

NEW ISSUE-BOOK ENTRY ONLY

NOT RATED

(See "CONCLUDING INFORMATION - No Rating on the Bonds" herein)

In the opinion of Fulbright & Jaworski L.L.P., Los Angeles, California, Bond Counsel, under existing law interest on the Bonds is exempt from personal income taxes of the State of California 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 (the "Code") from the gross income of the owners thereof for federal income tax purposes and is not an item of preference under section 57(a) of the Code for purposes of the federal alternative minimum tax. See, however, "LEGAL MATTERS - Tax Exemption" herein regarding certain other tax considerations.

COUNTY OF RIVERSIDE

STATE OF CALIFORNIA



\$23,460,000

CITY OF LAKE ELSINORE

COMMUNITY FACILITIES DISTRICT NO. 2004-3

(ROSETTA CANYON) SPECIAL TAX BONDS

(IMPROVEMENT AREA NO. 2) 2006 SERIES A

Dated: Date of Delivery

Due: September 1, As Shown Below

This cover page contains certain information for quick reference only. It is not a summary of the issue. Potential investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision. Investment in the Bonds involves risks. See "BONDOWNERS' RISKS" herein for a discussion of special risk factors that should be considered in evaluating the investment quality of the Bonds.

Interest on the Bonds is payable semiannually on March 1 and September 1 of each year, commencing March 1, 2007, until maturity or earlier redemption (see "THE BONDS - General Provisions" and "THE BONDS - Redemption" herein).

The information contained within this Official Statement was prepared under the direction of the City by the following firm serving as Financing Consultant to the City.



Rod Gunn Associates, Inc.

MATURITY SCHEDULE

\$3,510,000 SERIAL BONDS

<u>Maturity Date</u> <u>September 1</u>	<u>Principal</u> <u>Amount</u>	<u>Interest</u> <u>Rate</u>	<u>Reoffering</u> <u>Rate</u>	<u>Maturity Date</u> <u>September 1</u>	<u>Principal</u> <u>Amount</u>	<u>Interest</u> <u>Rate</u>	<u>Reoffering</u> <u>Rate</u>
2008	\$30,000	4.000%	4.000%	2015	\$250,000	4.700%	4.850%
2009	55,000	4.150%	4.150%	2016	290,000	4.750%	4.900%
2010	80,000	4.250%	4.250%	2017	335,000	5.000%	5.000%
2011	110,000	4.375%	4.375%	2018	380,000	5.000%	5.050%
2012	145,000	4.500%	4.500%	2019	430,000	5.000%	5.070%
2013	175,000	4.500%	4.650%	2020	480,000	5.000%	5.090%
2014	210,000	4.600%	4.750%	2021	540,000	5.000%	5.110%

\$3,665,000 5.200% Term Bond due September 1, 2026, Price 100%

\$16,285,000 5.250% Term Bond due September 1, 2037, Price 100%

The Bonds will be issued under the Mello-Roos Community Facilities Act of 1982, as amended (Section 53311 *et seq.* of the Government Code of the State of California). Repayment of the Bonds will be from Special Taxes (as defined herein) to be levied within Improvement Area No. 2 of the City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon) and certain other funds held under the Fiscal Agent Agreement, as described herein (see "SOURCES OF PAYMENT FOR THE BONDS" and "BONDOWNERS' RISKS" herein). It is anticipated that the Bonds, in book-entry form, will be available for delivery through the facilities of The Depository Trust Company on or about September 19, 2006 (see "THE BONDS - General Provisions - Book-Entry-Only System" herein).

The date of the Official Statement is September 7, 2006.



**CITY OF LAKE ELSINORE
COMMUNITY FACILITIES DISTRICT NO. 2004-3
(ROSETTA CANYON)**

CITY COUNCIL

Robert Magee, *Mayor*
Robert Schiffner, *Mayor Pro Tem*
Genie Kelley, *Council Member*
Thomas Buckley, *Council Member*
Daryl Hickman, *Council Member*

CITY STAFF

Robert Brady, *City Manager*
Matt N. Pressey, *Director of Administrative Services*
Frederick Ray, *City Clerk*

PROFESSIONAL SERVICES

Bond Counsel and Disclosure Counsel

Fulbright & Jaworski L.L.P.
Los Angeles, California

City Attorney

Leibold, McClendon & Mann, P.C.
Laguna Hills, California

Financing Consultant

Rod Gunn Associates, Inc.
Huntington Beach, California

Fiscal Agent

Union Bank of California, N.A.
Los Angeles, California

Underwriter

Southwest Securities, Inc.
Newport Beach, California

Underwriter's Counsel

McFarlin & Anderson LLP
Lake Forest, California

Special Tax Consultant

Harris & Associates
Irvine, California

Appraiser

Harris Realty Appraisal
Newport Beach, California

Market Absorption Consultant

Empire Economics, Inc.
Capistrano Beach, California

FOR ADDITIONAL INFORMATION

Matt Pressey, City of Lake Elsinore (951) 674-3124
Southwest Securities, Inc. (949) 717-2000

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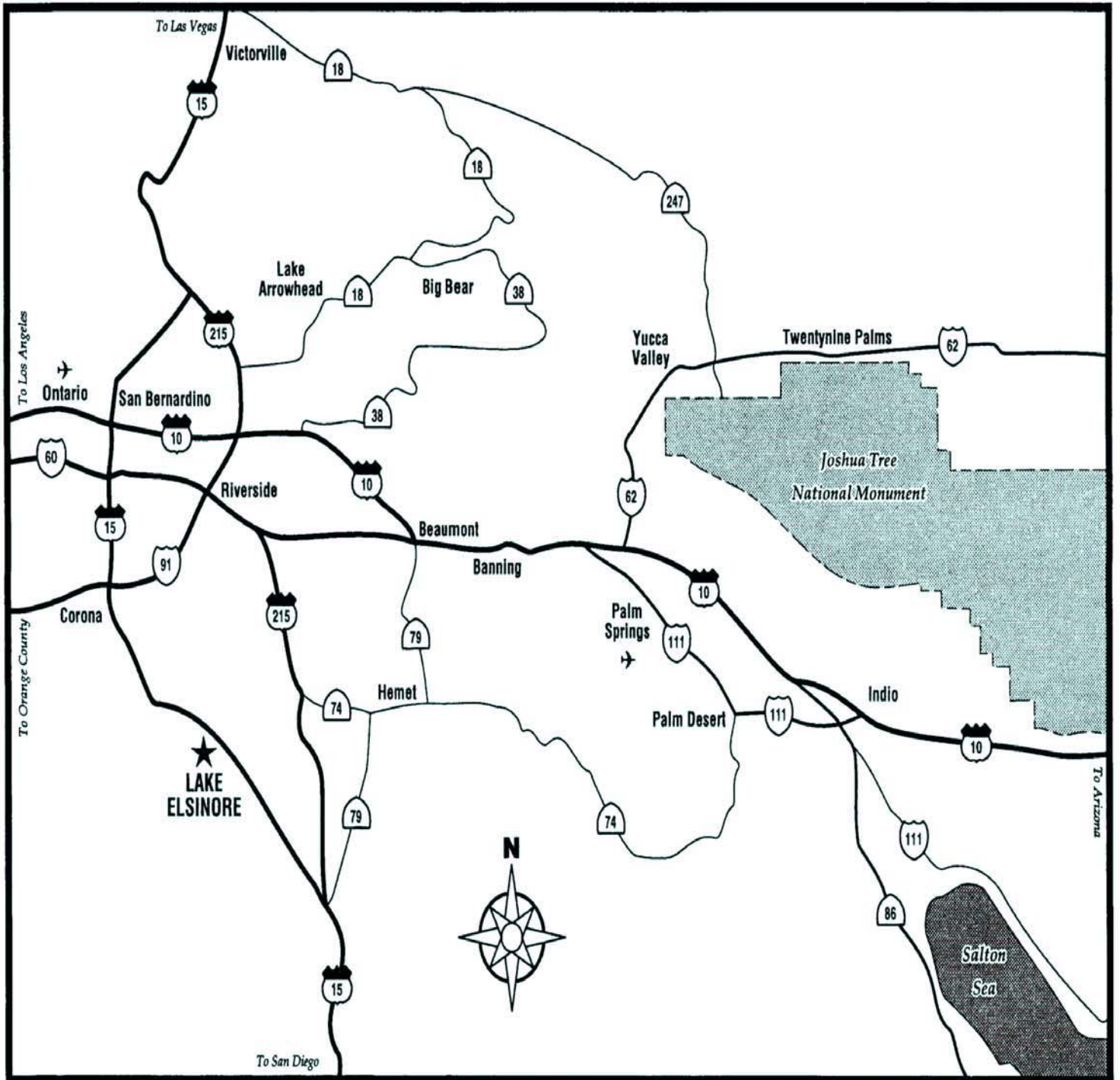
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Lake Elsinore Vicinity Map



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OFFICIAL STATEMENT

\$23,460,000

CITY OF LAKE ELSINORE COMMUNITY FACILITIES DISTRICT NO. 2004-3 (ROSETTA CANYON) SPECIAL TAX BONDS (IMPROVEMENT AREA NO. 2) 2006 SERIES A

This Official Statement which includes the cover page and appendices (the “Official Statement”) is provided to furnish certain information concerning the sale of the City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon) Special Tax Bonds (Improvement Area No. 2) 2006 Series A (the “Bonds”), in the aggregate principal amount of \$23,460,000.

INTRODUCTORY STATEMENT

*This Introductory Statement contains only a brief description of this issue and does not purport to be complete. This Introductory Statement is subject in all respects to more complete information in the entire Official Statement and the offering of the Bonds to potential investors is made only by means of the entire Official Statement and the documents summarized herein. Investment in the Bonds involves risks. Potential investors must read the entire Official Statement to obtain information essential to the making of an informed investment decision with respect to the Bonds (see “**BONDOWNERS’ RISKS**” herein).*

The City and the District

The City. The City of Lake Elsinore (the “City”) was founded in 1883 and incorporated on April 23, 1888 in San Diego County. In 1893 the Elsinore Valley, previously in San Diego County, became a part of the new County of Riverside (the “County”). The City encompasses approximately 39 square miles, with over 10 miles of lake shore, and is located at the southwestern end of Riverside County. It is 73 miles east of downtown Los Angeles and 74 miles north of downtown San Diego. Neighboring communities include Canyon Lake, Murrieta and Temecula (see “**Vicinity Map**” herein).

