard Industrial Classification

Source: State of California Employment Development Department Labor Market Information Division.

Construction Activity

The following is a summary of the valuation of building permits issued in the City

**CITY OF LEMON GROVE
Building Permit Valuations And Permits Issued
For Years 1998 through 2003 (Dollar Volume in \$1,000s)**

	1998	1999	2000	2001	2002	2003
<u>Residential</u>						
Single Family	\$682.8	\$791.9	\$1,306.0	\$746.0	\$2,929.7	\$1,475.6
Multifamily	151.6	0.0	0.0	0.0	0.0	0.0
Alterations/Additions	<u>626.7</u>	<u>1,541.3</u>	<u>1,812.9</u>	<u>1,485.6</u>	<u>2,117.5</u>	<u>2,720.6</u>
Total	\$1,461.0	\$2,333.2	\$3,118.9	\$2,231.6	\$5,047.2	\$4,196.2
<u>Non-Residential</u>						
New Commercial	\$1,565.3	\$0.0	\$0.0	\$325.0	\$0.0	\$557.3
New Industry	0.0	0.0	0.0	0.0	0.0	0.0
Other ⁽¹⁾	207.9	238.3	512.7	327.1	196.8	270.4
Alterations/Additions	<u>988.0</u>	<u>843.7</u>	<u>306.4</u>	<u>1,592.5</u>	<u>732.9</u>	<u>479.2</u>
Total	\$2,761.2	\$1,081.9	\$819.2	\$2,244.6	\$929.7	\$1,306.8
<u>Total All Industry</u>	<u>\$4,222.2</u>	<u>\$3,415.1</u>	<u>\$3,938.1</u>	<u>\$4,476.2</u>	<u>\$5,976.9</u>	<u>\$5,503.0</u>
<u>Units</u>						
Single Family ⁽²⁾	6	5	11	10	19	12
Multiple Family ⁽²⁾	<u>2</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
Total ⁽²⁾	8	5	11	10	19	12

⁽¹⁾ Includes churches and religious buildings, hospitals and institutional buildings, schools and educational buildings, residential garages, public works and utilities buildings and non-residential alterations and additions.

⁽²⁾ Not in dollars.

Source: Construction Industry Research Board.

Utilities

Water is supplied to the City by the Helix Water District. Electricity and natural gas are provided by San Diego Gas & Electric. Telephone service is provided by SBC. Sewer collection service is provided by the Lemon Grove Sanitation District and sewage treatment is provided by the Metropolitan Sewer Agency.

Transportation

The City has freeway access to State Route 94 which runs east to west along the northern boundary of the City. Caltrans is in the process of improving State Route 125 which runs north to south along the eastern boundary of the City.

The City receives bus service through the San Diego County Transit System and the Metropolitan Transit Development Board. Additionally, the City participates with the Metropolitan Transit Development Board for light rail service running through the City into downtown San Diego. The City has two stations.

Education

Primary education in the City is provided by the Lemon Grove School District. Grossmont Union High School District provides secondary and adult education. Within the city limits there are five public elementary schools and two middle schools. There are no high school campuses located within the City limits.

Lower division college studies are available from the Grossmont-Cuyamaca Community College District. Located within the County are five four-year institutions of higher education; the University of California at San Diego, San Diego State University, United States International University, University of San Diego and Point Loma Nazarene College.

The University of California at San Diego offers both graduate and undergraduate instruction. The campus serves as headquarters for the University's Institute of Marine Resources and includes the Scripps Institution on Oceanography. There is a School of Medicine in the educational complex.

San Diego State University offers bachelor's degrees in 54 fields and master's degrees in 42. There are doctorate programs in chemistry, genetics and ecology at this campus. The University of San Diego offers the master's degree in numerous fields and awards the Juris Doctor degree at its Law School. Point Loma College offers both undergraduate and graduate studies.

APPENDIX C

SUMMARY OF CERTAIN PROVISIONS OF THE INDENTURE

The following is a summary of certain provisions of the Indenture of Trust and does not purport to be complete. Copies of the Indenture are available from the Agency upon request. All capitalized terms used herein and not otherwise defined shall have the same meaning as used in the Indenture.

Definitions.

"Additional Revenues" means, as of the date of calculation, the amount of Tax Revenues which, as shown in the report of a Redevelopment Consultant, are estimated to be receivable by the Agency within the Fiscal Year following the Fiscal Year in which such calculation is made as a result of increase in the assessed valuation of taxable property in the Project Area due to (a) the application of a growth factor equal to the lesser of 2.00% or the Consumer Price Index adjustment applicable in the then current Fiscal Year and (b) completion of construction which is not yet reflected on the tax rolls, or due to transfers of ownership or any other interest in real property which has been recorded but which is not yet reflected in the tax roll.

"Agency" means the Lemon Grove Community Development Agency.

"Alternate Reserve Account Security" means one or more letters of credit, surety bonds, bond insurance policies, or other form of guaranty from a financial institution for the benefit of the Trustee, in substitution for or in place of all or any portion of the Reserve Requirement, which shall be approved by the Bond Insurer.

"Annual Debt Service" means, for any Bond Year, the principal and interest payable on the Outstanding Bonds in such Bond Year.

"Bond" or *"Bonds"* means the "Lemon Grove Community Development Agency, Lemon Grove Redevelopment Project Area, 2004 Tax Allocation Bonds," authorized by the Indenture.

"Bond Counsel" means an attorney or firm of attorneys acceptable to the Agency of nationally recognized standing in matters pertaining to the federal tax exemption of interest on bonds issued by states and political subdivisions, and duly admitted to practice law before the highest court of any state of the United States of America or the District of Columbia.

"Bond Insurer" or *"Insurer"* means Radian Asset Assurance Inc., a corporation organized under the laws of the State of New York, or any successor hereto.

"Bondowner" or *"Owner of Bonds,"* or any similar term, means any person who shall be the registered owner or his duly authorized attorney, trustee, or representative of any Outstanding Bond.

"Bond Year" means the twelve (12) month period commencing on August 2 of each year, provided that the first Bond Year shall extend from the Delivery Date to August 1, 2005.

"Business Day" means a day of the year other than (i) a Saturday, Sunday, legal holiday or day on which banking institutions in the city in which the Principal Office of the Trustee is located are required or authorized to remain closed, or (ii) a day on which the New York Stock Exchange is closed.

"Certificate" or *"Certificate of the Agency"* means a certificate signed by the Chair or Executive Director of the Agency or their respective deputies.

"Chair" means the chair of the Agency appointed pursuant to Section 33113 of the Health and Safety Code of the State of California, or other duly appointed officer of the Agency authorized by the Agency by resolution or bylaw to perform the functions of the chair in the event of the chair's absence or disqualification.

"City" means the City of Lemon Grove, California.

"Code" means the Internal Revenue Code of 1986, as amended, and any regulations, rulings, judicial decisions, and notices, announcements, and other releases of the United States Treasury Department or Internal Revenue Service interpreting and construing it, or any applicable regulations adopted under the Internal Revenue Code of 1954, as amended.

"Costs of Issuance" means the costs and expenses incurred in connection with the issuance and sale of the Bonds including the initial fees and expenses of the Trustee, the premium for the Financial Guaranty Insurance Policy, legal fees and expenses of the Trustee and the Agency, costs of printing the Bonds and Official Statement, fees of financial consultants and other fees and expenses set forth in a Certificate of the Agency.

"County" means the County of San Diego, California.

"Debt Service Fund" means the Fund by that name established and held by the Trustee pursuant to the Indenture (with special trust accounts contained therein known as the "Interest Account," the "Principal Account," the "Costs of Issuance Account," the "Reserve Account" and the "Surplus Account").

"Delivery Date" means the date the Bonds are delivered to the original purchaser thereof.

"Depository" means (a) initially, DTC, and (b) any other Securities Depository acting as Depository pursuant to the Indenture.

"DTC" means The Depository Trust Company, New York, New York, and its successors and assigns.

"Event of Default" means any of the events described in the Indenture.

"Escrowed Bonds" means the bonds the proceeds of which are on deposit in the Escrowed Proceeds Fund.

"Escrowed Proceeds Fund" means the fund by that name established pursuant to the Indenture.

"Excess Investment Earnings Fund" means the fund by that name established pursuant to the Indenture (and in which there shall be established two separate sub-accounts designated the "Rebate Account" and the "Alternative Penalty Account").

"Federal Securities" means 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 principal of and interest on which are unconditionally guaranteed by the United States of America.

"Financial Guaranty Insurance Policy" shall mean the financial guaranty insurance policy issued by Bond Insurer insuring the payment when due of the principal of and interest on the Bonds as provided therein.

"Fiscal Year" means any twelve (12) month period beginning on July 1st and ending on the next following June 30th.

"Housing Fund" means the Low and Moderate Income Housing Fund established pursuant to Section 33334.2 and 33334.3 of the Law.

"Indenture" means the Indenture of Trust between the Agency and the Trustee, as originally adopted or as it may be amended or supplemented by any Supplemental Indenture entered into pursuant to the provisions hereof.

“Independent Financial Consultant,” “Independent Certified Public Accountant” or “Independent Redevelopment Consultant” means any individual or firm engaged in the profession involved, appointed by the Agency, and who, or each of whom, has a favorable reputation in the field in which his/her opinion or certificate will be given, and:

- (1) Is in fact independent and not under domination of the Agency;
- (2) Does not have any substantial interest, direct or indirect, with the Agency; and
- (3) Is not connected with the Agency as an officer or employee of the Agency, but who may be regularly retained to make reports to the Agency.

“Insurance Trustee” shall mean The Bank of New York. *“Interest Payment Date”* means February 1 and August 1 of each year commencing February 1, 2005.

“Law” means the Community Redevelopment Law of the State (the “State”), constitution Part 1 of Division 24 of the Health and Safety Code of the State of California (commencing with Section 33000), as amended, and all laws amendatory thereof or supplemental thereto.

“LMI Tax Revenue” means, for each Fiscal Year, all taxes allocated to the Agency with respect to the Project following the Closing Date which are required to be deposited into the Housing Fund.

“LMI Tax Revenue Bond Payment Account” means the separate account established by the Agency within the Housing Fund.

“LMI Tax Revenue Portion of the Bonds” means a principal amount of the Bonds equal to \$2,540,000.

“Maximum Annual Debt Service” means the largest of the sums obtained for any Bond Year after the computation is made, by totaling the following for each such Bond Year:

- (1) The principal amount of all serial Bonds and serial Parity Bonds, if any, and the amount of minimum sinking account payments payable in such Bond Year; and
- (2) The interest which would be due during such Bond Year on the aggregate principal amount of Bonds and Parity Bonds which would be outstanding in such Bond Year if the Bonds and Parity Bonds outstanding on the date of such computation were to mature or be redeemed in accordance with the maturity schedules for the serial Bonds and serial Parity Bonds. At the time and for the purpose of making such computation, the amount of term Bonds and term Parity Bonds already retired in advance of the above-mentioned schedules shall be deducted pro rata from the remaining amounts thereon.

“1998 Bonds” means the Lemon Grove Community Development Agency Tax Allocation Bonds (1998 Refunding).

“1998 Bonds Indenture” means the Indenture of Trust dated as of May 1, 1998 pursuant to which the 1998 Bonds were issued.

“Opinion of Counsel” means a written opinion of an attorney or firm of attorneys of favorable reputation in the field of municipal bond law. Any opinion of such counsel may be based upon, insofar as it is related to factual matters, information which is in the possession of the Agency as shown by a certificate or opinion of, or representation by, an officer or officers of the Agency, unless such counsel knows, or in the exercise of reasonable care should have known, that the certificate, opinion or representation with respect to the matters upon which his or her opinion may be based, as aforesaid, is erroneous.

“Outstanding,” when used as of any particular time with reference to Bonds, means, subject to the provisions of Article XI, all Bonds except:

- (1) Bonds theretofore cancelled by the Trustee or surrendered to the Trustee for cancellation;

(2) Bonds paid or deemed to have been paid pursuant to the Indenture; and

(3) Bonds in lieu of or in substitution for which other Bonds shall have been authorized, executed, issued and delivered by the Agency pursuant to the Indenture or any Supplemental Indenture.

"Parity Bonds" means any additional tax allocation bonds (including, without limitation, bonds, notes, interim certificates, debentures or other obligations) issued by the Agency as permitted by the Indenture payable out of Tax Revenues and ranking on a parity with the Bonds and, to the extent Outstanding, the 1998 Bonds.

"Pass-Through Agreements" means the agreements entered into on or prior to the date hereof pursuant to Section 33401 of the Health and Safety Code with the County of San Diego and Lemon Grove School District.