The District. The Mello-Roos Community Facilities Act of 1982, as amended, constituting Section 53311 *et seq.* of the Government Code of the State of California (the “Act”), was enacted by the California Legislature to provide an alternative method of financing certain public facilities, improvements and services. The Act authorizes local governmental entities to establish community facilities districts as legally constituted governmental entities within defined boundaries, with the legislative body of the local applicable governmental entity acting on behalf of such district. Subject to approval by at least a two-thirds vote of the votes cast by qualified electors within such district and compliance with the provisions of the Act, the legislative body may issue bonds for such community facilities district established by it and may levy and collect a special tax within such district to repay such bonds (see “**SELECTED FACTS**” and “**SPECIAL TAXES AND DEBT SERVICE**” herein).

On March 22, 2005 the City formed City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon) (the “District”). The District consists of two improvement areas (each an “Improvement Area” and collectively the “Improvement Areas”). Each Improvement Area has a separate rate and method of apportionment approved by the qualified electors within each respective Improvement Area. The qualified electors within each Improvement Area voted in favor of the incurrence of bonded indebtedness and each Improvement Area has separate bond authorizations.

On March 22, 2005, the qualified electors within Improvement Area No. 2 approved the tax levy of the Special Tax (the "Special Tax") in accordance with the rate and method of apportionment for Improvement Area No. 2 (the "Rate and Method of Apportionment") and approved issuance of bonds by the District (see "**APPENDIX E - RATE AND METHOD OF APPORTIONMENT**" herein). The Bonds are not secured by Special Taxes levied in the other Improvement Area within the District. On June 27, 2006, change proceedings were conducted to amend the Rate and Method of Apportionment and to increase the bond authorization amount. The bond authorization amount for Improvement Area No. 2 approved by the qualified electors is \$33,000,000. After issuance of the Bonds, the District expects to issue one or more additional series of bonds secured by Special Taxes levied in Improvement Area No. 2 to finance facilities related to Improvement Area No. 2 as described herein (see "**THE BONDS – Additional Obligations**" and "**IMPROVEMENT AREA NO. 2 – Facilities and Fees to be Financed by the District**" herein).

The boundaries of the District coincide with the development generally known as "Rosetta Canyon." The District is located 1 1/2 miles east of the Interstate 15 freeway and south of Highway 74. Development within Improvement Area No. 2 is planned for 503 single family homes on approximately 153.31 gross acres (the "Development"). Centex Homes, a Nevada general partnership (the "Developer"), currently owns all of the land in Improvement Area No. 2 and is in the process of constructing homes in four different residential communities. As of July 15, 2006, out of the total of 503 lots, 33 were in various stages of construction, 413 were in near finished lot condition and 57 lots were in a blue-top condition. As of July 31, 2006, 59 homes within four communities were sold but escrows have not yet closed. As is common with sales at this stage of development, the sales are subject to a number of contingencies and the Developer can provide no assurance that the current sales will result in closed escrows.

Security and Sources of Repayment

The Bonds. The Bonds are secured under the Fiscal Agent Agreement, dated as of September 1, 2006 (the "Fiscal Agent Agreement"), between the District and Union Bank of California, N.A., Los Angeles, California, as fiscal agent (the "Fiscal Agent") (see "**APPENDIX B - SUMMARY OF THE FISCAL AGENT AGREEMENT**" herein). The District has covenanted in the Fiscal Agent Agreement to levy in each Fiscal Year the Special Taxes on parcels of land pledged to the repayment of the Bonds in an amount sufficient to pay debt service on the Bonds and the administrative expenses subject to the limitation on the Maximum Annual Special Tax that may be levied on such land within Improvement Area No. 2 (see "**IMPROVEMENT AREA NO. 2**" and "**SPECIAL TAXES AND DEBT SERVICE**" for a description of the Special Tax within Improvement Area No. 2) (see "**SOURCES OF PAYMENT FOR THE BONDS**" and "**BONDOWNERS' RISKS**" herein).

The Bonds are special obligations of the District. The Bonds do not constitute a debt or liability of the City, the State of California (the "State") or of any political subdivision thereof, other than the District. The District shall only be obligated to pay the principal of the Bonds, and the interest thereon, from the funds described herein, and neither the faith and credit nor the taxing power of the City, the State or any of its political subdivisions is pledged to the payment of the principal of or the interest on the Bonds. See "SOURCES OF PAYMENT FOR THE BONDS" and "BONDOWNERS' RISKS" herein.

Purpose

The Bonds. The Bonds are being issued to provide the District with funds to finance public infrastructure, including certain capital fees imposed by the City and the Elsinore Valley Municipal Water District, related to Improvement Area No. 2 (the "Facilities") (see "**IMPROVEMENT AREA NO. 2 – Facilities and Fees to be Financed by the District**"), to fund interest on the Bonds to and including September 1, 2007, to pay the expenses of the District and the Developer in connection with issuance of the Bonds and to make a deposit to the Reserve Account. The amount of the deposit into the Reserve Account will be in the amount equal to \$2,085,898.99 (see "**ESTIMATED SOURCES AND USES OF FUNDS**" herein).

The Bonds

Redemption. The Bonds maturing September 1, 2026 and September 1, 2037 are subject to mandatory redemption, without premium, prior to their maturity date, in part by lot on September 1 in each year commencing September 1, 2022 in the case of the Bonds maturing September 1, 2026 and September 1, 2027 in the case of the Bonds maturing September 1, 2037 from mandatory sinking fund payments under the Fiscal Agent Agreement (see “**THE BONDS - Redemption – Mandatory Sinking Payment Redemption**” herein).

The Bonds are subject to optional redemption prior to maturity, in whole or in part, by lot, on September 1, 2008, and on any date thereafter at a redemption price equal to the principal amount thereof, plus accrued interest to the date of redemption, plus a premium, as described herein (see “**THE BONDS - Redemption - Optional Redemption**” herein).

The Bonds are subject to redemption, in part, on any date from amounts constituting prepayments of Special Taxes at a redemption price equal to the principal amount thereof, plus accrued interest to the date of redemption, plus a premium, as described herein (see “**THE BONDS - Redemption – Special Mandatory Redemption from Prepayment of Special Taxes**” herein).

The Bonds are subject to special mandatory redemption in whole or in part, on any date without premium under certain other circumstances as described herein (see “**THE BONDS – Redemption**” herein).

Denominations. The Bonds will be issued in the minimum denomination of \$5,000 each or any integral multiple thereof (see “**THE BONDS - General Provisions**” herein).

Registration, Transfer and Exchange. The Bonds will be issued in fully-registered form without coupons. Any Bond may, in accordance with its terms, be transferred or exchanged, pursuant to the provisions of the Fiscal Agent Agreement (see “**THE BONDS - General Provisions - Transfer or Exchange of Bonds**” herein). When delivered, the Bonds will be registered in the name of The Depository Trust Company, New York, New York (“DTC”), or its nominee. DTC will act as securities depository for the Bonds. Individual purchases of Bonds will be made in book-entry form only in the principal amount of \$5,000 each or any integral thereof. Purchasers of the Bonds will not receive certificates representing their Bonds (see “**THE BONDS - General Provisions - Book-Entry-Only System**” herein).

Payment. Principal of the Bonds and any premium upon redemption will be payable in each of the years and in the amounts set forth on the cover page hereof upon surrender at the corporate trust office of the Fiscal Agent in Los Angeles, California. Interest on the Bonds will be paid by check of the Fiscal Agent mailed by first class mail on the Interest Payment Date to the person entitled thereto (except as otherwise described herein for interest paid to an account in the continental United States of America by wire transfer as requested in writing no later than the applicable Record Date by owners of \$1,000,000 or more in aggregate principal amount of Bonds) (see “**THE BONDS - General Provisions**” herein).

Initially, interest on and principal and premium, if any, of the Bonds will be payable when due by wire of the Fiscal Agent to DTC which will in turn remit such interest, principal and premium, if any, to DTC Participants (as defined herein), which will in turn remit such interest, principal and premium, if any, to Beneficial Owners (as defined herein) of the Bonds (see “**THE BONDS - General Provisions - Book-Entry-Only System**” herein).

Notice. Notice of any redemption will be mailed by first class mail by the Fiscal Agent at least thirty (30) but no more than sixty (60) days prior to the date fixed for redemption to the registered owners of any Bonds designated for redemption and to the Securities Depositories and Information Services provided in the Fiscal Agent Agreement. Neither failure to receive such notice nor any defect in the notice so mailed will affect the sufficiency of the proceedings for redemption of such Bonds or the cessation of accrual of interest on the redemption date (see “**THE BONDS - Redemption - Notice of Redemption**” herein).

Legal Matters

The legal proceedings in connection with the issuance of the Bonds are subject to the approving opinion of Fulbright & Jaworski L.L.P., Los Angeles, California, as Bond Counsel. Such opinion, and certain tax consequences incident to the ownership of the Bonds, including certain exceptions to the tax treatment of interest, are described more fully under the heading “LEGAL MATTERS” herein. Certain legal matters will be passed on for the City by Leibold, McClendon & Mann, P.C., Laguna Hills, California, as City Attorney and by Fulbright & Jaworski L.L.P., Los Angeles, California, Disclosure Counsel. Certain legal matters will be passed on for the Underwriter by McFarlin & Anderson LLP, Lake Forest, California, Underwriter’s Counsel.

Professional Services

Union Bank of California, N.A., Los Angeles, California, will serve as Fiscal Agent under the Fiscal Agent Agreement. The Fiscal Agent will act on behalf of the Bondowners for the purpose of receiving all moneys required to be paid to the Fiscal Agent, to allocate, use and apply the same, to hold, receive and disburse the Special Taxes and other funds held under the Fiscal Agent Agreement, and otherwise to hold all the offices and perform all the functions and duties provided in the Fiscal Agent Agreement to be held and performed by the Fiscal Agent.

Harris & Associates, Irvine, California, Special Tax Consultant, prepared the cash flow certificate for the District demonstrating that there will be sufficient Special Taxes, assuming timely receipt, to pay debt service on the Bonds (see “CONCLUDING INFORMATION – Experts” herein).

Rod Gunn Associates, Inc., Huntington Beach, California, Financing Consultant, advised the City as to the financial structure and certain other financial matters relating to the Bonds.