"Paying Agent" means any paying agent appointed by the Agency (or Trustee, as the case may be) pursuant to the Indenture.

"Permitted Investments" means to the extent permitted by applicable law:

(i) Certificates or interest-bearing notes or obligations of the United States, or those for which the full faith and credit of the United States are pledged for the payment of principal and interest.

(ii) Investments in any of the following obligations provided such obligations are backed by the full faith and credit of the United States (a) direct obligations or fully guaranteed certificates of beneficial interest of the Export-Import Bank of the United States, (b) debentures of the Federal Housing Administration, (c) guaranteed mortgage backed bonds of the Government National Mortgage Association, (d) certificates of beneficial interest of the Farmers Home Administration, (e) obligations of the Federal Financing Bank or (f) project notes and local authority bonds of the Department of Housing and Urban Development.

(iii) Investments in (a) senior obligations of the Federal Home Loan Bank System, (b) participation certificates or senior debt obligations of the Federal Home Loan Mortgage Corporation, (c) mortgage-backed securities and senior debt obligations (excluding stripped mortgage securities that are valued greater than par on the portion of unpaid principal) of the Federal National Mortgage Association or (d) senior debt obligations of the Student Loan Marketing Association.

(iv) Repurchase agreements with primary dealers and/or banks rated, at all times, AA and AA2 or better by Standard & Poor's Corporation and Moody's Investors Service, Inc., respectively, collateralized with the obligations described in (i) or (ii) above, held by a third party custodian, at the levels set forth below, which repurchase agreements have been approved by the Insurer.

(v) S.E.C. registered money market mutual funds conforming to Rule 2a-7 of the Investment Company Act of 1940 that invest primarily in direct obligations issued by the U.S. Treasury and repurchase agreements backed by those obligations, including funds for which the Trustee or an affiliate of the Trustee acts as an advisor, and rated in the highest category by Standard & Poor's Corporation and Moody's Investors Service, Inc.

(vi) Certificates of deposit of any bank (including the Trustee), trust company or savings and loan association whose short term obligations are rated, at all times, A-1 or better by Standard & Poor's Corporation and P-1 by Moody's Investors Service, Inc. provided that such certificates of deposit are fully secured by the obligations described in (i) or (ii) above, at the levels set forth below, the Trustee has a perfected first security interest in the obligations securing the certificates and the Trustee holds (or shall have the option to appoint a bank, trust company or savings and loan association as its agent to hold) the obligations securing the certificates.

(vii) Certificates of deposit of any bank (including the Trustee), trust company or savings and loan association which certificates are fully insured by the Federal Deposit Insurance Corporation.

(viii) Commercial paper rated, at all times, P-1 or better by Moody's Investors Service, Inc. and A-1+ by Standard & Poor's Corporation.

(ix) Obligations of, or obligations fully guaranteed by, any state of the United States of America or any political subdivision thereof which obligations, at all times, are rated by Standard & Poor's Corporation and Moody's Investors Service, Inc. in the highest rating categories (without regard to any refinement or graduation of rating category by numerical modifier or otherwise) and without regard to credit enhancement assigned by such rating agencies to obligations of that nature.

Collateral Levels for United States Government Securities:

Remaining Maturity

<u>Frequency of Valuation</u>	<u>1 Year or Less</u>	<u>5 Years or Less</u>	<u>10 Years or Less</u>	<u>15 Years or Less</u>	<u>30 Years or Less</u>
Daily	102	105	106	107	113
Weekly	103	110	111	113	118
Monthly	106	116	119	123	130
Quarterly	106	118	128	130	135

Further Requirements: (1) On each valuation date the market value of the collateral will be an amount equal to the requisite collateral percentage of the obligation (including unpaid accrued interest) that is being secured. (2) In the event the collateral level is below its collateral percentage on a valuation date, such percentage shall be restored within the following restoration periods. One business day for daily valuations, two business days for weekly valuations, and one month for monthly and quarterly valuations. The use of different restoration periods affect the requisite collateral percentage. (3) the Indenture must require the Trustee to terminate the repurchase agreement upon a failure to maintain the requisite collateral percentage after the restoration period and, if not paid by the counterparty in federal funds against transfer of the repo securities, liquidate the collateral.

"Principal Office or Principal Corporate Trust Office" means the corporate trust office of the Trustee located at 633 West Fifth Street, 24th Floor, Los Angeles, California, Attention: Corporate Trust Services, or such other or additional offices as may be designated in writing by the Trustee; provided, however, that for the purposes of payment, transfer or exchange of Bonds such term means c/o U.S. Bank National Association, 60 Livingston Avenue, St. Paul, Minnesota 55107, Attention: Corporate Trust, or at such other address as may be designated in writing by the Trustee.

"Rebate Regulations" means the final, proposed and temporary Treasury Regulations issued under Section 148(f) of the Code.

"Redemption Fund" shall have the meaning set forth in the Indenture.

"Redevelopment Agency" or "Agency" means the Lemon Grove Community Development Agency.

"Redevelopment Plan" means the Redevelopment Plan for the Lemon Grove Redevelopment Project Area, approved and adopted by the City Council of the City by Ordinance No. 136 on November 17, 1986, and includes any amendment thereof, hereafter or heretofore made pursuant to the Law.

"Redevelopment Project Area," "Redevelopment Project," or "Project Area" means the project area defined and described in the Redevelopment Plan as Lemon Grove Redevelopment Project Area.

"Regular Record Date" means the fifteenth day of the month preceding any Interest Payment Date whether or not such day is a Business Day.

"Report" means a document in writing signed by an Independent Financial Consultant and including:

(1) A statement that the person or firm making or giving such Report has read the pertinent provisions of the Indenture to which such Report relates;

(2) A brief statement as to the nature and scope of the examination or investigation upon which the Report is based; and

(3) A statement that, in the opinion of such person or firm, sufficient examination or investigation was made as is necessary to enable said consultant to express an informed opinion with respect to the subject matter referred to in the Report.

“Reserve Requirement” means, as of the date of computation of the Bonds, excluding the Escrowed Bonds (to the extent secured by the Escrowed Proceeds Fund), an amount equal to the least of (i) Maximum Annual Debt Service, (ii) 10% of the net Bond proceeds, or (iii) 125% of average Annual Debt Service on all Bonds. The computation shall be made with respect to all Bonds and Parity Bonds Outstanding at the time of such computation.

“Revenues” means the Tax Revenues together with all other moneys held by the Trustee in any Fund or Account (except the Excess Investment Earnings Fund) and the interest earnings thereon.

“Six-Month Period” means the period of time beginning on the Delivery Date and ending six months thereafter, and each six-month period thereafter until the latest maturity date of the Bond issue (and any obligations that refund the Bond issue).

“Standard & Poor’s” means Standard & Poor’s Ratings Group, New York, New York, and its successors and assigns.

“State” means the State of California.

“Supplemental Indenture” or *“supplemental indenture”* means any indenture then in full force and effect which has been duly entered into by the Agency under the Law, or any act supplementary hereto or amendatory thereof, at a meeting of the Agency duly convened and held, at which a quorum was present and acted thereon, amendatory of or supplemental to the Indenture; but only if and to the extent that such Supplemental Indenture is specifically authorized hereunder.

“Tax Certificate” means that certain Tax Certificate executed in connection with the issuance of the Bonds or any Parity Bonds.

“Tax Revenues” means that portion of taxes levied upon taxable property in the Project Area and received by the Agency on or after the date of issue of the Bonds, for the Project Area of the Agency pursuant to Article 6 of Chapter 6 of the Law and Section 16 of Article XVI of the Constitution of the State, excluding therefrom the portion of taxes which are attributable to a tax rate levied by a taxing agency for the purpose of producing revenues in an amount sufficient to make annual payments of principal of and interest on any bonded indebtedness approved by the voters of the taxing agency on or after January 1, 1989 for the acquisition or improvement of real property, which portion shall be allocated to, and when collected shall be paid into the fund of that taxing agency but, including that portion of such taxes otherwise required by Section 33334.2 of the Law to be deposited in the Low and Moderate Income Housing Fund, but only to the extent necessary to repay that portion of the Bonds and any Parity Bonds (to the extent that portion of Tax Revenues are pledged hereto) which were issued or which shall be issued to finance amounts deposited in the Low and Moderate Income Housing Fund for use pursuant to Section 33334.2 of the Law; but excluding all other amounts of such taxes (if any) (i) required to be deposited into the Low and Moderate Income Housing Fund of the Agency pursuant to Section 33334.2 of the Law and (ii) payable or required to be set aside by the Agency under the Pass-Through Agreements.

“Treasurer” or *“Treasurer of the Agency”* means the officer who is then performing the functions of Treasurer of the Agency.

“Trustee” means the trustee appointed by the Agency pursuant to the Indenture, its successors and assigns, and any other corporation or association which may at any time be substituted in its place, as provided in the Indenture.

“Trust Estate” shall have the meaning attributable to such term in the “Granting Clause First” herein.

Revenues and Funds

Source of Payment of Bonds. The Bonds and all payments required of the Agency hereunder are not general obligations of the Agency but are limited obligations as described in the Indenture. The Tax Revenues and all moneys held in the Special Fund or any of the Accounts thereunder and the Redemption Fund are hereby conveyed, pledged and assigned absolutely and as a first lien pledge as security for the equal and ratable benefit of the owners of the Bonds, excluding therefrom the Escrowed Bonds, and shall be used for no other purpose than payment of the principal of, premium (if any) and interest on the Bonds, except as may be otherwise expressly authorized in the Indenture.

Creation of Funds and Accounts. There is hereby continued a special trust fund to be held and maintained by the Treasurer, called the “Lemon Grove Redevelopment Project Area, Redevelopment Fund” (hereinafter sometimes called the “Redevelopment Fund”), the “Lemon Grove Redevelopment Project Area, Housing Fund” (the “Housing Fund”) and the “Lemon Grove Redevelopment Project Area Special Fund” (the “Special Fund”). There is hereby continued a special trust fund to be held and maintained by the Trustee, called the “Lemon Grove Redevelopment Project Area, Debt Service Fund” with special trust accounts contained therein known as the “Interest Account,” the “Principal Account,” the “Costs of Issuance Account,” the “Reserve Account” and the “Surplus Account,” and a special trust fund called the “Excess Investment Earnings Fund.” There is hereby established with the Trustee, a special trust fund known as the “Escrowed Proceeds Fund with a special trust account therein known as the “Escrowed Proceeds Capitalized Interest Account.” Notwithstanding any other provision of the Indenture, neither the Excess Investment Earnings Fund nor amounts credited or properly creditable thereto shall be deemed to be pledged to secure the Bonds. Article VI of the Indenture creates the Redemption Fund described therein.

So long as any of the Bonds, or any interest on them, remain unpaid, the Agency shall not have any beneficial right or interest in the Tax Revenues and Trust Estate except as provided in the Indenture and the moneys in the foregoing Funds and Accounts shall be used for no purposes other than those required or permitted by the Indenture and the Law and the foregoing Funds and Accounts on deposit with the Trustee shall be pledged to the payment of the Bonds.

Each Fund and Account (other than the Redevelopment Fund) shall be maintained by the Trustee as a separate and distinct trust fund or account to be held, managed, invested, disbursed and administered as provided in the Indenture. All moneys deposited in the Funds and Accounts shall be used solely for the purposes set forth in the Indenture. The Trustee shall keep and maintain adequate records pertaining to each Fund and Account and all disbursements therefrom (other than the Redevelopment Fund as to which the Agency will keep such records).

Special Fund. The Special Fund shall be held by the Agency in trust. Until such time as the amount on deposit in the Special Fund, including interest earnings thereon, together with available funds in the LMI Tax Revenue Bond Payment Account equals the aggregate amounts required to be transferred to the Trustee pursuant to the Indenture for such Bond Year, the Agency shall deposit all Tax Revenues, other than LMI Tax Revenue, received in any Bond Year into the Special Fund promptly upon receipt.

Until such time as the amount on deposit in the LMI Tax Revenue Bond Payment Account, including interest earnings thereon, together with available funds in the Special Fund equals the aggregate amounts required to be transferred to the Trustee pursuant to the Indenture for such Bond Year, the Agency shall deposit all LMI Tax Revenues received in any Bond Year into the LMI Tax Revenue Bond Payment Account promptly upon receipt. Notwithstanding the immediately preceding sentence, (1) the amount deposited into the LMI Tax Revenue Bond Payment Account each Bond Year shall not exceed (i) the corresponding debt service requirement for the Bond Year with respect to the LMI Tax Revenue Portion of the Bonds as shown on Exhibit B attached to the Indenture and (ii) any redemption permitted by the Indenture, and (2) from and after the date on which LMI Tax Revenue has been expended in an amount sufficient, on a present value basis based on the schedule of payments shown on Exhibit B to the Indenture as adjusted for any prepayments, to have fully paid the principal of and accrued interest on the LMI Tax Revenue Portion of the Bonds, no further LMI Tax Revenue shall be

deposited into the LMI Tax Revenue Bond Payment Account. LMI Tax Revenue received by the Agency and not deposited into the LMI Tax Revenue Bond Payment Account shall be deposited into the Agency's Low and Moderate Income Housing Fund.

On or before the sixth day immediately preceding any Interest Payment Date (or, in the event that a Surety Instrument has been substituted for amounts required to be on deposit in the Reserve Account, on or before the fifth day immediately preceding any Interest Payment Date), the Agency shall withdraw from the LMI Tax Revenue Bond Payment Account and the Special Fund and deposit with the Trustee the amount of money necessary to make the deposits required in the Indenture. Upon notice from the Trustee, the Agency shall withdraw from the LMI Tax Revenue Bond Payment Account and the Special Fund and deposit with the Trustee the amount of money necessary to make any deposit required by the Indenture. All Tax Revenues received by the Agency at any time during any Bond Year in excess of the amount required to be deposited into the LMI Tax Revenue Bond Payment Account and the Special Fund, respectively, during such Bond Year pursuant to the Indenture shall be released from the pledge and lien hereunder for the security of the Bonds and the Agency may apply such excess Tax Revenues for any lawful purpose of the Agency. Prior to the payment in full of the principal of, premium (if any) and interest on the Bonds and the payment in full of all other amounts payable hereunder and under any Parity Debt Instrument, the Agency shall not have any beneficial right or interest in the moneys on deposit in the Special Fund, except as may be provided in the Indenture and in any Parity Debt Instrument.

Transfer of Amounts to the Trustee; Allocation of Revenues. The Debt Service Fund shall be held by the Trustee in trust. The Trustee shall deposit moneys transferred by the Agency to the Trustee from the LMI Tax Revenue Bond Payment Account and the Special Fund into the following accounts in the amounts and order of priority as follows:

Interest Account. Deposits shall be made into the Interest Account so that the balance in the Interest Account at least five (5) days prior to each Interest Payment Date shall be equal to interest due and payable on the then outstanding Bonds on such Interest Payment Date. Moneys in the Interest Account shall be used solely for the payment of interest on the Bonds as interest becomes due, including accrued interest on any Bonds purchased or redeemed prior to maturity.

Principal Account. After the deposits have been made pursuant to paragraph above, deposits shall next be made into the Principal Account so that the balance in the Principal Account at least five (5) days prior to each August 1 is equal to the principal coming due on such date on the then outstanding serial Bonds or the amount of the minimum sinking account payments due on the term Bonds on such date. All monies in the Principal Account shall be used and withdrawn by the Trustee solely for the purpose of paying principal and minimum sinking account payments on the Bonds as they shall become due and payable.

Reserve Account. After deposits have been made pursuant to the Interest Account and the Principal Account above, deposits shall be made to the Reserve Account, if necessary, in order to cause the amount on deposit therein to equal the Reserve Requirement. Moneys in the Reserve Account shall be transferred to the Interest Account or the Principal Account to pay interest on and principal of the Bonds either (i) as it becomes due to the extent moneys on deposit are insufficient therefor or (ii) at the final maturity of the Bonds. Any portion of the Reserve Account which is in excess of the Reserve Requirement shall be transferred at least semiannually on the first Business Day following an Interest Payment Date to the Interest Account. Amounts on deposit in the Escrowed Bond Proceeds Fund shall not be included in calculating the Reserve Requirement, until such time as monies are released from the Escrowed Bond Proceeds Fund to the Redevelopment Fund as described in the Indenture. The Trustee shall transfer from the Escrowed Bond Proceeds Fund to the Reserve Account the amount set forth in the Written Certificate of the Agency required pursuant to such release.

Anything to the contrary herein notwithstanding the Agency may at any time substitute an Alternate Reserve Account Security (herein "Security"), with the consent of the Bond Insurer, and upon such substitution, the Agency shall be entitled to receive all moneys then held in the Reserve Account and the Agency shall deposit such moneys in the Redevelopment Fund for application to the costs of the Redevelopment Project. In the event the Agency delivers an Alternate Reserve Account Security, the Trustee shall hold and apply such instrument pursuant to the Indenture so as to have moneys available

thereunder for the purposes and at the times required under the Indenture. The Trustee shall deliver to the provider of the Security a demand for payment under the Alternate Reserve Account Security not less than three days prior to the date upon which moneys are required hereunder. The Trustee shall apply all cash amounts in the Reserve Account to the purposes herein provided prior to making any demand for payment upon the provider of the Security. The Trustee shall maintain adequate records, verified with the provider of the Security, as to the amount available to be drawn at any given time under the Alternate Reserve Account Security and as to the amounts paid and owing to the provider of the Security.

Surplus Account. It is the intent of the Indenture: (i) that the deposits to the Interest Account and the Principal Account, respectively, shall be made as scheduled, and (ii) that the deposits to the Reserve Account shall be made as necessary to maintain a balance equal to the Reserve Requirement, if and only if the Tax Revenues are sufficient therefor. Should it be necessary to defer all or part of any deposits referred to in the Reserve Account above, such deferred deposits shall be cumulative and shall be made when the Tax Revenues are sufficient to make the deposits required by the Interest Account and the Principal Account and thereafter make the deposits required by the Reserve Account.

If: (i) the above transfers have been made so that the required amounts as of that time are in the above mentioned Accounts and the required transfer has been made to the Excess Investment Earnings Fund as set forth below, (ii) the Tax Revenues to be received by the Agency in the current Fiscal Year, based upon the most recent assessed valuation of taxable property in Redevelopment Project Area, furnished by the appropriate officer of the County are at least equal to 125% of the Maximum Annual Debt Service on all Bonds and Parity Bonds and any loans, advances or indebtedness payable from Tax Revenues on a parity with the Bonds pursuant to Section 33670 of the Law, as shown by the certificate or opinion of an Independent Financial Consultant employed by the Agency, said opinion or certificate having been filed with the Trustee, and (iii) there has been no material change in the status of the Redevelopment Project which in the opinion of an Independent Redevelopment Consultant, said opinion having been filed with the Trustee, would be likely to result in diminution of increment in the succeeding Fiscal Year, upon direction of the Agency, any balances in the Special Fund shall be deposited in the Surplus Account and may be used and applied by the Agency for any lawful purpose, including without limitation, the purchase and/or call and redemption of Bonds and Parity Bonds.

Excess Investment Earnings Fund. A special fund is created and designated the "Excess Investment Earnings Fund" (the "Excess Investment Earnings Fund") which is to be held by the Trustee and in which there shall be established two separate sub-accounts designated the "Rebate Account" and the "Alternative Penalty Account." Absent an opinion of bond counsel that the exclusion from gross income for federal income tax purposes of interest on the applicable Bonds will not be adversely affected, the Agency shall cause to be deposited in each such account of the Excess Investment Earnings Fund such amounts as are required to be deposited therein pursuant to the Indenture and the Tax Certificate. All money at any time deposited in the Rebate Account or the Alternative Penalty Account shall be held by the Trustee in trust, for payment to the United States Treasury. All amounts on deposit in the Excess Investment Earnings Fund shall be governed by the Indenture and the Tax Certificate, unless and to the extent that the Agency delivers to the Trustee an opinion of bond counsel that the exclusion from gross income for federal income tax purposes of interest on the Bonds will not be adversely affected if such requirements are not satisfied.

The following requirements shall be satisfied with respect to the Rebate Account:

Computation. Within 55 days of the end of each fifth Bond Year, the Agency shall calculate or cause to be calculated the amount of rebatable arbitrage, in accordance with Section 148(f)(2) of the Code and Section 1.148-3 of the Rebate Regulations (taking into account any applicable exceptions with respect to the computation of the rebatable arbitrage, described, if applicable, in the Tax Certificate [e.g., the temporary investments exceptions of Section 148(f)(4)(B) and (C) of the Code], and taking into account whether the election pursuant to Section 148(f)(4)(C)(vii) of the Code [the "11/2% Penalty"] has been made), for this purpose treating the last day of the applicable Bond Year as a computation date, within the meaning of Section 1.148 1(b) of the Rebate Regulations (the "Rebatable Arbitrage"). The Agency shall obtain expert advice as to the amount of the Rebatable Arbitrage to comply with this Section.

Transfer. Within 55 days of the end of each fifth Bond Year, upon the written direction of the Agency, an amount shall be deposited to the Rebate Account by the Trustee from any Revenues legally

available for such purpose (as specified by the Agency in the aforesaid written direction), if and to the extent required so that the balance in the Rebate Account shall equal the amount of Rebatable Arbitrage so calculated in accordance with (a) of this Subsection (a)(i). In the event that immediately following the transfer required by the previous sentence, the amount then on deposit to the credit of the Rebate Account exceeds the amount required to be on deposit therein, upon written instructions from the Agency, the Trustee shall withdraw the excess from the Rebate Account and then credit the excess to the Special Fund.

Payment to the Treasury. The Trustee shall pay, as directed by the Agency, to the United States Treasury, out of amounts in Rebate Account: Not later than 60 days after the end of (a) the fifth Bond Year, and (b) each applicable fifth Bond Year thereafter, an amount equal to at least 90% of the Rebatable Arbitrage calculated as of the end of such Bond Year; and not later than 60 days after the payment of all the Bonds, an amount equal to 100% of the Rebatable Arbitrage calculated as of the end of such applicable Bond Year, and any income attributable to the Rebatable Arbitrage, computed in accordance with Section 148(f) of the Code.

In the event that, prior to the time of any payment required to be made from the Rebate Account, the amount in the Rebate Account is not sufficient to make such payment when such payment is due, the Agency shall calculate or cause to be calculated the amount of such deficiency and deposit an amount received from any legally available source equal to such deficiency prior to the time such payment is due. Each payment required to be made pursuant to the Indenture shall be made to the Internal Revenue Service Center, Philadelphia, Pennsylvania 19255 on or before the date on which such payment is due, and shall be accompanied by Internal Revenue Service Form 8038 T, which shall be prepared by the Agency and provided to the Trustee or shall be made in such other manner as the Agency shall direct.

Alternative Penalty Account.

Six-Month Computation. If the 11/2% Penalty has been elected, within 85 days of each particular Six-Month Period, the Agency shall determine or cause to be determined whether the 11/2% Penalty is payable (and the amount of such penalty) as of the close of the applicable Six-Month Period. The Agency shall obtain expert advice in making such determinations.

Six-Month Transfer. Within 85 days of the close of each Six-Month Period, upon the written direction of the Agency, the Trustee shall deposit in the Alternative Penalty Account from any legally available source of funds (as specified by the Agency in the aforesaid written direction), if and to the extent required, so that the balance in the Alternative Penalty Account equals the amount of the 11/2% Penalty due and payable to the United States Treasury determined as provided in the Indenture. In the event that immediately following the transfer provided in the previous sentence, the amount then on deposit to the credit of the Alternative Penalty Account exceeds the amount required to be on deposit therein to make the payments required by the Indenture, the Trustee, at the written direction of the Agency, may withdraw the excess from the Alternative Penalty Account and credit the excess to the Special Fund.

Payment to the Treasury. The Trustee shall pay, as directed in writing by the Agency, to the United States Treasury, out of amounts in an Alternative Penalty Account, not later than 90 days after the close of each Six-Month Period the 11/2% Penalty, if applicable and payable, computed in accordance with Section 148(f)(4) of the Code. In the event that, prior to the time of any payment required to be made from the Alternative Penalty Account, the amount in such account is not sufficient to make such payment when such payment is due, the Agency shall calculate the amount of such deficiency and direct the Trustee to deposit an amount received from any legally available source of funds equal to such deficiency into the Alternative Penalty Account prior to the time such payment is due. Each payment required to be made pursuant to this Subsection (a)(ii) shall be made to the Internal Revenue Service, Philadelphia, Pennsylvania 19255 on or before the date on which such payment is due, and shall be accompanied by Internal Revenue Service Form 8038 T which shall be prepared by the Agency and provided to the Trustee or shall be made in such other manner as directed by the Agency.