Fees payable to Bond Counsel, Disclosure Counsel, Underwriter’s Counsel and the Financing Consultant are contingent upon the sale and delivery of the Bonds.

Offering of the Bonds

Authority for Issuance. The Bonds are to be issued and secured pursuant to the Fiscal Agent Agreement, as authorized by resolution of the City adopted on August 22, 2006. The Bonds are also issued in accordance with the laws of the State, and particularly the Mello-Roos Community Facilities Act of 1982, as amended (Section 53311 *et seq.* of the Government Code of the State).

The Bonds are being sold to Southwest Securities, Inc. (the “Underwriter”) pursuant to a Purchase Contract approved by the City by Resolution adopted on August 22, 2006.

Offering and Delivery of the Bonds. The Bonds are offered when, as and if issued, subject to the approval as to their legality by Fulbright & Jaworski L.L.P., Los Angeles, California, as Bond Counsel. Certain legal matters will be passed upon for the City by Leibold, McClendon & Mann, P.C., Laguna Hills, California, as City Attorney and by Fulbright & Jaworski L.L.P., Los Angeles, California, Disclosure Counsel. Certain legal matters will be passed upon for the Underwriter by McFarlin & Anderson LLP, Lake Forest, California, as Underwriter’s Counsel.

It is anticipated that the Bonds, in book-entry form, will be available for delivery through the facilities of The Depository Trust Company on or about September 19, 2006.

No dealer, broker, salesperson or other person has been authorized by the District, the City, the Financing Consultant or the Underwriter to give any information or to make any representations in connection with the offer or sale of the Bonds described herein, other than as contained in this Official Statement, and if given or made, such other information or representations must not be relied upon as having been authorized by any of the foregoing.

This Official Statement does not constitute an offer to sell nor the solicitation of an offer to buy, nor shall there be any sale of the Bonds by any person in any jurisdiction in which it is unlawful for such person to make such offer, solicitation or sale or to any person to whom it is unlawful to make such offer, solicitation or sale.

IN CONNECTION WITH THE OFFERING OF THE BONDS, 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.

The Bonds are exempt from registration with the Securities and Exchange Commission pursuant to the Securities Act of 1933, as amended. The Bonds have not been registered or qualified under the securities laws of any state.

The Bonds will not be listed on any stock or securities exchange. Neither the Securities and Exchange Commission nor any other federal, state or other governmental entity or agency will have passed upon the accuracy or adequacy of the Official Statement or approved the Bonds for sale.

Information Concerning this Official Statement

This Official Statement speaks only as of its date. The information set forth herein has been obtained by the Financing Consultant from the City, the District, the Developer and other sources which are believed to be reliable, but such information is not guaranteed as to accuracy or completeness, nor has it been independently verified and is not to be construed as a representation by the Financing Consultant, the City or the District. 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 a part of, its responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriter does not guarantee the accuracy or completeness of such information. Statements contained in this Official Statement which involve estimates, forecasts or matters of opinion, whether or not expressly so described herein, are intended as such and are not to be construed as representations of fact.

Official Statement Deemed Final. The information set forth herein is in a form deemed final, as of its date, by the District for the purpose of Rule 15c2-12 (as defined below) under the Securities Exchange Act of 1934, as amended. The information and expressions of opinion herein are subject to change without notice and the delivery of this Official Statement shall not, under any circumstances, create any implication that there has been no change in the information or opinions set forth herein or in the affairs of the District since the date hereof.

Continuing Disclosure. The District and the Developer have covenanted for the benefit of owners of the Bonds to provide certain financial information and operating data relating to Improvement Area No. 2 each year. The District has agreed to make such information available not later than 225 days after the end of the City's fiscal year, commencing with fiscal year 2005/06 and the Developer has agreed to make such information available not later than February 15 of each year until the obligation is terminated, commencing February 15, 2007 (each an "Annual Report" and collectively the "Annual Reports"), and to provide notices of the occurrences of certain enumerated events, if material. The District and the Developer shall file or cause to be filed by the Dissemination Agent the Annual Reports 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 Dissemination Agent on behalf of the District and the Developer with the Municipal Securities Rulemaking Board (and with the appropriate State information depository, if any) or each Nationally Recognized Municipal Securities Information Repository. The specific nature of information to be contained in the Annual Reports or the

notice of material events is summarized in “**APPENDIX F -- FORMS OF CONTINUING DISCLOSURE AGREEMENTS.**” These covenants have been made by the District and the Developer in order to assist the Underwriter in complying with Rule 15c2-12(b)(5) (the “Rule”) promulgated by the Securities and Exchange Commission. The Developer will be released from its obligation under its Continuing Disclosure Agreement to provide its Annual Report and notices of material events upon the earliest to occur of certain events, including at such time that the property owned by the Developer in Improvement Area No. 2 is no longer responsible for payment of 20% or more of the Special Taxes in Improvement Area No. 2 in any given fiscal year. The District has never failed to meet its continuing disclosure requirements under such rule in any material manner. An officer or representative executing a certificate on behalf of the Developer will certify that to his or her knowledge, the Developer has not previously failed to comply in any material respect with undertakings by it under the Rule to provide periodic continuing disclosure reports or notice of material events in California within the past five years.

Each year until the final maturity of the Bonds, the District is required to, not later than October 30 of each year, supply the following information to the California Debt and Investment Advisory Commission by mail, postage prepaid:

1. The principal amount of Bonds outstanding.
2. The balance in any Bonds reserve fund.
3. The balance in any capitalized interest fund.
4. The number of parcels which are delinquent with respect to their Special Tax payments, the amount that each parcel is delinquent, the length of time that each has been delinquent, and when foreclosure was commenced for each delinquent parcel.
5. The balance in any construction funds.
6. The assessed value of all parcels subject to Special Tax to repay the Bonds as shown on the most recent equalized roll.

In addition, the District is required to notify the California Debt and Investment Advisory Commission by mail, postage prepaid, within 10 days if any of the following events occur:

1. The District or its Fiscal Agent fails to pay principal and interest due on any scheduled payment date.
2. Funds are withdrawn from any reserve fund to pay principal and interest on the Bonds.

Neither the District nor the California Debt and Investment Advisory Commission will be liable for any inadvertent error in reporting the required information. The failure by the District to comply with its reporting obligations is not a default under the Fiscal Agent Agreement.

Availability of Legal Documents. The summaries and references contained herein with respect to the Fiscal Agent Agreement, the Bonds, and other statutes or documents do not purport to be comprehensive or definitive and are qualified by reference to each such document or statute, and references to the Bonds are qualified in their entirety by reference to the form thereof included in the Fiscal Agent Agreement. Definitions of certain terms used herein are set forth in “**APPENDIX A**” hereto. Copies of the documents described herein are available for inspection during the period of initial offering of the Bonds at the offices of the Underwriter, Southwest Securities, Inc., 620 Newport Center Drive, Suite 300, Newport Beach, California 92660, telephone (949) 717-2000. Copies of these documents may be obtained after delivery of the Bonds from the City at 130 S. Main Street, Lake Elsinore, California 92530, telephone (951) 674-3124.

SELECTED FACTS

*The following summary does not purport to be complete. Reference is hereby made to the complete Official Statement in this regard. Furthermore, the following summary makes certain assumptions regarding valuation of property within Improvement Area No. 2. Neither the City nor the District makes any representation as to the current value of property in Improvement Area No. 2 or provides any assurance as to the estimated values of property being achieved (see “**BONDOWNERS’ RISKS**” herein).*

THE BONDS

Principal Amount of Bonds:	\$23,460,000
Additional Bonds:	Additional bonds on a parity with the Bonds are authorized (see “ THE BONDS – Additional Obligations ” and “ APPENDIX B - SUMMARY OF THE FISCAL AGENT AGREEMENT ” herein).
Maximum Bond Authorization:	\$33,000,000
First Optional Redemption Date:	September 1, 2008 at 103% of Principal Amount (see “ THE BONDS-Redemption ” herein).
First Special Mandatory Redemption Date:	On any date on or after March 1, 2007 from prepayment of Special Taxes at a premium, as described herein.
Primary Source of Revenues for Repayment:	Special Taxes levied within Improvement Area No. 2 as defined herein (see “ SPECIAL TAXES AND DEBT SERVICE ” herein).
Priority:	All Bonds are secured by a first pledge of and lien on all Special Taxes levied within Improvement Area No. 2 (see “ SOURCES OF PAYMENT FOR THE BONDS ” and “ BONDOWNERS’ RISKS ” herein).

IMPROVEMENT AREA NO. 2

Estimated Acreage:	153.31 gross acres
Discounted “Bulk Value” of Parcels in Improvement Area No. 2:	\$78,500,000
Ratio of Market Value to Principal Amount of Bonds:	3.35 to 1
Minimum Ratio of Authorized Maximum Annual Special Taxes in any Fiscal Year to Annual Debt Service on the Bonds:	125%

PROPERTY OWNER AND DEVELOPMENT

Property Owner:	Centex Homes, a Nevada general partnership (see “ BONDOWNERS’ RISKS– Concentration of Ownership ” herein).
Description of Proposed Development:	The Developer expects to construct 503 single family homes in Improvement Area No. 2.
Government Approvals:	Building Permits have been issued on 408 homes within Improvement Area No. 2.
Status of Development:	Out of the total of 503 lots, 33 production homes are in various stages of unit construction, 413 lots were in near finished lot condition and 57 lots were in blue-top condition.
Presales:	59 homes in the 4 communities had presold.
Estimated Absorption Period:	2006 to 2008
Estimated Price Range of Homes:	\$359,990 to \$537,990
Estimated Home Sizes:	1,979 to 4,063 Sq. Ft.

ESTIMATED SOURCES AND USES OF FUNDS

Under the provisions of the Fiscal Agent Agreement, the Fiscal Agent will receive the proceeds from the sale of the Bonds and will apply them as follows:

Sources of Funds

Principal Amount of the Bonds	\$23,460,000.00
Original Issue Discount	(24,745.95)
Underwriter's Discount	<u>(469,200.00)</u>
 Total	 \$22,966,054.05

Uses of Funds

Acquisition and Construction Fund	\$19,350,336.18
Interest Account ⁽¹⁾	1,154,318.88
Reserve Account ⁽²⁾	2,085,898.99
Costs of Issuance Account ⁽³⁾	350,000.00
Administrative Expense Account ⁽⁴⁾	<u>25,500.00</u>
 Total	 \$22,966,054.05

(1) Capitalized interest through September 1, 2007.