Investment of Moneys in Funds and Accounts. Moneys in the Special Fund and the Accounts therein (other than the Reserve Account), the Escrowed Proceeds Fund and the Redemption Fund shall be invested and reinvested by the Trustee in Permitted Investments, provided that such investments mature

by their terms prior to the date on which such moneys are required to be paid out hereunder. Moneys in the Reserve Account shall be invested by the Trustee solely in Permitted Investments described in (i), (ii) and (v) of the definition of Permitted Investments having a maturity not greater than 5 years or beyond the date it is anticipated that such moneys will be needed, whichever comes first; provided, that such moneys may be invested pursuant to an investment agreement approved by the Bond Insurer. No Debt Service Reserve Fund credit facilities, insurance policies, investment agreements, forward delivery agreements, hedge or par put agreements may be used without the prior written consent of Insurer. Such investments shall be made in specific investments meeting the requirements of this section as directed in writing by the Executive Director (such written direction to be received by 12:00 noon Pacific Time two [2] Business Days prior to such investment) or, in the absence of such written direction, by the Trustee in Permitted Investments described in (v) of the definition thereof. The Trustee shall be protected from any liability in acting in accordance with this section or the Agency's direction. Moneys in the Redevelopment Fund shall be invested as directed by the Agency by the Treasurer in any legal investments for Agency funds which will by their terms mature not later than the date the Agency estimates the moneys represented by the particular investment will be needed for withdrawal from the Redevelopment Fund. Moneys in the Excess Investment Earnings Fund shall be invested in Federal Securities which mature before the date such amounts are required to be paid to the United States. Obligations purchased as an investment of moneys in any Fund or Account held by the Trustee hereunder shall be deemed to be part of such Fund or Account. Any or all interest or gain received from such investment of moneys in any Fund or Account shall be deposited by the Trustee in the respective Fund or Account and any loss incurred in connection with such investment shall be debited against the Fund or Account from which the investment was made. The Trustee shall have no liability or responsibility for any loss resulting from any investment made in accordance with the provisions of the Indenture.

Except as otherwise provided in the Indenture, obligations purchased as an investment of moneys in any of the Funds or Accounts shall be deemed at all times to be a part of such respective Fund or Account, and the interest accruing thereon and any gain or loss realized from an authorized investment will be charged to such Fund or Account without liability to the Agency or the members and officers thereof or to the Trustee. The Agency or the Trustee, as the case may be, shall sell or present for redemption any obligation purchased whenever it will be necessary to do so in order to provide moneys to meet any payment or transfer from such Fund or Account as required by the Indenture and shall incur no liability for any loss realized upon such a sale. The investment constituting a part of the Fund or Account will be valued at the lower of cost or the then estimated or appraised market value of the investment at least semi-annually. All interest earnings received on any moneys invested in the Interest Account, Principal Account or Reserve Account, to the extent they exceed the amount required to be in such Account, will be transferred on each Interest Payment Date to the Special Fund. All interest earnings on moneys invested in the Redevelopment Fund will be retained in such Fund and applied to the costs of the Redevelopment Project. All interest earnings on moneys invested in the Excess Investment Earnings Fund will be retained in such Fund and applied as set forth in the Indenture.

The Agency acknowledges that to the extent that regulations of the Comptroller of the Currency or other applicable regulatory agency grant the Agency the right to receive brokerage confirmations of security transactions as they occur, the Agency specifically waives receipt of such confirmations to the extent permitted by law. The Trustee shall furnish to the Agency periodic statements of account which include detail for all investment transactions made by the Trustee.

Covenants of the Agency. As long as the Bonds and any Parity Bonds are Outstanding and unpaid, the Agency shall (through its proper members, officers, agents or employees) faithfully perform and abide by all of the covenants, undertakings and provisions contained in the Indenture or in any Bond issued hereunder, including the following covenants and agreements for the benefit of the Bondowners which are necessary, convenient and desirable to secure the Bonds and will tend to make them more marketable; provided, however, that the covenants do not require the Agency to expend any funds other than amounts credited to the Redevelopment Fund to the extent required to fulfill the Agency objectives with respect to Covenant 1 and Covenant 2, Tax Revenues and the income thereon:

Covenant 1. Complete Redevelopment Project; Amendment to Redevelopment Plan. The Agency covenants and agrees that it will diligently carry out and continue to completion in a sound and economical manner, with all practicable dispatch, the Redevelopment Project in accordance with its duty to do so under and in accordance with the Law and the Redevelopment Plan. The Redevelopment Plan

may be amended as provided in the Law but no amendment shall be made unless it will not substantially impair the security of the Bonds or the rights of the Bondowners, as shown by an Opinion of Counsel, based upon a certificate or opinion of an Independent Financial Consultant appointed by the Agency and with respect to any amendment which could result in a reduction of the amount of Tax Revenues allocated and paid to the Agency, the Bond Insurer shall have consented in writing.

Covenant 2. Use of Proceeds, Management and Operation of Properties. The Agency covenants and agrees that the proceeds of the sale of the Bonds will be deposited and used as provided in the Indenture and that it will manage and operate all properties owned by it comprising any part of the Project Area in a sound and businesslike manner consistent with the Redevelopment Plan.

Covenant 3. No Priority. The Agency covenants and agrees that it will not issue any obligations payable, either as to principal or interest, from the Tax Revenues which have any lien upon Tax Revenues prior to or superior to the lien of the Bonds. The Agency shall represent and warrant that it has not heretofore made a pledge of, granted a lien on or security interest in, or made an assignment or sale of the Tax Revenues that ranks on a parity with or prior to the pledge granted under the Indenture, except to secure the 1998 Bonds that will be outstanding upon issuance of the Bonds. Except as permitted by the Indenture, it will not issue any obligations, payable as to principal or interest, from the Tax Revenues which have any lien upon the Tax Revenues on a parity with the Bonds. Notwithstanding the foregoing, nothing in the Indenture shall prevent the Agency: (i) from issuing and selling pursuant to law, refunding obligations payable from and having any lawful lien upon the Tax Revenues, if such refunding obligations are issued for the purpose of, and are sufficient for the purpose of, refunding all of the Outstanding Bonds or Parity Bonds; (ii) from issuing and selling obligations which have, or purport to have, any lien upon the Tax Revenues which is junior to the Bonds and any Parity Bonds; or (iii) from issuing and selling bonds or other obligations which are payable in whole or in part from sources other than the Tax Revenues. As used herein "obligations" shall include, without limitation, bonds, notes, interim certificates, debentures or other obligations, loans, advances, or other forms of indebtedness incurred by the Agency.

Covenant 4. Punctual Payment. The Agency covenants and agrees that it will duly and punctually pay or cause to be paid the principal of and interest on each of the Bonds on the date, at the place and in the manner provided in the Bonds.

Covenant 5. Payment of Taxes and Other Charges. The Agency covenants and agrees that it will from time to time pay and discharge, or cause to be paid and discharged, all payments in lieu of taxes, service charges, assessments or other governmental charges which may lawfully be imposed upon the Agency or any of the properties then owned by it in the Project Area, or upon the revenues and income therefrom, and will pay all lawful claims for labor, materials and supplies which if unpaid might become a lien or charge upon any of the properties, revenues or income or which might impair the security of the Bonds or the use of Tax Revenues or other legally available funds to pay the principal of and interest on the Bonds, all to the end that the priority and security of the Bonds shall be preserved; provided, however, that nothing in this covenant shall require the Agency to make any such payment so long as the Agency in good faith shall contest the validity of the payment.

Covenant 6. Books and Accounts; Financial Statements. The Agency covenants and agrees that it will at all times keep, or cause to be kept, proper and current books and accounts (separate from all other records and accounts) in which complete and accurate entries shall be made of all transactions relating to the Redevelopment Project and the Tax Revenues and other funds relating to the Redevelopment Project. The Agency will prepare within one hundred eighty (180) days after the close of each of its Fiscal Years a complete financial statement or statements for such year, in reasonable detail covering the Tax Revenues and other funds, accompanied by an opinion of an Independent Certified Public Accountant appointed by the Agency, and will furnish a copy of the statement or statements to the Trustee, the Bond Insurer and any rating agency which maintains a rating on the Bonds and, upon written request, to any Bondowner. The Trustee shall have no duty to review the Agency's financial statements.

Covenant 7. Eminent Domain Proceedings. The Agency covenants and agrees that if all or any part of the Project Area should be taken from it without its consent, by eminent domain proceedings or

other proceedings authorized by law, for any public or other use under which the property will be tax exempt, it shall take all steps necessary to adjust accordingly the base year valuation of the Project Area.

Covenant 8. Disposition of Property. The Agency covenants and agrees that it will not dispose of more than ten percent (10%) of the land area in the Project Area (except property shown in the Redevelopment Plan in effect on the date the Indenture is adopted as planned for public use, or property to be used for public streets, public offstreet parking, sewage facilities, parks, easements or right-of-way for public utilities, or other similar uses) to public bodies or other persons or entities whose property is tax exempt, unless such disposition will not result in the security of the Bonds and any Parity Bonds or the rights of Bondowners being substantially impaired, as shown by an Opinion of Counsel addressed to the Agency and the Trustee, based upon the certificate or opinion of an Independent Financial Consultant appointed by the Agency.

Covenant 9. Protection of Security and Rights of Bondowners. The Agency covenants and agrees to preserve and protect the security of the Bonds and any Parity Bonds and the rights of the Bondowners and any Parity Bondowners and to contest by court action or otherwise: (a) the assertion by any officer of any government unit or any other person whatsoever against the Agency that (i) the Law is unconstitutional or (ii) that the Tax Revenues pledged hereunder cannot be paid to the Agency for the debt service on the Bonds, or (b) any other action affecting the validity of the Bonds or diluting the security therefor.

Covenant 10. Tax Covenants. The Agency covenants and agrees to contest by court action or otherwise any assertion by the United States of America or any department or agency thereof that the interest received by the Bondowners is includable in gross income of the recipient under federal income tax laws. Notwithstanding any other provision of the Indenture, absent an opinion of Bond Counsel that the exclusion from gross income of interest with respect to the Bonds and any Parity Bonds will not be adversely affected for federal income tax purposes, the Agency covenants to comply with all applicable requirements of the Code necessary to preserve such exclusion from gross income and specifically covenants, without limiting the generality of the foregoing, as follows:

(i) Private Activity. The Agency will take no action or refrain from taking any action or make any use of the proceeds of the Bonds or any Parity Bonds or of any other monies or property which would cause the Bonds or any Parity Bonds to be "private activity bonds" within the meaning of Section 141 of the Code;

(ii) Arbitrage. The Agency will make no use of the proceeds of the Bonds or any Parity Bonds or of any other amounts or property, regardless of the source, or take any action or refrain from taking any action which will cause the Bonds or any Parity Bonds to be "arbitrage bonds" within the meaning of Section 148 of the Code;

(iii) Federal Guaranty. The Agency will make no use of the proceeds of the Bonds or any Parity Bonds or take or omit to take any action that would cause the Bonds or any Parity Bonds to be "federally guaranteed" within the meaning of Section 149(b) of the Code;

(iv) Information Reporting. The Agency will take or cause to be taken all necessary action to comply with the informational reporting requirement of Section 149(e) of the Code;

(v) Hedge Bonds. The Agency will make no use of the proceeds of the Bonds or any Parity Bonds or any other amounts or property, regardless of the source, or take any action or refrain from taking any action that would cause either the Bonds or any Parity Bonds to be considered "hedge bonds" within the meaning of Section 149(g) of the Code unless the Agency takes all necessary action to assure compliance with the requirements of Section 149(g) of the Code to maintain the exclusion from gross income of interest on the Bonds and any Parity Bonds for federal income tax purposes; and

(vi) Miscellaneous. The Agency will take no action or refrain from taking any action inconsistent with its expectations stated in that certain Tax Certificate executed by the Agency in connection with each issuance of Bonds and any Parity Bonds and will comply with the covenants and requirements stated therein and incorporated by reference herein.

Covenant 11. Taxation of Leased Property. Whenever any property in the Project Area has been redeveloped and thereafter is leased by the Agency to any person or persons (other than a public agency), or whenever the Agency leases real property in the Project Area to any person or persons (other than a public agency) for redevelopment, the property shall be assessed and taxed in the same manner as privately owned property, as required by Section 33673 of the Law, and the lease or contract shall provide: (a) that the lessee shall pay taxes upon the assessed value of the entire property and not merely upon the assessed value of his or its leasehold interest; and (b) that if for any reason the taxes levied on the property in any year during the term of the lease or contract are less than the taxes which would have been levied if the entire property had been assessed and taxed in the same manner as privately owned property, the lessee shall pay such difference to the Agency within thirty (30) days after the taxes for the year become payable to the taxing agencies and in no event later than the delinquency date of such taxes established by law. All such payments shall be treated as Tax Revenues, and when received by the Agency shall be used as provided herein. As an alternative to payment to the Agency pursuant to (b) above, the new owner or owners of property becoming exempt from taxation may elect to make payment to the Agency in a single sum equal to the amount estimated by an Independent Financial Consultant to be receivable by the Agency from taxes on said property from the date of said payment to the maturity date of the Bonds, less a reasonable discount value. All such single sum payments in lieu of taxes shall be treated as Tax Revenues and shall be transferred to the Trustee for deposit in the Special Fund.