(2) Equal to the Reserve Requirement.

(3) Expenses include fees of Bond Counsel, Financing Consultant, Disclosure Counsel, Appraiser, Market Consultant, Special Tax Consultant, Fiscal Agent, costs of printing the Official Statement, and other costs of issuance of the Bonds.

(4) City administration fees, fees and expenses of levying the Special Taxes in the first year

Investment of Funds

All moneys in any of the funds or accounts established with the Fiscal Agent pursuant to the Fiscal Agent Agreement will be invested solely in Authorized Investments (see “**APPENDIX A - DEFINITION OF CERTAIN TERMS USED IN THE FISCAL AGENT AGREEMENT**” herein), as directed pursuant to the Written Request of the District filed with the Fiscal Agent at least two (2) Business Days in advance of the making of such investments. In the absence of any such Written Request, the Fiscal Agent will invest any such moneys in money market funds. Obligations purchased as an investment of moneys in any fund shall be deemed to be part of such fund or account. For the purpose of determining the amount in any fund, the value of Authorized Investments credited to such fund will be calculated at the market thereof (excluding any accrued interest).

THE BONDS

General Provisions

Repayment of the Bonds. Interest is payable on the Bonds at the rates per annum set forth on the cover page hereof. Interest with respect to the Bonds will be computed on the basis of a year consisting of 360 days and twelve 30-day months.

Each Bond will be dated the Delivery Date, and interest with respect thereto will be payable from the Interest Payment Date next preceding the date of authentication thereof, unless (a) it is authenticated after a Record Date and on or before an Interest Payment Date and after the close of business on the preceding Record Date, in which event interest with respect thereto will be payable from such Interest Payment Date; (b) it is authenticated on or before February 15, 2007, in which event interest with respect thereto will be payable from the Delivery Date; or (c) interest with respect to any Outstanding Bond is in default, in which event interest with respect thereto will be payable from the date to which interest has been paid in full, payable on each Interest Payment Date.

Interest with respect to the Bonds will be payable by check of the Fiscal Agent mailed by first class mail on the applicable Interest Payment Date to the Owners thereof provided that in the case of an Owner of \$1,000,000 or greater in principal amount of Outstanding Bonds, such payment may, at such Owner's option, be made by wire transfer of immediately available funds to an account in the United States in accordance with written instructions provided prior to the applicable Record Date to the Fiscal Agent by such Owner. The Owners of the Bonds shown on the Registration Books on the Record Date for the Interest Payment Date will be deemed to be the Owners of the Bonds on said Interest Payment Date for the purpose of the paying of interest. Principal of the Bonds and any premium upon early redemption is payable upon presentation and surrender thereof, at the corporate trust office of the Fiscal Agent in Los Angeles, California.

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

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

DTC, the world's largest securities 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 2.2 million issues of U.S. and non-U.S. equity corporate and municipal debt issues, and money market instruments from over 100 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, Fixed Income Clearing Corporation and Emerging Markets Clearing Corporation, (respectively, "NSCC," "FICC," 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 and www.dtc.org.

Purchases of the Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the Bonds on DTC’s records. The ownership interest of each actual purchaser of each Bond (“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 Bonds are to be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in the Bonds, except in the event that use of the book-entry system for the Bonds is discontinued.

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

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners of the Bonds may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Bonds, such as redemptions, tenders, defaults, and proposed amendments to the Bond documents. For example, Beneficial Owners of the Bonds may wish to ascertain that the nominee holding the Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the registrar and request that copies of notices be provided directly to them.

Redemption notices shall be sent to DTC. If less than all of the Bonds 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.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Bonds 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 the Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal, redemption price, and interest payments on the Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC’s practice is to credit Direct Participants’ accounts upon DTC’s receipt of funds and corresponding detail information from the District or the Fiscal Agent, 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, the Fiscal Agent, or the District, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal, redemption price and interest payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the District or the

Fiscal Agent, 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.

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

The District may decide to discontinue use of the system of book-entry only transfers through DTC (or a successor securities depository). In that event, Bond certificates will be printed and delivered to DTC. In the event that the book-entry system is discontinued as described above, the requirements of the Fiscal Agent Agreement will apply.

The foregoing information concerning DTC and DTC's book-entry system has been provided by DTC, and neither the District nor the Fiscal Agent take any responsibility for the accuracy thereof. Neither the District nor the Underwriter can, and do not, give any assurances that DTC, the Participants or others will distribute payments of principal, interest or premium, if any, evidenced by the Bonds paid to DTC or its nominee as the registered owner, or will distribute any redemption notices or other notices, to the Beneficial Owners, or that they will do so on a timely basis or will serve and act in the manner described in this Official Statement. Neither the District nor the Underwriter is responsible or liable for the failure of DTC or any Participant to make any payment or give any notice to a Beneficial Owner with respect to the Bonds or an error or delay relating thereto.

Transfer or Exchange of Bonds. Any Bond may, in accordance with its terms, be transferred or exchanged, pursuant to the provisions of the Fiscal Agent Agreement, upon surrender of such Bond for cancellation at the corporate trust office of the Fiscal Agent. Whenever any Bond or Bonds shall be surrendered for transfer or exchange, the Fiscal Agent shall authenticate and deliver a new Bond or Bonds for like aggregate principal amount. The Fiscal Agent may require the payment by the Bondowner requesting such transfer or exchange of any tax or other governmental charge required to be paid with respect to such transfer or exchange. The Fiscal Agent is not required to transfer or exchange (a) any Bonds or portions thereof during the period established by the Fiscal Agent for selection of Bonds for redemption, or (b) any Bonds selected for redemption.

Bonds Mutilated, Lost, Destroyed or Stolen. If any Bond becomes mutilated, the District, at the expense of the Bondowner, will execute, and the Fiscal Agent will thereupon authenticate and deliver, a new Bond of like series, tenor and authorized denomination in exchange and substitution for the Bond so mutilated, but only upon surrender to the Fiscal Agent of the Bond so mutilated. Every mutilated Bond so surrendered to the Fiscal Agent will be canceled by it. If any Bond issued under the Fiscal Agent Agreement is lost, destroyed or stolen, evidence of such loss, destruction or theft may be submitted to the Fiscal Agent and the District and, if such evidence is satisfactory to them and indemnity satisfactory to them is given, the District, at the expense of the Bondowner, will execute, and the Fiscal Agent will thereupon authenticate and deliver, a new Bond of like series and tenor in lieu of and in substitution for the Bond so lost, destroyed or stolen. Any Bond issued under the provisions of the Fiscal Agent Agreement described in this paragraph in lieu of any Bond alleged to be lost, destroyed or stolen will be equally and proportionately entitled to the benefits of the Fiscal Agent Agreement with all other Bonds secured by the Fiscal Agent Agreement.

Redemption

Optional Redemption. The Bonds are subject to redemption prior to maturity at the option of the District on any date on or after September 1, 2008 as a whole or in part, by lot, from any available source of funds at the following redemption prices (expressed as a percentage of the principal amount of Bonds to be redeemed), together with accrued interest thereon to the date fixed for redemption:

<u>Redemption Periods</u>	<u>Redemption Prices</u>
September 1, 2008 through August 31, 2009	103.0%
September 1, 2009 through August 31, 2010	102.5%
September 1, 2010 through August 31, 2011	102.0%
September 1, 2011 through August 31, 2012	101.5%
September 1, 2012 through August 31, 2013	101.0%
September 1, 2013 through August 31, 2014	100.5%
September 1, 2014 and thereafter	100.0%

Special Mandatory Redemption from Prepayment of Special Taxes. The Bonds are subject to mandatory redemption prior to maturity on any date on or after March 1, 2007, in whole or in part, in a manner determined by the District from prepayments of Special Taxes at the following redemption prices (expressed as a percentage of the principal amount of Bonds to be redeemed), together with accrued interest thereon to the date fixed for redemption:

<u>Redemption Periods</u>	<u>Redemption Prices</u>
March 1, 2007 through August 31, 2009	103.0%
September 1, 2009 and thereafter	as provided for optional redemption

Mandatory Sinking Payment Redemption. The Bonds maturing on September 1, 2026 and September 1, 2037 are subject to mandatory redemption, in part by lot, on September 1 in each year commencing September 1, 2022 in the case of the Bonds maturing September 1, 2026 and September 1, 2027 in the case of the Bonds maturing September 1, 2037 from mandatory sinking payments made by the District pursuant to the Fiscal Agent Agreement at a redemption price equal to the principal amount thereof to be redeemed, without premium, plus accrued interest thereon to the date of redemption as set forth in the following schedule; provided, however, that (i) in lieu of redemption thereof, the Bonds may be purchased by the District and tendered to the Fiscal Agent, and (ii) if some but not all of the Bonds have been redeemed pursuant to optional redemption, mandatory redemption from Special Taxes or special mandatory redemption provisions described herein, the total amount of all future sinking payments will be reduced by the aggregate principal amount of the Bonds so redeemed, to be allocated among such sinking payments on a pro rata basis (as nearly as practicable) in integral multiples of \$5,000 as determined by the District.

**SCHEDULE OF MANDATORY SINKING PAYMENT REDEMPTIONS
TERM BONDS MATURING SEPTEMBER 1, 2026**

<u>September 1 Year</u>	<u>Principal Amount</u>	<u>September 1 Year</u>	<u>Principal Amount</u>
2022	\$595,000	2025	\$800,000
2023	660,000	2026	880,000 (maturity)
2024	730,000		

**SCHEDULE OF MANDATORY SINKING PAYMENT REDEMPTIONS
TERM BONDS MATURING SEPTEMBER 1, 2037**

<u>September 1</u> <u>Year</u>	<u>Principal</u> <u>Amount</u>	<u>September 1</u> <u>Year</u>	<u>Principal</u> <u>Amount</u>
2027	\$960,000	2033	\$1,565,000
2028	1,045,000	2034	1,685,000
2029	1,135,000	2035	1,815,000
2030	1,235,000	2036	1,955,000
2031	1,340,000	2037	2,100,000 (maturity)
2032	1,450,000		

Special Mandatory Redemption.

The Bonds are subject to special mandatory redemption on any date from unused proceeds of the Bonds after completion or abandonment of the improvements to be financed with such proceeds, from the deposit of fees with the District by a public agency which has accepted facilities serving the District, and from insurance or condemnation proceeds or other mandatory redemption, without premium, plus accrued interest to the redemption date, all as determined by the District (see “**IMPROVEMENT AREA NO. 2 – Facilities and Fees to be Financed by the District**” for a description of the scope of the Development).

Notice of Redemption. When redemption is authorized or required, the Fiscal Agent is required to give written notice of the redemption of Bonds to the Bondowners designated for redemption at their addresses appearing on the bond registration books, to certain Securities Depositories, and to one or more Information Services, all as provided in the Fiscal Agent Agreement, by first class mail, postage prepaid, no less than thirty (30), nor more than sixty (60), days prior to the date fixed for redemption. Neither failure to receive such notice nor any defect in the notice so mailed will affect the sufficiency of the proceedings for redemption of such Bonds or the cessation of accrual of interest on the redemption date.

Effect of Redemption. The rights of a Bondowner to receive interest will terminate on the date, if any, on which the Bond is to be redeemed pursuant to a call for redemption. The Fiscal Agent Agreement contains no provisions requiring any publication of notice of redemption, and Bondowners must maintain a current address on file with the Fiscal Agent to receive any notices of redemption.

Partial Redemption. In the event only a portion of any Bond is called for redemption, then upon surrender of such Bond the District will execute and the Fiscal Agent will authenticate and deliver to the Bondowner thereof, at the expense of the District, a new Bond or Bonds of the same series and maturity date, of authorized denominations in an aggregate principal amount equal to the unredeemed portion of the Bond to be redeemed.

Additional Obligations

The qualified electors within Improvement Area No. 2 authorized bonded indebtedness in the amount of \$33,000,000. Pursuant to the provisions of the Fiscal Agent Agreement, the District is authorized to issue additional parity bonds for Improvement Area No. 2 and currently expects to issue additional parity bonds to finance additional facilities (see “**IMPROVEMENT AREA NO. 2 – Facilities and Fees to be Financed by the District**” herein).

Parity Bonds. The District covenants that any Parity Bonds which shall be issued or incurred which are payable out of the Special Taxes of the Improvement Area No. 2 in whole or in part shall be issued in accordance with the following:

(a) the amount of such Parity Bonds shall not, together with all other Bonds and Parity Bonds then Outstanding with respect to the Improvement Area No. 2, exceed the total amount of Bonds authorized to be issued by the District with respect to Improvement Area No. 2;

(b) The District shall be in compliance with all covenants set forth in the Fiscal Agent Agreement and a certificate of the District to that effect shall have been filed with the City Clerk on behalf of the District; provided, however, that Parity Bonds may be issued notwithstanding that the District is not in compliance with all such covenants so long as immediately following the issuance of such Parity Bonds for Improvement Area No. 2 the District will be in compliance with all such covenants; and

(c) The District shall have received the following documents or money or securities, all of such documents dated or certified, as the case may be, as of the date of delivery of such Parity Bonds by the Fiscal Agent (unless the Fiscal Agent shall accept any of such documents bearing a prior date):

(1) An opinion of Bond Counsel and/or counsel to the District to the effect that (a) the District has the right and power under the Act to execute and deliver the Supplemental Fiscal Agent Agreement relating to such Parity Bonds, and the Fiscal Agent Agreement and all such Supplemental Fiscal Agent Agreements have been duly and lawfully adopted, executed and delivered by the District, are in full force and effect and are valid and binding upon the District 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) the Fiscal Agent Agreement creates the valid pledge which it purports to create of the Special Taxes of Improvement Area No. 2 as provided in the Fiscal Agent Agreement, subject to the application thereof to the purposes and on the conditions permitted by the Fiscal Agent Agreement; and (c) such Parity Bonds are valid and binding limited obligations of the District, enforceable in accordance with their terms (except as enforcement may be limited by bankruptcy, insolvency, reorganization and other similar laws relating to the enforcement or creditors' rights) and the terms of the Fiscal Agent Agreement and all Supplemental Fiscal Agent Agreements thereto and entitled to the benefits of the Fiscal Agent Agreement and all such Supplemental Fiscal Agent Agreements, and such Parity Bonds have been duly and validly authorized and issued in accordance with the Act (or other applicable laws) and the Fiscal Agent Agreement and all such Supplemental Fiscal Agent Agreements and further opinion of Bond Counsel to the effect that, assuming compliance by the District with certain tax covenants, the issuance of the Parity Bonds will not adversely affect the exclusion from gross income for federal income tax purposes of interest on any Outstanding Bonds and Parity Bonds theretofore issued or the exemption from State of California personal income taxation of interest on any Outstanding Bonds and Parity Bonds theretofore issued; and

(2) A certificate from one or more Independent Financial Consultants which, when taken together, certify that (i) the amount of the maximum Special Taxes that may be levied by the CFD pursuant to the Act and the applicable resolutions and ordinances of the CFD in each subsequent Fiscal Year on properties that have building permits issued is at least 1.10 times the corresponding Annual Debt Service for each remaining Bond Year on all Outstanding Bonds theretofore issued and the Parity Bonds proposed to be issued, and (ii) the value of all parcels of real property in the CFD subject to the levy of the Special Tax and not delinquent in the payment of any Special Taxes due and owing, as determined based on an appraisal performed on a basis generally consistent with the appraisal conducted in connection with the issuance of the Bonds or based on assessed value, is at least 3 times the sum of (a) the aggregate principal amount of all Bonds and Parity Bonds then Outstanding, plus (b) the aggregate principal amount of the series of Parity Bonds proposed to be issued, plus (c) the aggregate principal amount of any fixed assessment liens on the parcels in Improvement Area No. 2, plus (d) a portion of the aggregate principal amount of any and all other community facilities district bonds then outstanding and payable at least partially from special taxes to be levied on parcels of property within Improvement Area No. 2 (the "Other CFD Bonds") equal to the aggregate principal amount of the Other CFD Bonds multiplied by a fraction, the numerator of which is the amount of special taxes levied for the Other CFD Bonds on parcels of property within Improvement Area No. 2, and the denominator of which is the total amount of special taxes levied for the Other CFD Bonds on all parcels of property which are subject to the levy of such special taxes are levied to pay the Other CFD Bonds (such fraction to be determined

based upon the maximum special taxes which could be levied in the year in which maximum annual debt service on the Other CFD Bonds occurs), based upon information which is available for the then current Fiscal Year. For purposes of making the certifications required by this paragraph, the Independent Financial Consultants may rely on reports or certificates of such other persons as may be acceptable to the CFD, the City, Bond Counsel and the Underwriter of the proposed Parity Bonds.

Scheduled Debt Service on the Bonds

The following is the scheduled debt service on the Bonds.

<u>Interest Payment Date</u>	<u>Principal</u>	<u>Interest</u>	<u>Annual Debt Service</u>
March 1, 2007		\$546,782.63	
September 1, 2007		607,536.25	\$1,154,319
March 1, 2008		607,536.25	
September 1, 2008	\$30,000	607,536.25	1,245,073
March 1, 2009		606,936.25	
September 1, 2009	55,000	606,936.25	1,268,873
March 1, 2010		605,795.00	
September 1, 2010	80,000	605,795.00	1,291,590
March 1, 2011		604,095.00	
September 1, 2011	110,000	604,095.00	1,318,190
March 1, 2012		601,688.75	
September 1, 2012	145,000	601,688.75	1,348,378
March 1, 2013		598,426.25	
September 1, 2013	175,000	598,426.25	1,371,853
March 1, 2014		594,488.75	
September 1, 2014	210,000	594,488.75	1,398,978
March 1, 2015		589,658.75	
September 1, 2015	250,000	589,658.75	1,429,318
March 1, 2016		583,783.75	
September 1, 2016	290,000	583,783.75	1,457,568
March 1, 2017		576,896.25	
September 1, 2017	335,000	576,896.25	1,488,793
March 1, 2018		568,521.25	
September 1, 2018	380,000	568,521.25	1,517,043
March 1, 2019		559,021.25	
September 1, 2019	430,000	559,021.25	1,548,043
March 1, 2020		548,271.25	
September 1, 2020	480,000	548,271.25	1,576,543
March 1, 2021		536,271.25	
September 1, 2021	540,000	536,271.25	1,612,543
March 1, 2022		522,771.25	
September 1, 2022	595,000	522,771.25	1,640,543
March 1, 2023		507,301.25	
September 1, 2023	660,000	507,301.25	1,674,603
March 1, 2024		490,141.25	
September 1, 2024	730,000	490,141.25	1,710,283
March 1, 2025		471,161.25	
September 1, 2025	800,000	471,161.25	1,742,323
March 1, 2026		450,361.25	
September 1, 2026	880,000	450,361.25	1,780,723
March 1, 2027		427,481.25	
September 1, 2027	960,000	427,481.25	1,814,963
March 1, 2028		402,281.25	
September 1, 2028	1,045,000	402,281.25	1,849,563
March 1, 2029		374,850.00	
September 1, 2029	1,135,000	374,850.00	1,884,700

Scheduled Debt Service Continued

<u>Interest Payment Date</u>	<u>Principal</u>	<u>Interest</u>	<u>Annual Debt Service</u>
March 1, 2030		345,056.25	
September 1, 2030	\$1,235,000	345,056.25	\$1,925,113
March 1, 2031		312,637.50	
September 1, 2031	1,340,000	312,637.50	1,965,275
March 1, 2032		277,462.50	
September 1, 2032	1,450,000	277,462.50	2,004,925
March 1, 2033		239,400.00	
September 1, 2033	1,565,000	239,400.00	2,043,800
March 1, 2034		198,318.75	
September 1, 2034	1,685,000	198,318.75	2,081,638
March 1, 2035		154,087.50	
September 1, 2035	1,815,000	154,087.50	2,123,175
March 1, 2036		106,443.75	
September 1, 2036	1,955,000	106,443.75	2,167,888
March 1, 2037		55,125.00	
September 1, 2037	2,100,000	55,125.00	2,210,250

SOURCES OF PAYMENT FOR THE BONDS

General

The principal of, premium, if any, and the interest on the Bonds, and the Administrative Expenses, are payable from the Special Taxes collected on real property within Improvement Area No. 2 and certain funds held by the Fiscal Agent and available for such purposes pursuant to the Fiscal Agent Agreement.