Covenant 12. Compliance With Law. The Agency covenants that it shall comply with all requirements of the Law to insure the allocation and payment to it of the Tax Revenues including, without limitation, the timely filing of any necessary statements of indebtedness with appropriate officials of the County, and shall forward information copies of each such filing to the Trustee. The Agency further covenants and agrees that, except for the Pass-Through Agreements, it has not entered into any agreements with other tax entities as of the date of the Indenture for the pass-through of any Tax Revenues to such entities and will not hereafter enter into any such agreement which requires payment to such taxing entities prior to deposit of Tax Revenues in the Special Fund.

Covenant 13. Limitation on Indebtedness. The Agency covenants and agrees that it has not and will not incur any loans, obligations or indebtedness repayable from Tax Revenues such that the total aggregate debt service on said loans, obligations or indebtedness incurred from and after the date of adoption of the Redevelopment Plan, when added to any predecessor debt and the total aggregate debt service on the Bonds, will exceed the maximum amount of Tax Revenues to be divided and allocated to the Agency pursuant to the Redevelopment Plan.

Covenant 14. Further Assurances. The Agency covenants and agrees to adopt, make, execute and deliver any and all such further indentures, instruments and assurances as may be reasonably necessary or proper to carry out the intention or to facilitate the performance of the Indenture, and for the better assuring and confirming unto the Trustee and the Owners of the Bonds and any Parity Bonds of the rights and benefits provided therein.

Compliance with Indenture, Contracts, Laws and Regulations. The Agency shall faithfully observe and perform all the covenants, conditions and requirements of the Indenture, shall not issue any Bonds in any manner other than in accordance with the Indenture, and shall not exercise its discretion in any way that might materially weaken, diminish or impair the security intended to be given pursuant to the Indenture. Subject to the limitations and consistent with the covenants, conditions and requirements contained in the Indenture, the Agency shall comply with the terms, covenants and provisions, express or implied, of all contracts concerning or affecting the application of proceeds of the Bonds or the Tax Revenues. The Agency shall comply promptly, fully and faithfully with and abide by any statute, law, ordinance, order, rule or regulation, judgment, decree, direction or requirement now in force or hereafter enacted, adopted, prescribed, imposed or entered by any competent governmental authority or agency applicable to or affecting the Redevelopment Project.

Defaults.

(a) Events of Default. Each of the following shall constitute an Event of Default:

(i) Default in the due and punctual payment by the Agency of any installment of interest on any Bond when the interest installment becomes due and payable;

(ii) Default in the due and punctual payment by the Agency of the principal and premium, if any, of any Bond when the principal becomes due and payable, whether at maturity, by declaration or otherwise;

(iii) Default made by the Agency in the observance of any of the covenants, agreements or conditions contained in the Indenture or in the Bonds, where the default continues for a period of thirty (30) days following written notice to the Agency;

(iv) Default in complying with the provisions of the Indenture relating to Subordinated Indebtedness; or

(v) The Agency files a petition seeking reorganization or arrangement under the federal bankruptcy laws or any other applicable law of the United States of America, or if a court of competent jurisdiction shall approve a petition, filed with or without the consent of the Agency, seeking reorganization under the federal bankruptcy laws or any other applicable law of the United States of America, or if, under the provisions of any other law for the relief or aid of debtors, any court of competent jurisdiction shall assume custody or control of the Agency or of the whole or any substantial part of its property.

In each Event of Default described in (i) or (ii) above the Trustee shall, and in each Event of Default described in (iii), (iv) or (v) above, the Trustee shall upon written request of Bond Insurer or the Owners of not less than a majority of the aggregate principal amount of the Bonds at the time outstanding, with the consent of Bond Insurer, (such request to be in writing to the Trustee and to the Agency), declare the principal of all of the Bonds then outstanding and the interest accrued thereon, to be due and payable immediately. The Insurer may, in its discretion, either direct the accelerated payment of the Bonds or continue to pay principal and interest on the originally scheduled due dates of the Bonds. Upon any such declaration the Bonds shall become and shall be immediately due and payable, anything in this Indenture or in the Bonds to the contrary notwithstanding. No waivers shall be granted by the Agency or the Trustee without the prior written consent of the Insurer.

Upon an Event of Default, all Tax Revenues under the Indenture shall be immediately deposited with the Trustee.

The declaration may be rescinded by the Owners of not less than a majority of the Bonds then outstanding provided the Agency cures the default or defaults and deposits with the Trustee a sum sufficient to pay all principal on the Bonds matured prior to the declaration and all matured installments of interest (if any) upon all the Bonds so that the Agency is currently in compliance with all payment, deposit and transfer provisions of the Indenture, and has paid or provided for the payment of any fees and expenses incurred by the Trustee in connection with the default.

(b) Certain Remedies of Bondowners. Any Bondowner shall have the right, for the equal benefit and protection of all Bondowners similarly situated--

(i) by mandamus, suit, action or proceeding, to compel the Agency and its members, officers, agents or employees to perform each and every term, provision and covenant contained in the Indenture and in the Bonds, and to require the carrying out of any or all such covenants and agreements of the Agency and the fulfillment of all duties imposed upon it by the Law;

(ii) by suit, action or proceeding in equity, to enjoin any acts or things which are unlawful, or the violation of any of the Bondowners' rights; or

(iii) upon the happening of any event of default (as defined in the Indenture), by suit, action or proceeding in any court of competent jurisdiction, to require the Agency and its members and employees to account as if it and they were the Trustees of an express trust.

Anything in the Indenture to the contrary notwithstanding, upon the occurrence and continuance of an Event of Default as defined herein, the Bond Insurer shall be entitled to control and direct the enforcement of all rights and remedies granted to the Bondholders or the Trustee for the benefit of the

Bondholders under the Indenture, including, without limitation, acceleration of the maturity of the Bonds as described in the Indenture and the right to annul any declaration of acceleration, and the Bond Insurer shall also be entitled to approve all waivers of events of default.

(c) Non-Waiver. Nothing in the Indenture or in any other provisions of the Indenture, or in the Bonds, shall affect or impair the obligation of the Agency, which is absolute and unconditional, to pay the principal of and interest on the Bonds to the respective Owners of the Bonds at the date of maturity, as herein provided, or affect or impair the right, which is also absolute and unconditional, of the Owners to institute suit to enforce the payment by virtue of the contract embodied in the Bonds.

No remedy conferred upon any Bondowner or Trustee by the Indenture is intended to be exclusive of any other remedy, but each remedy is cumulative and in addition to every other remedy and may be exercised without exhausting and without regard to any other remedy conferred by the Law or any other law of the State of California. No waiver of any default or breach of any duty or contract by any Bondowner or Trustee shall affect any subsequent default or breach of any duty or contract or shall impair any rights or remedies on the subsequent default or breach. No delay or omission of any Bondowner or Trustee to exercise any right or power accruing upon any default shall impair any such right or power or shall be construed as a waiver of any default or acquiescence therein. Every substantive right and every remedy conferred upon the Bondowners or Trustee may be enforced and exercised as often as may be deemed expedient. In case any suit, action or proceeding to enforce any right, or exercise any remedy, shall be brought and should said suit, action or proceeding be abandoned, or be determined adversely to the Bondowners or Trustee, then, and in every such case, the Agency, Trustee or the Bondowners shall be restored to their former positions, rights and remedies as if the suit, action or proceeding had not been brought or taken.

(d) Actions by Trustee as Attorney-in-Fact. Any suit, action or proceeding which any Bondowner shall have the right to bring to enforce any right or remedy hereunder may be brought by the Trustee for the equal benefit and protection of all Owners of Bonds similarly situated and the Trustee is hereby appointed (and the successive respective Owners of the Bonds issued hereunder, by taking and holding the same, shall be conclusively deemed so to have appointed it) the true and lawful attorney-in-fact of the respective Owners of the Bonds for the purpose of bringing any suit, action or proceeding and to do and perform any and all acts and things for and on behalf of the respective Owners of the Bonds as a class or classes, as may be necessary or advisable in the opinion of the Trustee as attorney-in-fact; provided, however, the Trustee shall not be required to act hereunder pursuant to this subsection (d) unless (i) the Owners of a majority in principal amount of the Bonds then Outstanding, by written instrument delivered to the Trustee, direct such action, and (ii) it shall receive indemnification satisfactory to it and reimbursement of all fees and expenses (including its reasonable attorneys fees and expenses) to which it may be put and to protect it against all liability, except liability which is to be adjudicated to have resulted from its negligence or willful misconduct in connection with any action so taken.

(e) General. After the issuance and delivery of the Bonds, the Indenture, and any supplemental indentures hereto, shall be irrevocable, but shall be subject to modification or amendment to the extent and in the manner provided in the Indenture, but to no greater extent and in no other manner.

(f) Default Rate. Amounts paid by Insurer in respect of the principal and/or interest on the Bonds shall bear interest until repaid to Insurer at a per annum rate of interest equal to the rate from time to time announced by the Insurance Trustee as its base lending rate plus three percent (3%) (the "Default Rate").

Application of Funds Upon Acceleration. Upon any acceleration of the Bonds, the Trustee shall, following payment of the costs and expenses (including fees and expenses of its agents and attorneys) of the Trustee and the Bondowners in declaring such Event of Default or any outstanding fees and expenses, transfer first to the Interest Account an amount equal to (i) the interest due on the Bonds to the date of acceleration minus the amount of moneys then held by the Trustee in the Interest Account and then to the Principal Account all of the moneys held in the Reserve Account and any other moneys held in the Special Fund and the Accounts therein or in the Redemption Fund. If such deposits are insufficient to pay the principal of and interest on the Bonds, the Trustee shall file a claim for payment with the Bond Insurer pursuant to the Indenture and apply the proceeds of such draw to the Interest Account and Principal Account, as appropriate. After the above transfers have been made, all of the amounts paid

under the Financial Guaranty Insurance Policy and all sums in the Special Fund and the Accounts therein upon the date of the declaration of acceleration as provided in the Indenture, and all sums thereafter received by the Trustee hereunder, shall be applied by the Trustee to the payment of all other outstanding fees and expenses of the Trustee (including fees and expenses of its counsel) and thereafter in the following order upon presentation of the Bonds, and the stamping thereon of the payment if only partially paid, or upon the surrender thereof if fully paid:

First, moneys in the Principal Account, if any, shall be applied to the payment in full of the principal of the Outstanding Bonds;

Second, moneys in the Interest Account shall be applied to the payment of interest coming due and payable on the Bonds as of the date of acceleration; and

Third, any moneys remaining in the Special Fund and Accounts therein shall be applied to the payment of any amounts due and owing by the Agency to the Bond Insurer which are identified in a written certificate executed by a representative of the Bond Insurer and filed with the Trustee.

Payment Procedure Pursuant to Financial Guaranty Insurance Policy. The Trustee shall not make a claim for payment on the Financial Guaranty Insurance Policy until any and all funds held pursuant to the Indenture have been fully drawn to pay debt service on the Bonds.

As long as the Financial Guaranty Insurance Policy shall be in full force and effect, the Trustee agrees to comply with the following provisions:

(a) At least three (3) days prior to all Interest Payment Dates, the Trustee, will determine whether there will be sufficient funds to pay the principal of or interest on the Bonds on such Interest Payment Date. If the Trustee determines that there will be insufficient funds, the Trustee shall so notify the Insurance Trustee. Such notice shall specify the amount of the anticipated deficiency, the Bonds to which such deficiency is applicable and whether such Bonds will be deficient as to principal or interest, or both. The Insurer will make payments of principal or interest due on the Bonds on or before the first (1st) day next following the date on which the Insurance Trustee shall have received notice of nonpayment from the Trustee.

(b) The Trustee shall, after giving notice to the Insurance Trustee as provided in (a) above, make available to the Insurer and the Insurance Trustee, the registration books of the Agency maintained by the Trustee, and all records relating to the funds maintained under this Indenture.

(c) The Trustee shall provide the Insurer and the Insurance Trustee with a list of registered owners of Bonds entitled to receive principal or interest payments from the Insurer under the terms of the Financial Guaranty Insurance Policy, and shall make arrangements with the Insurance Trustee (i) to mail checks or drafts to the registered owners of Bonds entitled to receive full or partial interest payments from the Insurer and (ii) to pay principal upon Bonds surrendered to the Insurance Trustee by the registered owners of Bonds entitled to receive full or partial principal payments from the Insurer.