The Bonds are limited obligations of the District payable solely from the proceeds of Special Taxes levied on certain parcels within Improvement Area No. 2. The Bonds shall not be deemed to constitute a debt or liability of the City or the State or of any political subdivision thereof, other than the District. Neither the faith and credit nor the taxing power of the City, the State or any of its political subdivisions is pledged to the payment of the principal of or the interest on the Bonds.

Special Taxes

The Special Taxes are excepted from the tax limitation of California Constitution Article XIII A pursuant to Section 4 thereof as a “special tax” authorized by at least a two-thirds vote of the qualified electors as set forth in the Act. Consequently, the City Council (the “City Council”) of the City on behalf of the District has the power and is obligated by the Fiscal Agent Agreement to cause the levy and collection of the Special Taxes.

The District has covenanted in the Fiscal Agent Agreement to levy (subject to the Maximum Annual Special Tax) in each Fiscal Year the Special Taxes in an amount sufficient to pay the debt service on the Bonds and the cost of providing Administrative Expenses.

The Special Taxes are to be levied and collected according to the Rate and Method of Apportionment described in the section entitled “SPECIAL TAXES AND DEBT SERVICE” herein.

Although the Special Taxes will constitute a lien on parcels of real property within Improvement Area No. 2, they do not constitute a personal indebtedness of the owner(s) of real property. There is no assurance that the property owner(s), or any successors and/or assigns thereto or subsequent purchaser(s) of land within Improvement Area No. 2, will be able to pay the annual Special Taxes or if able to pay the Special Taxes that they will do so (see “BONDOWNERS’ RISKS” and “IMPROVEMENT AREA NO. 2” herein).

The Special Taxes initially are required to be collected by the County of Riverside Tax Collector in the same manner and at the same time as regular *ad valorem* property taxes are collected by the Tax Collector of the County. When received, such Special Taxes will be deposited in the Special Tax Fund to be held by the Fiscal Agent as provided in the Fiscal Agent Agreement.

Reserve Account

In order to secure further the timely payment of principal of and interest on the Bonds, the District is required, upon delivery of the Bonds, to deposit in the Reserve Account for the Bonds an amount equal to the Reserve Requirement. The Reserve Requirement means, as of any date of calculation, an amount equal to the lowest of (1) 10% of the issue price (as defined pursuant to section 148 of the Code), or (2) Maximum Annual Debt Service, or (3) 125% of the average Annual Debt Service of the Outstanding Bonds. Thereafter, the District is required to deposit from the payment of the Bonds and maintain an amount of money equal to the Reserve Requirement in the Reserve Account at all times while the Bonds are Outstanding. The amount of the deposit into the Reserve Account will be in the amount equal to \$2,085,898.99. Amounts in the Reserve Account will be used to pay debt service on the Bonds to the extent other moneys are not available therefor. Amounts in the Reserve Account in excess of the Reserve Requirement will be deposited into the Acquisition and Construction Fund until all Facilities have been financed or it is determined sufficient funds are on deposit in the Acquisition and Construction Fund to fund all Facilities expected to be funded and thereafter such excess funds shall be deposited into the

Interest Account. Amounts in the Reserve Account may be used to pay the final year's debt service on the Bonds (see "APPENDIX B - SUMMARY OF THE FISCAL AGENT AGREEMENT" herein). Upon mandatory redemption, amounts on deposit in the Reserve Account shall be reduced (to an amount not less than the Reserve Requirement) and excess money shall be transferred to the Redemption Account and used for the redemption of Bonds.

Capitalized Interest

There will be an initial deposit to the Interest Account out of Bond proceeds which has been calculated to be sufficient to make interest payments on the Bonds due to and including September 1, 2007.

Covenant for Superior Court Foreclosure

Pursuant to Section 53356.1 of the Act, in the event of a delinquency in the payment of the Special Taxes levied, the District may order the institution of a superior court action to foreclose the lien therefor, provided such action is brought not later than four years after the final maturity date of the Bonds. In such an action, the real property subject to the unpaid amount may be sold at a judicial foreclosure sale.

The District has covenanted in the Fiscal Agent Agreement for the benefit of the owners of the Bonds that the District will determine or cause to be determined, no later than March 1 and August 1 of each year, whether or not any owners of the property within Improvement Area No. 2 of the District are delinquent in the payment of Special Taxes and, if such delinquencies exist, the District will order and cause to be commenced not later than April 15 (with respect to the March 1 determination date) or September 1 (with respect to the August 1 determination date), and thereafter diligently prosecute, an action in the superior court to foreclose the lien of any Special Taxes or installment thereof not paid when due, provided, however, that the District shall not be required to order the commencement of foreclosure proceedings if (i) the total Special Tax delinquency of Improvement Area No. 2 for such Fiscal Year is less than five percent (5%) of the total Special Tax levied in such Fiscal Year, and (ii) the District shall have established from any source of lawfully available funds (other than Special Taxes) an escrow fund to provide for the payment of principal of and interest on the Bonds. Notwithstanding the foregoing, if the District determines that any single property owner is delinquent in excess of ten thousand dollars (\$10,000) in the payment of the Special Tax, then it will diligently institute, prosecute and pursue foreclosure proceedings against such property owner. Notwithstanding any provision of the Act or other law of the State to the contrary, in connection with any foreclosure related to delinquent Special Taxes:

(a) The District or the Fiscal Agent is authorized to credit bid at any foreclosure sale, without any requirement that funds be set aside in the amount so credit bid, in the amount specified in Section 53356.5 of the Act, or such less amount as determined under clause (b) below or otherwise under Section 53356.6 of the Act.

(b) The District may permit, in its sole and absolute discretion, property with delinquent Special Tax payments to be sold for less than the amount specified in Section 53356.5 of the Act, if it determines that such sale is in the interest of the Bond Owners. The Bond Owners, by their acceptance of the Bonds, consent to such sale for such lesser amounts (as such consent is described in Section 53356.6 of the Act), and release the District and the City, and their respective officers and agents from any liability in connection therewith. If such sale for lesser amounts would result in less than full payment of principal of and interest on the Bonds, the CFD will use best efforts to seek approval of the Bond Owners.

(c) The District is authorized to use amounts in the Special Tax Fund to pay costs of foreclosure of delinquent Special Taxes.

(d) The District may forgive all or any portion of the Special Taxes levied or to be levied on any parcel in Improvement Area No. 2 so long as the District determines that such forgiveness is not expected to adversely affect its obligation to pay principal of and interest on the Bonds as such payments become due and payable.

No assurances can be given that the real property subject to foreclosure and sale at a judicial foreclosure sale will be sold or, if sold, that the proceeds of such sale will be sufficient to pay any delinquent Special

Tax installment. Although the Act authorizes the District to cause such an action to be commenced and diligently pursued to completion, the Act does not require the District or the City to purchase or otherwise acquire any lot or parcel of property sold at the execution sale pursuant to the judgment in any such action if there is no other purchaser at such sale, nor does the Act specify the priority relationship, if any, between the Special Taxes and other taxes and assessment liens.

As a result of the foregoing, in the event of a delinquency or nonpayment by the property owners in Improvement Area No. 2 of one or more Special Taxes installments, there can be no assurance that there would be available to the District sufficient funds to pay when due the principal of, interest on and premium, if any, on the Bonds (see **“BONDOWNERS’ RISKS - Concentration of Ownership,” “BONDOWNERS’ RISKS - Bankruptcy and Foreclosure Delays”** and **“BONDOWNERS’ RISKS - Property Controlled by Federal Deposit Insurance Corporation and other Federal Agencies”** herein).

Prepayment of Special Tax.

A property owner may prepay its Special Taxes and thereby cause a redemption of Bonds. See **“APPENDIX E – RATE AND METHOD OF APPORTIONMENT - PREPAYMENT OF SPECIAL TAX”** herein.

Special Taxes Are Not Within Teeter Plan

The County has adopted a Teeter Plan as provided for in Section 4701 *et seq.* of the California Revenue and Taxation Code, under which a tax distribution procedure is implemented and secured roll taxes are distributed to taxing agencies within the County on the basis of the tax levy, rather than on the basis of actual tax collections. However, by policy, the County does not include assessments, reassessments and special taxes in its Teeter program. The Special Taxes are not included in the County’s Teeter Program.

BONDOWNERS' RISKS

General

BEFORE PURCHASING ANY OF THE BONDS, ALL PROSPECTIVE INVESTORS AND THEIR PROFESSIONAL ADVISORS SHOULD CAREFULLY CONSIDER, AMONG OTHER THINGS, THE FOLLOWING RISK FACTORS, WHICH ARE NOT MEANT TO BE AN EXHAUSTIVE LISTING OF ALL RISKS ASSOCIATED WITH THE PURCHASE OF THE BONDS. MOREOVER, THE ORDER OF PRESENTATION OF THE RISK FACTORS DOES NOT NECESSARILY REFLECT THE ORDER OF THEIR IMPORTANCE.

The purchase of the Bonds involves investment risk. If a risk factor materializes to a sufficient degree, it could delay or prevent payment of principal of and/or interest on the Bonds. Such risk factors include, but are not limited to, the following matters.

Limited Obligation

Neither the faith and credit nor the taxing power of the City, the State or any political subdivision thereof other than the District is pledged to the payment of the Bonds. Except for the Special Taxes derived from Improvement Area No. 2, no other taxes are pledged to the payment of the Bonds. The Bonds are not general or special obligations of the City, the State or any political subdivision thereof or general obligations of the District, but are special obligations of the District, payable solely from Special Taxes and the other assets pledged therefor under the Fiscal Agent Agreement.

Insufficiency of Special Taxes

As discussed herein, the amount of Special Taxes that are collected with respect to Improvement Area No. 2 could be insufficient to pay principal of, interest and premium, if any, on the Bonds due to nonpayment of the Special Taxes levied and insufficient or no proceeds received from a foreclosure sale of land within Improvement Area No. 2.

The District has covenanted in the Fiscal Agent Agreement to institute foreclosure proceedings upon delinquencies in the payments of the Special Taxes as described herein and to sell any real property with a lien of delinquent Special Taxes to obtain funds to pay debt service on the Bonds. If foreclosure proceedings are ever instituted, any holder of a mortgage or deed of trust could, but would not be required to, advance the amount of delinquent Special Taxes to protect its security interest. See “**SOURCES OF PAYMENT FOR THE BONDS - Covenant for Superior Court Foreclosure**” herein for provisions which apply in the event foreclosure is required and which the District is required to follow in the event of delinquency in the payment of Special Taxes.