(d) The Trustee shall at the time it provides notice to the Insurance Trustee pursuant to (a) above, notify registered owners of Bonds entitled to receive the payment of principal or interest thereon from the Insurer (i) as to the fact of such entitlement, (ii) that the Insurer will remit to them all or part of the interest payments next coming due upon proof of registered owner entitlement to interest payments and delivery to the Insurance Trustee, in form satisfactory to the Insurance Trustee as determined by the Insurer, of an appropriate assignment of the registered owner's right to payment, (iii) that should they be entitled to receive full payment of principal from the Insurer, they must surrender their Bonds (along with an appropriate instrument of assignment in form satisfactory to the Insurer to permit ownership of such Bonds to be registered in the name of the Insurer) for payment to the Insurance Trustee, and not the Trustee and (iv) that should they be entitled to receive partial payment of principal from the Insurer, they must surrender their Bonds for payment thereon first to the Trustee, who shall note on such Bonds the portion of the principal paid by the Trustee and then, along with an appropriate instrument of assignment in form satisfactory to the Insurer, to the Insurance Trustee, which will then pay the unpaid portion of principal.

(e) In the event that the Trustee has notice that any payment of principal of or interest on a Bond which has become due for payment and which is made to a registered owner by or on behalf of the Issuer has been deemed a preferential transfer and theretofore recovered from its registered owner pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with the final, nonappealable order of a court having competent jurisdiction, the Trustee shall, at the time the Insurance Trustee is notified pursuant to (a) above, notify all registered owners that in the event that any registered owner's payment is so recovered, such registered owner will be entitled to payment from the Insurer to the extent of such recovery if sufficient funds are not otherwise available, and the Trustee shall furnish to the Insurance Trustee and the Insurer its records evidencing the payments of principal of and interest on the Bonds which have been made by the Trustee and subsequently recovered from registered owners and the dates on which such payments are made.

(f) The Insurer shall, to the extent it makes payment of principal of or interest on Bonds, become subrogated to the rights of the recipients of such payments in accordance with the terms of the Financial Guaranty Insurance Policy, and to evidence such subrogation (i) in the case of subrogation as to claims for past due interest, the Trustee shall note the Insurer's rights as subrogee on the registration books of the Agency maintained by the Trustee, upon receipt from the Insurer of proof of the payment of interest thereon to the registered owners of the Bonds and (ii) in the case of subrogation as to claims for past due principal, the Trustee shall note the Insurer's rights as subrogee on the registration books of the Agency maintained by the Trustee upon surrender of the Bonds by the registered owners thereof together with proof of the payment of principal thereof.

Amendments: The Indenture, and the rights and obligations of the Agency and of the Owners of the Bonds issued hereunder, may be modified or amended at any time by Supplemental Indenture adopted by the Agency with the consent of the Bond Insurer: (a) without the consent of Bondowners, if the modification or amendment is for the purpose of preserving the exclusion of interest on the Bonds (or any refunding obligations therefor) from gross income for federal income tax purposes or if the modification or amendment is for the purpose of adding covenants and agreements further to secure Bond payment, to prescribe further limitations and restrictions on Bond issuance, to surrender rights or privileges of the Agency, to make modifications not affecting any Outstanding series of Bonds only with the consent of the Trustee, for the purpose of curing any ambiguities, defects or inconsistent provisions in the Indenture or to insert such provisions clarifying matters or questions arising under the Indenture as are necessary and desirable to accomplish the same, provided that the modifications or amendments do not adversely affect the rights of the Owners of any Outstanding Bonds; or (b) for any purpose with the consent of the Bondowners holding not less than sixty percent (60%) in aggregate principal amount of the Outstanding Bonds, exclusive of Bonds, if any, owned by the Agency or the City, and obtained as hereinafter set forth; provided, however, that no modification or amendment shall, without the express consent of the registered owner of the Bond affected, reduce the principal amount of any Bond, reduce the interest rate payable on it, extend its maturity or the times for paying interest, change the monetary medium in which principal and interest is payable, or create a mortgage, pledge or lien upon the Tax Revenues superior to or on a parity (except as provided in the Indenture) with the pledge and lien created for the Bonds and any Parity Bonds or reduce the percentage of consent required for amendment or modification and provided further, that no amendments affecting the duties, obligations or rights of the Trustee shall take effect without the consent of the Trustee. Any rating agency rating the Bonds must receive notice of each amendment to the Indenture and a copy thereof at least fifteen (15) Business Days in advance of its execution or adoption. The Insurer shall be provided with a full transcript of all proceedings relating to the execution of any such amendment.

Any act done pursuant to a modification or amendment permitted by the Indenture shall be binding upon the Owners of all of the Bonds, and shall not be deemed an infringement of any of the provisions of the Indenture or of the Law, whatever the character of the act may be, and may be done and performed as fully and freely as if expressly permitted by the original terms of the Indenture and after consent as required in the Indenture has been given, and no Bondowner shall have any right or interest to object to the action, to question its propriety or to enjoin or restrain the Agency or its officers from taking any action pursuant to such modification or amendment. The Trustee may request that the Agency provide an opinion of counsel that any such Supplemental Indenture complies with the provisions of this Article X and the Trustee may conclusively rely upon such opinion.

(a) Calling Bondowners' Meeting. If the Agency shall desire to obtain the Bondowners' consent, it shall duly adopt a resolution calling a meeting of the Bondowners for the purpose of considering the action for which consent is desired.

(b) Notice of Meeting. Notice specifying the purpose, place, date and hour of a Bondowners' meeting shall be mailed, postage prepaid by the Agency, to the respective registered owners at their addresses appearing on the bond register as maintained by the Trustee. The notice shall set forth the nature of the proposed action for which consent is desired. The place, date and hour of the meeting and the date or dates of mailing the notice shall be determined by the Agency in its discretion; provided that such notice shall be mailed at least 15 days prior to the date of the Bondowners' meeting.

The actual receipt by any Bondowner of notice of any Bondowners' meeting shall not be a condition precedent to the holding of the meeting, and failure to receive notice shall not affect the validity of the proceedings at the meeting. A certificate by the Secretary of the Agency approved by resolution of the Agency, that the meeting has been called and that notice has been given as provided herein, shall be conclusive as against all parties and no Bondowner shall have the right to show that he failed to receive actual notice of the meeting.

(c) Voting Qualifications. The Trustee shall prepare and deliver to the chairman of the meeting a statement of the names and addresses of the registered Owners of Bonds. This statement shall show maturities, serial numbers and principal amounts so that voting qualifications can be determined. No Bondowners shall be entitled to vote at the meeting unless their names appear upon the statement. No Bondowners shall be permitted to vote with respect to a larger aggregate principal amount of Bonds than is set against their names on the statement.

(d) Issuer-Owned Bonds. The Agency covenants that it will present at the meeting a certificate, signed and verified by one of its members and by the Treasurer, stating the Bond numbers and principal amounts of all Bonds owned by, or held for account of, the Agency or the City, directly or indirectly. No person shall be permitted at the meeting to vote or consent with respect to any Bond appearing upon the certificate, or any Bond which is established at or prior to the meeting to be owned by the Agency or the City, directly or indirectly, and no such Bond (in the Indenture referred to as "issuer-owned Bonds") shall be counted in determining whether a quorum is present at the meeting.

(e) Quorum and Procedure. A representation of at least sixty percent (60%) in aggregate principal amount of the Bonds then Outstanding (exclusive of issuer-owned Bonds, if any) shall be necessary to constitute a quorum at any meeting of Bondowners, but less than a quorum may adjourn the meeting from time to time, and the meeting may be held as adjourned without further notice, whether such adjournment shall have been held by a quorum or by less than a quorum. The Agency shall, by an instrument in writing, appoint a temporary chairman of the meeting, and the meeting shall be organized by the election of a permanent chairman and secretary. At any meeting each Bondowner shall be entitled to one vote for every \$5,000 principal amount of Bonds with respect to which he shall be qualified to vote as set forth above, and the vote may be given in person or by proxy duly appointed by an instrument in writing presented at the meeting. The Agency and/or the Trustee by their duly authorized representatives and counsel, may attend any meeting of the Bondowners, but shall not be required to do so.

(f) Vote Required. At any Bondowners' meeting there shall be submitted for the consideration and action of the Bondowners a statement of the proposed action for which consent is desired. If the action is consented to and approved by Bondowners holding at least sixty percent (60%) in aggregate principal amount of the Bonds then Outstanding (exclusive of issuer-owned Bonds), the chairman and secretary of the meeting shall so certify in writing to the Agency with a copy to the Trustee. The certificate shall constitute complete evidence of consent of the Bondowners under the provisions of the Indenture. A certificate signed and verified by the chairman and the secretary of any Bondowners' meeting shall be conclusive evidence and the only competent evidence of matters stated in the certificate relating to proceedings taken at the meeting.

Consent of Bond Insurer.

(a) Any provision of the Indenture expressly recognizing or granting rights in or to the Bond Insurer may not be amended in any manner which affects the rights of the Bond Insurer hereunder without the prior written consent of the Bond Insurer.

(b) Unless otherwise provided in the Indenture, Bond Insurer's consent shall be required in addition to Bondholder consent, when required, for the following purposes: (i) execution and delivery of any supplemental Indenture or any amendment, supplement or change to or modification of the Indenture (ii) removal of the Trustee or Paying Agent or selection and appointment of any successor trustee or paying agent; and (iii) initiation or approval of any action not described in (i) or (ii) above which requires Bondholder consent.

Defeasance. If the Agency shall pay or cause to be paid, or there shall be otherwise paid or provisions for payment made to or for the holders and owners of the Bonds, the principal, premium, if any, and interest due or to become due thereon at the time and in the manner stipulated therein, and if the Agency shall keep, perform and observe all and singular the covenants and promises in the Bonds and in the Indenture expressed as to be kept, performed and observed by it or on its part, and shall pay or cause to be paid to the Trustee all sums of money due or to become due according to the provisions hereof including fees and expenses of the Trustee, and shall pay or cause to be paid to the Bond Insurer all sums of money due or to become due according to the provisions hereof then the Indenture and the lien, rights and interest created hereby shall cease, determine and become null and void (except as to any surviving rights of registration, transfer or exchange of Bonds herein provided for and except for the rights of the Trustee to receive compensation and indemnification in accordance within the Indenture), whereupon the Trustee shall cancel and discharge the Indenture, and execute and deliver to the Agency such instruments in writing as shall be requested by the Agency and requisite to discharge the Indenture, and release, assign and deliver unto the Agency any and all the estate, right, title and interest in and to any and all rights assigned or pledged to the Trustee or otherwise subject to the Indenture, except moneys or securities held by the Trustee for the payment of the principal of, premium, if any, and interest on the Bonds.

The lien of the Indenture shall be discharged if the Agency shall pay and discharge the entire indebtedness on all Bonds Outstanding in any one or more of the following ways:

(a) By well and truly paying or causing to be paid the principal of and interest on all Bonds Outstanding, together with all amounts due the Trustee as and when the same become due and payable;

(b) By depositing with the Trustee, in a special trust fund created for such purpose, at or before maturity, moneys which, together with moneys then on deposit in the Special Fund and Accounts therein, is fully sufficient to pay all Bonds Outstanding, including all principal, interest and redemption premiums together with all amounts due the Trustee; or

(c) By depositing with the Trustee, in a special trust created for such purpose, moneys invested in non- redeemable obligations of the United States or those for which the full faith and credit of the United States are pledged (or cash held in certificates of deposit, savings accounts, deposit accounts or money market deposits which are fully insured by the FDIC) for the timely payment of principal and interest in such amount as an Independent Financial Consultant shall determine will, together with the interest to accrue thereon without reinvestment and moneys then on deposit in the Special Fund and Accounts therein, be fully sufficient to pay and discharge any indebtedness on all Bonds (including all principal, interest, and redemption premiums, if any) at or before maturity; then, at the option of the Agency, and notwithstanding that all Bonds shall not have been surrendered for payment, the pledge of the Tax Revenues and other funds provided for in the Indenture and all other obligations of the Agency under the Indenture with respect to all Bonds Outstanding shall cease and terminate, except only the obligation of the Agency to pay or cause to be paid to the Owners of the Bonds not so surrendered and paid all sums due thereon, and the rights of the Trustee to indemnification and payment of fees and expenses under Article IX hereof. Notice of the exercise of such option shall be filed with the Trustee. No forward delivery agreements, hedge, investment, purchase and resale agreements or par-put agreements may be used with respect to the investment of any funds or securities defeasing the Bonds without the prior written consent of the Insurer.