Section 53317.3 of the Act provides that, if any real property within Improvement Area No. 2 not otherwise exempt from the Special Tax is acquired by a public entity through a negotiated transaction, or by gift or devise, the Special Tax will continue to be levied on and be enforceable against the public entity that acquires the property. Additionally, Section 53317.5 provides that, if any property subject to the Special Tax is acquired by a public entity through eminent domain proceedings, the obligation to pay the Special Tax with respect to that property is to be treated as if it were a special assessment and be paid from the eminent domain award. However, the constitutionality and operation of these provisions of the Act have not been tested. If for any reason, property subject to the Special Tax becomes exempt from taxation by reason of ownership by a non-taxable entity, such as the federal government or another public agency, and the District is unable to collect the Special Taxes or obtain compensation through the condemnation procedure, the Special Tax will be reallocated to the remaining taxable properties within Improvement Area No. 2 up to the Maximum Annual Special Tax. This reallocation would result in the owners of taxable properties within Improvement Area No. 2 subject to the Special Tax paying a greater amount of the Special Tax and could have an adverse impact upon the timely payment of the Special Tax by such owners and therefore the ability to pay debt service on the Bonds.

Concentration of Ownership

All of the property within Improvement Area No. 2 is owned by the Developer (see “**IMPROVEMENT AREA NO. 2**” herein). The only assets of the property owners which constitute security for the Bonds are their taxable property within Improvement Area No. 2. There are expected to be subsequent transfers of ownership of the property within Improvement Area No. 2 to individual owners of single family homes during the development of the land within Improvement Area No. 2, although there is no assurance that such transfers of property will occur as described herein, if at all. The fact that a limited number of property owners own significant amounts of land within Improvement Area No. 2 presents substantial risk to the Bondowners.

No Personal Liability for Special Taxes

No property owner (including the Developer) or any officer, partner, member, or affiliate thereof will be personally liable for the payment of the Special Taxes to be applied to pay the principal of and interest on the Bonds. In addition, there is no assurance that any property owner or the Developer will be able to pay the Special Taxes or that any property owner or the Developer will pay such Special Taxes even if it is financially able to do so. No representation is made that the Developer will have moneys available (or that it will advance such moneys, if available) to complete the development of the land within Improvement Area No. 2 in the manner described herein. Accordingly, the Developer’s financial statements are not included in this Official Statement. No property owner is obligated in any manner to continue to own any of the land it presently owns within Improvement Area No. 2.

Adjustable Rate and Non-Conventional Mortgages

Since the end of 2002, many persons have financed the purchase of new homes using loans with little or no down payment and with adjustable interest rates that start low and are subject to being reset at higher rates on a specified date or upon the occurrence of specified conditions. Many of these loans allow the borrower to pay interest only for an initial period, in some cases up to 10 years. Currently, in Southern California, a substantial portion of outstanding home loans are adjustable rate loans at historically low interest rates. In the opinion of some economists, the significant increase in home prices in this time period has been driven, in part, by the ability of home purchasers to access adjustable rate and non-conventional loans. If interest rates on new loans increase and if the interest rates on existing adjustable rate loans are reset (and payments are increased) there could be a decrease in home sales due to the inability of purchasers to qualify for loans with higher interest rates. Such a decrease in home sales could, eventually, result in a decrease in home prices. Such a reduction in home prices could result in recent homebuyers having loan balances that exceed the value of their homes, given their low down payments and small amount of equity in their homes.

Homeowners in Improvement Area No. 2 who purchase their homes with adjustable rate and non-conventional loans with no or low down payments may experience difficulty in making their loan payments due to automatic mortgage rate increases and rising interest rates. This could result in an increase in the Special Tax delinquency rate in Improvement Area No. 2 and draws on the Reserve Account. If there were significant delinquencies in Special Tax collections in Improvement Area No. 2 and the Reserve Account was fully depleted, there could be a default in the payment of principal of and interest on the Bonds.

If mortgage loan defaults increase, bankruptcy filing by such homeowners could also increase. Bankruptcy filings by homeowners with delinquent Special Taxes would delay the commencement and completion of foreclosure proceedings to collect delinquent Special Taxes.

Foreclosure and Sale Proceedings

Payment of the Special Taxes is secured by the parcels assessed. In the event an annual installment of the Special Taxes included in the County tax bill of an assessed parcel is not paid when due, the District can institute foreclosure proceedings in court to cause the parcel to be sold in order to recover the delinquent

amount from the sale of proceeds (see “**SOURCES OF REPAYMENT FOR THE BONDS**” herein). Foreclosure and sale may not always result in the recovery of any or the full amount of delinquent Special Taxes.

Sufficiency of the foreclosure sales proceeds to cover the delinquent amount depends in part upon the market for and the value of the parcel at the time of the foreclosure sale (see “**Land Values**” below). The current appraised value is some evidence of such future value. However, future events may result in significant changes from the current appraised value. Such events could include changes in land ownership, development plans and other factors affecting the progress of land development, legal requirements affecting the development of parcels, a downturn in the economy, as well as a number of additional factors. Any of these factors may result in a significant erosion in value, with consequent reduced security of the Bonds.

Sufficiency of foreclosure sale proceeds to cover a delinquency may also depend upon the value of prior or parity liens and similar claims. A variety of governmental liens may presently exist or may arise in the future with respect to a parcel which, unless subordinate to the lien securing the Special Taxes, may effectively reduce the value of such parcel. Further, other governmental claims, such as hazardous substance claims, may affect the realizable value even though such claims may not rise to the status of liens.

Timely foreclosure and sale proceedings with respect to a parcel may be forestalled or delayed by a stay in the event the owner of the parcel becomes the subject of bankruptcy proceedings. Further, should the stay not be lifted, payment of Special Taxes may be subordinated to bankruptcy law priorities.

Land Values

If a property owner defaults in the payment of the Special Tax, the District’s only remedy is to commence foreclosure proceedings against the defaulting property owner’s real property within Improvement Area No. 2 for which the Special Tax has not been paid, in an attempt to obtain funds to pay the delinquent Special Tax. Therefore, the value of the land and improvements within Improvement Area No. 2 is a critical factor in determining the investment quality of the applicable corresponding series of Bonds and, therefore, the Bonds. Reductions in property values within Improvement Area No. 2 due to a downturn in the economy or the real estate market, events such as earthquakes, droughts, or floods, stricter land use regulations, or other events may adversely impact the security underlying the Special Tax.

The District had the following two studies prepared in order to estimate the current aggregate market value of land in Improvement Area No. 2.

1. Market Absorption Study, Community Facilities District No. 2004-3 (Rosetta Canyon) City of Lake Elsinore, Riverside County, California prepared by Empire Economics, Inc., Capistrano Beach, California, Updated August 10, 2006 (the “Market Absorption Study”).
2. Appraisal Report, City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon) Improvement Area No. 2 prepared by Harris Realty Appraisal, Newport Beach, California (the “Appraisal”), dated August 10, 2006.

Collectively, the studies are referred to herein as the “Appraisal Documents.”

The purpose of the Appraisal was to estimate the bulk value of the land and improvements within Improvement Area No. 2 in its “as is” condition (which assumes sale of the Bonds and construction of publicly-financed improvements).

On the basis of the assumptions and limitations described in the Appraisal and in the Market Absorption Study, the Appraiser has estimated the aggregate discounted “bulk sale” value of all the parcels in Improvement Area No. 2 as of August 10, 2006 to be \$78,500,000, which is approximately 3.35 times the principal amount of the Bonds.

Prospective purchasers of the Bonds should not assume that the land and improvements could be sold for the appraised amount at a foreclosure sale for delinquent Special Taxes. In particular, the values of individual properties in Improvement Area No. 2 will vary in some cases significantly. The actual value of the land is subject to future events which might render invalid some or all of the basic assumptions of the Appraiser. The future value of the land can be expected to fluctuate due to many different, not fully predictable, real estate related investment risk factors, including, but not limited to: general tax law changes related to real estate, changes in competition, general area employment base changes, population changes, changes in real estate related interest rates affecting general purchasing power, advertising, changes in allowed zoning uses and density, natural disasters such as floods, earthquakes and landslides, and similar factors.

Appraisals in general are the result of an inexact process, and estimated market value is dependent, in part, upon assumptions which may or may not be realized and upon market conditions and perceptions of market value, which are likely to change over time. The appraisal valuations represent opinions only and are not intended to be absolutes or assurances of specific resale values.

If more than one appraiser were employed, it is reasonable to assume that a reasonable range of value opinions on the land and improvement value within Improvement Area No. 2 would be reflected depending upon personal professional interpretation of data, facts and circumstances reviewed and assumptions employed. Prospective purchasers should not assume that the land could be sold for the appraised amount at a foreclosure sale for delinquent Special Taxes.

Copies of the Appraisal Documents are included in the Appendices. The summary herein of some of the conclusions in the Appraisal Documents does not purport to be complete. Reference is made to the Appraisal Documents for further information. The District makes no representations as to the value of the real property within Improvement Area No. 2, and prospective purchasers of the Bonds are referred to the Appraisal Documents referred to above in evaluating the value of real property within Improvement Area No. 2.

Value-to-Lien Ratio

Valuation-to-lien ratios are derived by dividing the appraised value of the property in Improvement Area No. 2 by the principal amount of the Bonds. For example, a 3:1 ratio means that the value is three times the total Bond amount.

According to the Appraisal the value of the land within Improvement Area No. 2 is \$78,500,000. Therefore, the value to lien-ratio-is 3.35 to 1. The value-to-lien ratio of individual parcels may be less or more than the aggregate value-to-lien ratio for an District. In particular, the value of developed property is substantially more than undeveloped property (see “**Concentration of Ownership**” above).

Investors must recognize the uncertainties with respect to the fair market values of the parcels, since the Bonds are secured by the Special Taxes levied on the parcels. See “Land Values” above.

Potential purchasers of the Bonds should be aware that if a parcel bears a Special Tax liability in excess of its market value, then there may be little incentive for the owner of the parcel to pay the Special Taxes on such parcel and little likelihood that such property would be purchased in a foreclosure sale. See “Foreclosure and Sale Proceedings” above describing risks relating to market values of parcels in Improvement Area No. 2.