Any funds held by the Trustee after discharge of the lien of the Indenture including any funds which have not been claimed by the person entitled thereto within two (2) years of the date upon which such funds were scheduled to be paid, or which are not required for said purpose, shall be paid over to the Agency and thereafter Bondowners shall look only to the Agency for payment,

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APPENDIX D

FORM OF BOND COUNSEL OPINION

[Closing Date]

Lemon Grove Community Development Agency
3232 Main Street
Lemon Grove, California 91945

Re: \$6,330,000 Lemon Grove Community Development Agency (Lemon Grove
Redevelopment Project Area) 2004 Tax Allocation Bonds

Ladies and Gentlemen:

We have examined certified copies of proceedings of the Lemon Grove Development Agency (the "Agency"), and other information and documents submitted to us relative to the issuance and sale by the Agency of its (Lemon Grove Redevelopment Project Area) 2004 Tax Allocation Bonds in the original aggregate principal amount of \$6,330,000 (the "Bonds") and such other information and documents as we consider necessary to render this opinion. In rendering this opinion, we also have relied upon certain representations of fact and certifications made by the Agency, the Trustee, the purchasers of the Bonds and others. We have not undertaken to verify through independent investigation the accuracy of the representations and certifications relied upon by us.

The Bonds have been issued pursuant to the authority contained in Part 1 of Division 24 of the Health and Safety Code of the State of California (the "Act") and an Indenture of Trust dated as of August 1, 2004 between the Agency and U.S. Bank National Association, as Trustee (the "Indenture") which was approved by Resolution No. 192 of the Agency adopted on July 6, 2004 (the "Resolution").

The Bonds are initially dated as of August 10, 2004, and mature on the dates and bear interest payable on the dates and at the rates per annum set forth in the Indenture. The Bonds are registered Bonds issued in the form set forth in the Indenture, redeemable in the amounts, at the times and in the manner provided for in the Indenture. All terms not defined herein, have the meanings ascribed to those terms in the Indenture.

Based upon our examination of all of the foregoing, and in reliance thereon and on all matters of fact as we deem relevant under the circumstances, and upon consideration of applicable laws, we are of the opinion that:

(1) The Bonds have been duly and validly authorized by the Agency and are legal, valid and binding special obligations of the Agency, secured and payable from Pledged Revenues (as defined in the Indenture) and other sources as and to the extent provided for in the Indenture. The Bonds are enforceable in accordance with their terms and the terms of the Indenture, except to the extent that enforceability may be limited by moratorium, bankruptcy, reorganization, insolvency or other similar laws affecting creditors' rights generally or by the exercise of judicial discretion in accordance with general principles of equity. The Bonds are special obligations of the Agency but are not a debt of the City of Lemon Grove, the State of California or any other political subdivisions thereof within the meaning of any constitutional or statutory limitation, and neither the City of Lemon Grove, the State of California, or any other of its political subdivisions is liable for the payment thereof.

(2) The Indenture has been duly authorized by the Agency, is valid and binding upon the Agency and is enforceable in accordance with its terms, except to the extent that enforceability may be limited by moratorium, bankruptcy, reorganization, insolvency or

other laws affecting creditors' rights generally or by the exercise of judicial discretion in accordance with general principles of equity.

(3) The Indenture creates a valid pledge of that which the Indenture purports to pledge, subject to the provisions of the Indenture, except to the extent that the enforceability of the Indenture may be limited by moratorium, bankruptcy, reorganization, insolvency or other laws affecting creditors' rights generally or by the exercise of judicial discretion in accordance with general principles of equity.

(4) Under existing statutes, regulations, rulings and judicial decisions, interest on the Bonds is excluded from gross income for federal income tax purposes, and such interest is not an item of tax preference for purposes of calculating the federal alternative minimum tax imposed on individuals and corporations; however, it should be noted that, with respect to corporations, interest on the Bonds may be included as an adjustment in the calculation of alternative minimum taxable income, which may affect such corporation's alternative minimum tax liability.

(5) Interest on the Bonds is exempt from State of California personal income tax.

(6) The difference between the issue price of a Bond (the first price at which a substantial amount of the Bonds of a maturity are to be sold to the public) and the stated redemption price at maturity with respect to such Bond constitutes original issue discount. Original issue discount accrues under a constant yield method, and original issue discount will accrue to a Bondowner before receipt of cash attributable to such excludable income. The amount of original issue discount deemed received by a Bondowner will increase the Bondowner's basis in the applicable Bond. Original issue discount that accrues to the Bondowner is excluded from the gross income of such owner for federal income tax purposes, is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations (as described in paragraph 4 above), and is exempt from State of California personal income tax.

The opinions set forth in paragraph (4) and (6) above as to the exclusion from gross income of interest (and original issue discount) on the Bonds are based upon certain representations of fact and certifications made by the Agency and others and are subject to the condition that the Agency comply with certain covenants and the applicable requirements of the Internal Revenue Code of 1986, as amended (the "Code"), that must be satisfied subsequent to the issuance of the Bonds to assure that interest (and original issue discount) on the Bonds will remain excludable from gross income for federal income tax purposes. Failure to comply with such covenants and requirements of the Code may cause interest (and original issue discount) on the Bonds to be included in gross income for federal income tax purposes retroactive to the date of issuance of the Bonds. The Agency has covenanted to comply with all such requirements. We express no opinion regarding other tax consequences with respect to the Bonds.

Certain requirements and procedures contained or referred to in the Indenture, the Bond Purchase Agreement, dated as of July 28, 2004, among the Agency, the Lemon Grove Financing Authority and Kinsell, Newcomb & De Dios, Inc., and the Tax Certificate may be changed, and certain actions may be taken, under the circumstances and subject to the terms and conditions set forth in such documents, upon the advice or with the approving opinion of counsel nationally recognized in the area of tax-exempt obligations. We express no opinion as to the exclusion of interest (and original issue discount) on the Bonds from gross income for federal income tax purposes on and after the date on which any such change occurs or action is taken based upon the advice or approval of counsel other than Stradling Yocca Carlson & Rauth, a Professional Corporation.

The opinions expressed herein are based on our analysis and interpretation of existing laws, regulations, rulings and judicial decisions and the foregoing opinions cover certain matters not directly addressed by such authorities. Such opinions may be affected by actions taken (or not taken) or events occurring (or not occurring) after the date hereof. We have not undertaken to determine, or to inform any person, whether any such actions or events are taken or do occur. Such actions or

events may adversely affect the value or tax treatment of the Bonds and we express no opinion with respect thereto.

We express no opinion herein as to the accuracy, completeness or sufficiency of the Official Statement relating to the Bonds or other offering material relating to the Bonds and purchasers of the Bonds should not assume that we have reviewed the Official Statement.

Respectfully submitted,

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APPENDIX E

FORM OF CONTINUING DISCLOSURE AGREEMENT

This CONTINUING DISCLOSURE AGREEMENT (the "Disclosure Agreement"), dated as of August 1, 2004, is executed and delivered by the LEMON GROVE COMMUNITY DEVELOPMENT AGENCY (the "Agency") and U.S. BANK NATIONAL ASSOCIATION, as trustee (the "Trustee") and acting in its capacity as Dissemination Agent hereunder, in connection with the issuance of the Agency's \$6,330,000 Lemon Grove Community Development Agency Lemon Grove Redevelopment Project Area 2004 Tax Allocation Bonds (the "Bonds"). The Bonds are being issued pursuant to provisions of an Indenture of Trust, dated as of August 1, 2004, by and between the Agency and the Trustee (the "Indenture"). The Agency, Dissemination Agent and the Trustee covenant and agree as follows:

SECTION 1. Purpose of the Disclosure Agreement. This Disclosure Agreement is being executed and delivered by the Agency and the Trustee for the benefit of the Beneficial Owners of the Bonds and in order to assist the Participating Underwriter in complying with S.E.C. Rule 15c2-12(b)(5).

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

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

"*Beneficial Owner*" shall mean any person which (a) has the power, directly or indirectly, to vote or consent with respect to, or to dispose of ownership of, any Bonds (including persons holding Bonds through nominees, depositories or other intermediaries), or (b) is treated as the owner of any Bonds for federal income tax purposes.

"*Disclosure Representative*" shall mean the Executive Director of the Agency or his or her designee, or such other officer or employee as the Agency shall designate in writing to the Trustee and Dissemination Agent from time to time.

"*Dissemination Agent*" shall mean the U.S. Bank National Association, acting in its capacity as Dissemination Agent hereunder, or any successor Dissemination Agent designated in writing by the Agency and which has filed with the Trustee a written acceptance of such designation.

"*Listed Events*" shall mean any of the events listed in Section 5(a) of this Disclosure Agreement.

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

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

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

"*Rule*" shall mean Rule 15c2-12(b)(5) adopted by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as the same may be amended from time to time.

"*State Repository*" shall mean any public or private repository or entity designated by the State as a state repository for the purpose of the Rule and recognized as such by the Securities and Exchange Commission. As of the date of this Agreement, there is no State Repository.

SECTION 3. Provision of Annual Reports.

(a) The Agency shall, or shall cause the Dissemination Agent to, not later than February 15 after the end of the Agency's fiscal year, commencing February 15, 2005, provide to each Repository an Annual Report which is consistent with the requirements of Section 4 of this Disclosure Agreement. The Annual Report may be submitted as a single document or as separate documents comprising a package, and may include by reference other information as provided in Section 4 of this Disclosure Agreement. If the Agency's fiscal year changes, it shall give notice of such change in the same manner as for a Listed Event under Section 5(f).

(b) Not later than fifteen (15) Business Days prior to the date specified in subsection (a) for providing the Annual Report to Repositories, the Agency shall provide the Annual Report to the Dissemination Agent and the Trustee (if the Trustee is not the Dissemination Agent). If by such date, the Trustee has not received a copy of the Annual Report, the Trustee shall contact the Agency and the Dissemination Agent to determine if the Agency is in compliance with the first sentence of this subsection (b). The Agency shall provide a written certification with each Annual Report furnished to the Dissemination Agent and the Trustee to the effect that such Annual Report constitutes the Annual Report required to be furnished by it hereunder. The Dissemination Agent and Trustee may conclusively rely upon such certification of the Agency and shall have no duty or obligation to review such Annual Report.

(c) If the Trustee is unable to verify that an Annual Report has been provided to Repositories by the date required in subsection (a), the Trustee shall send a notice to each Repository or to the Municipal Securities Rulemaking Board and the State Repository, if any in substantially the form attached as Exhibit A.

(d) The Dissemination Agent shall:

(i) determine each year prior to the date for providing the Annual Report the name and address of each National Repository and the State Repository, if any; and

(ii) to the extent information is known to it, file a report with the Agency and (if the Dissemination Agent is not the Trustee) the Trustee certifying that the Annual Report has been provided pursuant to this Disclosure Agreement, stating the date it was provided and listing all the Repositories to which it was provided.

SECTION 4. Content of Annual Reports. The Agency's Annual Report shall contain or include by reference and update of the following tables shown in the official statement prepared for the Bonds:

- (i) Table 2—Breakdown of Assessed Value by Category of Use;
- (ii) Table 3—Historical Taxable Values and tax Increment Revenues;
- (iii) Table 4—Largest Property Taxpayers, by Assessed Value;
- (iv) Table 5—Tax Revenue Collections; and
- (v) Table 6—Appeal History.

Any or all of the items listed above may be included by specific reference to other documents, including official statements of debt issues of the Agency or related public entities, which have been submitted to each of the Repositories or the Securities and Exchange Commission. If the document included by reference is a final official statement, it must be available from the Municipal Securities Rulemaking Board. The Agency shall clearly identify each such other document so included by reference.

SECTION 5. Reporting of Significant Events.

(a) Pursuant to the provisions of this Section 5, the Agency shall give, or cause to be given, notice of the occurrence of any of the following events with respect to the Bonds, if material:

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

(b) The Trustee shall, within one (1) Business Day of obtaining actual knowledge of the occurrence of any of the Listed Events, or as soon as reasonably practicable thereafter, contact the Disclosure Representative, inform such person of the event, and request that the Agency promptly notify the Dissemination Agent in writing whether or not to report the event pursuant to subsection (0) and promptly direct the Trustee whether or not to report such event to the Bondholders. In the absence of such direction the Trustee shall not report such event unless otherwise required to be reported by the Trustee to the Bondholders under the Indenture. The Trustee may conclusively rely upon such direction (or lack thereof). For purposes of this Disclosure Agreement, "actual knowledge" of the occurrence of such Listed Events shall mean actual knowledge by the officer at the corporate trust office of the Trustee with regular responsibility for the administration of matters related to the Indenture. The Trustee shall have no responsibility to determine the materiality of any of the Listed Events.

(c) Whenever the Agency obtains knowledge of the occurrence of a Listed Event, whether because of a notice from the Trustee pursuant to subsection (b) or otherwise, the Agency shall as soon as possible determine if such event would be material under applicable federal securities laws.

(d) If the Agency has determined that knowledge of the occurrence of a Listed Event would be material under applicable federal securities laws, the Agency shall promptly notify the Dissemination Agent in writing. Such notice shall instruct the Dissemination Agent to report the occurrence pursuant to subsection.

(e) If in response to a request under subsection (b), the Agency determines that the Listed Event would not be material under applicable federal securities laws, the Agency shall so notify the Dissemination Agent in writing and instruct the Dissemination Agent not to report the occurrence pursuant to subsection.

(f) If the Dissemination Agent has been instructed by the Agency to report the occurrence of a Listed Event, the Dissemination Agent shall file a notice of such occurrence with the Municipal Securities Rulemaking Board and the State Repository or the Repositories. Notwithstanding the foregoing, notice of Listed Events described in subsections (a)(4) and (5) need not be given under this subsection any earlier than the notice (if any) of the underlying event is given to Holders of affected Bonds pursuant to the Indenture.

SECTION 6. Termination of Reporting Obligation. The Agency's obligations under this Disclosure Agreement shall terminate upon the legal defeasance, prior redemption or payment in full of all of the Bonds. If such termination occurs prior to the final maturity of the Bonds, the Agency shall give notice of such termination in the same manner as for a Listed Event under Section 5(f).

SECTION 7. Dissemination Agent. The Agency may, from time to time, appoint or engage a Dissemination Agent to assist it in carrying out its obligations under this Disclosure Agreement, and

may discharge any such Dissemination Agent, with or without appointing a successor Dissemination Agent. The Dissemination Agent shall not be responsible in any manner for the content of any notice or report prepared by the Agency pursuant to this Disclosure Agreement. The initial Dissemination Agent shall be the U.S. Bank National Association. The Dissemination Agent may resign by providing thirty days written notice to the Agency and the Trustee. The Dissemination Agent shall not be responsible for the content of any report or notice prepared by the Agency. The Dissemination Agent shall have no duty to prepare any information report nor shall the Dissemination Agent be responsible for filing any report not provided to it by the Agency in a timely manner and in a form suitable for filing.

SECTION 8. Amendment; Waiver. Notwithstanding any other provision of this Disclosure Agreement, the Agency, Dissemination Agent and the Trustee may amend this Disclosure Agreement (and the Trustee and Dissemination Agent shall agree to any amendment so requested by the Agency) provided, neither the Trustee nor the Dissemination Agent shall be obligated to enter into any such amendment that modifies or increases its duties or obligations hereunder, and any provision of this Disclosure Agreement may be waived, provided that the following conditions are satisfied:

(a) If the amendment or waiver relates to the provisions of Sections 3(a), 4, or 5(a), it may only be made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature or status of an obligated person with respect to the Bonds, or the type of business conducted;

(b) The undertaking, as amended or taking into account such waiver, would, in the opinion of nationally recognized bond counsel, have complied with the requirements of the Rule at the time of the original issuance of the Bonds, after taking into account any amendments or interpretations of the Rule, as well as any change in circumstances; and

(c) The amendment or waiver either (i) is approved by the Holders of the Bonds in the same manner as provided in the Indenture for amendments to the Indenture with the consent of Holders, or (ii) does not, in the opinion of the Trustee or nationally recognized bond counsel, materially impair the interests of the Holders or Beneficial Owners of the Bonds.

In the event of any amendment or waiver of a provision of this Disclosure Agreement, the Agency shall describe such amendment in the next Annual Report, and shall include, as applicable, a narrative explanation of the reason for the amendment or waiver and its impact on the type (or, in the case of a change of accounting principles, on the presentation) of financial information or operating data being presented by the Agency.

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

SECTION 10. Default. In the event of a failure of the Agency or the Trustee to comply with any provision of this Disclosure Agreement, the Trustee (at the written request of any Participating Underwriter or the Holders of at least 25% aggregate principal amount of Outstanding Bonds, shall but only to the extent funds in an amount satisfactory to the Trustee have been provided to it or it has been otherwise indemnified to its satisfaction from any cost, liability, expense or additional charges and fees of the Trustee whatsoever, including, without limitation, fees and expenses of its attorneys), or any Holder or Beneficial Owner of the Bonds may take such actions as may be necessary and appropriate, including seeking mandate or specific performance by court order, to cause the Agency or Trustee, as the case may be, to comply with its obligations under this Disclosure Agreement. A default under this Disclosure Agreement shall not be deemed an Event of Default under the

SECTION 14. Counterparts. This Disclosure Agreement may be executed in several counterparts, each of which shall be an original and all of which shall constitute but one and the same instrument.

LEMON GROVE COMMUNITY
DEVELOPMENT AGENCY

By _____
Name _____
Title _____

U.S. BANK NATIONAL ASSOCIATION, as
Dissemination Agent

By _____
Name _____
Title _____

EXHIBIT A

NOTICE TO REPOSITORIES OF FAILURE TO FILE ANNUAL REPORT

Name of Issuer: Lemon Grove Community Development Agency
Name of Bond Issue: Lemon Grove Community Development Agency Lemon Grove
Redevelopment Project Area 2004 Tax Allocation Bonds
Date of Issuance: [Closing Date]

NOTICE IS HEREBY GIVEN that the Issuer has not provided an Annual Report with respect to the above-named Bonds as required by the Continuing Disclosure Agreement, dated as of August 1, 2004, with respect to the Bonds. [The Issuer anticipates that the Annual Report will be filed by _____]

Dated:

U.S. BANK NATIONAL ASSOCIATION, on
behalf of the Lemon Grove Community
Development Agency

cc: Issuer

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APPENDIX F

BOOK-ENTRY SYSTEM

The information in this Appendix G has been provided by The Depository Trust Company ("DTC"), New York, NY, for use in securities offering documents, and the Agency takes no responsibility for the accuracy or completeness thereof. The Agency cannot and does not give any assurances that DTC, DTC Participants or Indirect Participants will distribute the Beneficial Owners either (a) payments of interest, principal or premium, if any, with respect to the Bonds or (b) certificates representing ownership interest in or other confirmation of ownership interest in the Bonds, or that they will so do on a timely basis or that DTC, DTC Direct Participants or DTC Indirect Participants will act in the manner described in this Official Statement.

1. DTC will act as securities depository for the Bonds (the "Securities"). The Securities will be issued as fully-registered securities registered in the name of Cede & Co. (DTC's partnership nominee) or such other name as may be requested by an authorized representative of DTC. One fully-registered Security certificate will be issued for each maturity of the Securities, in the aggregate principal amount of such issue, and will be deposited with DTC.

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

3. Purchases of Securities under the DTC system must be made by or through Direct Participants, which will receive a credit for the Securities on DTC's records. The ownership interest of each actual purchaser of each Security ("Beneficial Owner") is in turn to be recorded on the Direct and Indirect Participants' records. Beneficial Owners will not receive written confirmation from DTC of their purchase. Beneficial Owners are, however, expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the Securities are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in Securities, except in the event that use of the book-entry system for the Securities is discontinued.

4. To facilitate subsequent transfers, all Securities deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be

requested by an authorized representative of DTC. The deposit of Securities with DTC and their registration in the name of Cede & Co. or such other DTC nominee do not effect any change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the Securities; DTC's records reflect only the identity of the Direct Participants to whose accounts such Securities are credited, which may or may not be the Beneficial Owners. The Direct and Indirect Participants will remain responsible for keeping account of their holdings on behalf of their customers.

5. Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

6. Redemption notices shall be sent to DTC. If less than all of the Securities within an issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

7. Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to Securities unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the issuer as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts Securities are credited on the record date (identified in a listing attached to the Omnibus Proxy).

8. Redemption proceeds, distributions, and dividend payments on the Securities will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the issuer or the paying agent or bond trustee, on payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC nor its nominee, the paying agent or bond trustee, or the issuer, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the issuer or the paying agent or bond trustee, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

9. DTC may discontinue providing its services as depository with respect to the Securities at any time by giving reasonable notice to the issuer or the paying agent or bond trustee. Under such circumstances, in the event that a successor depository is not obtained, Security certificates are required to be printed and delivered.

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

APPENDIX G
SPECIMEN FINANCIAL GUARANTY INSURANCE POLICY

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FINANCIAL GUARANTY INSURANCE POLICY

Obligor:

Bonds:

Bond Trustee:

Insurance Trustee:

Policy Number:

Premium:

Radian Asset Assurance Inc. ("Insurer"), a corporation organized under the laws of the State of New York, in consideration of the payment of the premium and subject to the terms of this Policy, hereby unconditionally and irrevocably guarantees the payment of the Obligation (hereinafter defined) to the Insurance Trustee for the benefit of the Holders (hereinafter defined) from time to time of the Bonds. This Policy does not insure against any risk other than nonpayment of the Obligation by or on behalf of the Obligor or any other obligor to the Bond Trustee. Nonpayment includes recovery from a Holder of Bonds or the Bond Trustee of any portion of the Obligation pursuant to a final judgment by any court of competent jurisdiction holding that such payment constituted a voidable preference within the meaning of any applicable bankruptcy law.

Upon receipt by the Insurer of telephonic or telegraphic notice, such notice subsequently confirmed to the Insurer in writing by registered or certified mail, from the Insurance Trustee that the Obligor (or other obligor responsible for payment of the Obligation) has failed to provide the Bond Trustee with sufficient funds for payment of the Obligation on the Due Date (hereinafter defined), the Insurer shall, not later than such Due Date or the first business day after receipt of such notice, whichever is later, pay to the Insurance Trustee for the benefit of the Holders of the Bonds an amount which shall be sufficient to pay the Obligation, but only upon receipt by the Insurer, in a form reasonably satisfactory to it, of (a) evidence of the Holder's right to receive such payment and (b) evidence, including any appropriate instruments of assignment, that all the Holder's rights with respect to such payment shall thereupon vest in the Insurer.

"Due Date" means, when referring to the principal of the Obligation, the stated maturity date thereof or the date on which the same shall have been duly called for mandatory sinking fund prepayment and does not refer to any earlier date on which payment is due by reason of any other call for redemption, acceleration or other advancement of maturity unless the Insurer shall elect, in its sole discretion, to pay such principal due upon such redemption, acceleration or other advancement of maturity together with any accrued interest to the date of redemption, acceleration or other advancement of maturity. Tendering of payment, to the Bond Trustee, of such principal due upon such redemption, acceleration or other advancement of maturity, together with any accrued interest to the date of such redemption, acceleration or other advancement of maturity, shall satisfy the Insurer's obligations under this Policy, in full. When referring to interest on the Obligation, "Due Date" means the stated date for payment of interest.

The Insurer shall, to the extent of any payment made by it pursuant to this Policy, be deemed to have acquired and become the Holder of the Bonds or portions thereof or interest thereon paid from such payment and shall be fully subrogated to all rights to payment thereof.

As used herein, the term "Holder" or "Holders" means the registered owners of the Bonds as indicated in the registration books maintained by the Bond Trustee for such purpose at the time of nonpayment of the Obligation. The terms "Holder" or "Holders" shall not include the Obligor or any person or entity whose direct or indirect obligation constitutes the underlying security for the Obligation. As used herein, the term "Bond Trustee" means the Bond Trustee above named and any successor trustee duly appointed. As used herein, the term "Insurance Trustee" means the Insurance Trustee above named and any successor insurance trustee duly appointed. As used herein, the term "Obligation" means the payment of principal and interest regularly scheduled to be paid on the Bonds, which shall have become due for payment but shall be unpaid on the Due Date, but does not include any premium payable with respect to the Bonds, nor any redemption (except mandatory sinking fund redemption), acceleration or other advancement of maturity.

This Policy is non-cancelable for any reason. Premiums paid on this Policy are not refundable for any reason including without limitation the payment prior to maturity of the Bonds.

IN WITNESS WHEREOF, the Insurer has caused this Policy to be issued to the Insurance Trustee for the benefit of the Holders from time to time of the Bonds and to be executed and delivered by its duly authorized officer to become effective and binding upon the Insurer by virtue of the execution and delivery thereof on this ____ day of _____, 20__.

RADIAN ASSET ASSURANCE INC.

By: _____
Name: [ANALYST]
Title: [TITLE]

In the event the insurer becomes insolvent, any claims arising under this policy are excluded from coverage by the California Insurance Guaranty Association, established pursuant to Article 15.2 (commencing with Section 1063) of Chapter 1 of Part 2 of Division 1 of the California Insurance Code.

This policy is not covered by the Property/Casualty Insurance Security Fund established by Article 76 of the New York Insurance Law.