The Progress of Land Development; Risks of Real Estate Secured Investments

Land development is an activity subject to substantial risk. Risk factors include, without limitation, general or local economic conditions; local real estate market conditions; supply of or demand for competitive properties; changes in the real estate tax rate; governmental regulation and approval requirements, particularly environmental quality, endangered species, land use, zoning and building

requirements; development, financing and marketing capabilities of the various landowners; natural disasters, including without limitation earthquakes, flood and fire which may result in uninsured losses; and accomplishment of development plans on a timely basis, including but not limited to the provision of infrastructure improvements in addition to the Facilities.

Since these are largely business risks of the type that landowners customarily evaluate individually, and inasmuch as changes in land ownership may well mean changes in the evaluation with respect to any particular parcel, the District has undertaken the financing without regard to any such evaluation. Thus, the undertaking of the financing by the District in no way implies that the District has evaluated these risks or the reasonableness of these risks.

Further, the risk to the owners of the Bonds of development delays may be heightened when land ownership is concentrated in only a few landowners or the Developer. If ownership is concentrated, timely payment of the Special Taxes may be dependent upon the financing available to such owners or Developer. Further, the continued progress of land development may be one of the present facts and circumstances forming the basis for the appraiser's opinion of value. Diminished values may lessen the effectiveness of foreclosure proceedings as a remedy.

The Special Taxes are to be collected from the owners of property located within Improvement Area No. 2, and levy of the Special Taxes is not dependent on the completion of the development of the properties within Improvement Area No. 2 (see "SPECIAL TAXES AND DEBT SERVICE" herein). Nevertheless, the extent of completion of the development of the property within Improvement Area No. 2 may affect the ability and willingness of property owners to pay the Special Taxes and may affect the market value of any property foreclosed upon for nonpayment of installments of the Special Taxes.

Geologic, Topographic and Climatic Conditions

Land and improvement value can be adversely affected by a variety of additional factors, particularly those which may affect infrastructure and private improvements of the parcels assessed and the continued habitability and enjoyment of such private improvements. Such additional factors include, without limitation, geologic conditions such as earthquakes and overdraft of groundwater basins; topographic conditions such as earth movements and floods; and climatic conditions such as droughts.

Further, building codes require that some of these factors be taken into account, to a limited extent, in the design of private improvements of the parcels in Improvement Area No. 2. Design criteria in any of these circumstances are established upon the basis of a variety of considerations and may change, leaving previously designed improvements unaffected by more stringent subsequently established criteria. In general, design criteria reflect a balance at the time of establishment between the present costs of protection and the future costs of lack of protections, based in part upon a present perception of the probability that the condition will occur and the seriousness of the condition should the condition occur.

Endangered and Threatened Species

During the past several years, there has been an increase in activity at the State and federal level related to the listing and possible listing of certain plant and animal species found in the State as endangered species and in programs designed to set aside additional geographical areas for habitat conservation. Although areas within Improvement Area No. 2 have been included in the Western Riverside County Multi Species Habitat Conservation Plan (MSHCP) study area, such areas are exempt from any requirements because of a pre-existing development agreement. There is no assurance that such areas will not be included in future study areas. An increase in the number of endangered species and/or the designation of additional habitat areas to be subjected to conservation planning similar to areas subject to the Western Riverside County MSHCP is expected to curtail development in a number of areas in the State. The area proposed to be developed within Improvement Area No. 2 is not known to contain any plant or animal species which either the California Fish and Game Commission or the U.S. Fish and Wildlife Service has listed as endangered or to the knowledge of the District proposed for addition to the endangered species list.

Further approval may be required for any planned clearing of land or construction across or impacting waterways, creeks or other drainages. If required, there is no assurance that such approvals will be obtained and that development will be permitted to proceed as projected.

On a regular basis, new species are proposed to be added to the State and federal protected species lists. Regardless of the stage of entitlements and actual development of a particular development, any action by the State or federal governments to protect species located on or adjacent to the property within Improvement Area No. 2 could negatively affect the Developer's ability to complete the development of the properties within Improvement Area No. 2 as planned. This, in turn, could reduce the ability or the willingness of the property owners to pay the Special Taxes when due and would likely reduce the value of the land and the potential revenues available at a foreclosure sale for delinquent Special Taxes.

Earthquakes

Southern California is among the most seismically active regions in the United States. The occurrence of seismic activity in Improvement Area No. 2 could result in substantial damage to properties in Improvement Area No. 2 which, in turn, could substantially reduce the value of such properties and could affect the ability or willingness of the property owners to pay their Special Taxes. Any major damage to structures as a result of seismic activity could result in a greater reliance on Undeveloped Property in the payment of Special Taxes. In the event of a severe earthquake, there may be significant damage to both property and infrastructure in Improvement Area No. 2. As a result, a substantial portion of the property owners may be unable or unwilling to pay the Special Taxes when due. In addition, the value of land in Improvement Area No. 2 could be diminished in the aftermath of such an earthquake, reducing the resulting proceeds of foreclosure sales in the event of delinquencies in the payment of Special Taxes.

Certain procedures and design standards are required to be followed during the construction of buildings within Improvement Area No. 2 to ensure that each building is designed and constructed to meet, at a minimum, the highest seismic standards required by law.

Legal Requirements

Other events which may affect the value of a parcel include changes in the law or application of law. Such changes may include, without limitation, local growth control initiatives; local utility connection moratoriums; and local application of statewide tax and governmental spending limitation measures.

Other Possible Claims Upon the Values of an Assessed Parcel

In addition to existing property taxes, other governmental obligations, such as general obligation bonds, assessments or special taxes may be authorized in the future, the tax, assessment or charge for which may become an obligation of one or more of the parcels within Improvement Area No. 2 and may be secured by a lien on a parity with the lien of the Special Taxes securing the Bonds.

In general, as long as the Special Taxes securing the Bonds are collected on the County tax roll, the Special Taxes and all other taxes, assessments and charges also collected on the tax roll are on a parity with each other. Questions of priority become significant when collection of one or more of the taxes, assessments or charges is sought by some other procedure, such as foreclosure and sale. Otherwise, in the event of such foreclosure proceedings, the Special Taxes will generally be on a parity with the other taxes, assessments and charges. The Special Taxes will have priority over non-governmental liens on a parcel, regardless of whether or not the non-governmental liens are in existence at the time of creation of any lien securing the Special Taxes.

While governmental taxes, assessments and charges are a common claim against the value of a parcel, other less common claims may be relevant. One of the most serious in terms of the potential reduction in the value of a parcel is a claim with regard to a hazardous substance. In general, the owners and operators of a parcel may be required by law to remedy conditions of the parcel relating to releases or threatened

releases of hazardous substances. Under many of these laws, the owner (or operator) is obligated to remedy a hazardous substance condition 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 parcels in Improvement Area No. 2 be affected by a hazardous substance, is to reduce the marketability and value of the parcel by the costs of remedying the condition, because the purchaser, upon becoming the owner, will become obligated to remedy the condition just as is the seller.

The values expressed herein, do not take into account the possible reduction in marketability and value of any of the parcels by reason of the possible liability of the owner (or operator) for the remedy of a hazardous substance condition of the parcel. The District is not aware that the owner (or operator) of any of the parcels has such a current liability with respect to any of the parcels in Improvement Area No. 2. However, it is possible that such liabilities do currently exist.

Further, it is possible that liabilities may arise in the future with respect to one or more of the parcels resulting from the existence, currently, on the parcel of a substance presently classified as hazardous or may arise in the future resulting from the existence, currently, on the parcel of a substance presently not classified as hazardous but which may in the future be so classified. Further, such liabilities may arise not simply from the existence of a hazardous substance but from the method of handling it. All of these possibilities could significantly reduce the value of a parcel.

Bankruptcy Proceedings

Regardless of the priority of the Special Taxes securing the Bonds over non-governmental liens on parcels, the exercise by the District of the foreclosure and sale remedy may be forestalled or delayed by bankruptcy, reorganization, insolvency, or other similar proceedings of the owner of a parcel. The federal bankruptcy laws provide for an automatic stay of foreclosure and sale proceedings, thereby delaying such proceedings perhaps for an extended period. Delay in exercise of remedies, especially if the owners own parcels the Special Taxes of which are significant or if bankruptcy proceedings are instituted with respect to a number of owners owning parcels the Special Taxes of which is significant, may result in periodic Special Tax collections which may be insufficient to pay the debt service on the Bonds. Further, should remedies be exercised under the bankruptcy law against the parcels, payment of Special Taxes may be subordinated to other claims in the bankruptcy proceedings. Thus, certain claims may have priority over a claim for unpaid Special Taxes, even though, in the absence of the bankruptcy proceedings, no such priority would exist.

Bankruptcy and Foreclosure Delays

The payment of the Special Taxes and the ability of the District to foreclose the lien of a delinquent unpaid Special Tax, as discussed in the section herein entitled “**SOURCES OF PAYMENT FOR THE BONDS**” may be limited by bankruptcy, insolvency, or other laws generally affecting creditors’ rights or by the laws of the State of California relating to judicial foreclosure.

The various legal opinions to be delivered concurrently with the delivery of the Bonds (including Bond Counsel’s approving legal opinion) will be qualified as to the enforceability of the various legal instruments, by bankruptcy, reorganization, insolvency or other similar laws affecting the rights of creditors generally.

Although bankruptcy proceedings would not cause the Special Taxes to become extinguished, bankruptcy of a property owner or of a partner or other owner of a property owner within Improvement Area No. 2 could result in a delay in prosecuting superior court foreclosure proceedings and could result in loss of priority of the lien securing any Special Taxes with respect to Special Taxes levied while bankruptcy proceedings are pending. In addition, the amount of any lien on property securing the payment of delinquent Special Taxes could be reduced if the value of the property were determined by the bankruptcy court to have become less than the amount of the lien, and the amount of the delinquent Special Taxes in excess of the reduced lien could be treated as an unsecured claim by the court. Such delay or loss of

priority or nonpayment, would increase the likelihood of a delay or default in payment of the principal of and interest on the Bonds and the possibility of delinquent Special Tax installments not being paid in full. To the extent a significant percentage of the property in Improvement Area No. 2 continues to be owned by a limited number of property owners, the payment of the Special Taxes and the ability of Improvement Area No. 2 to foreclose the lien of a delinquent unpaid Special Taxes installment could be delayed by bankruptcy, insolvency, or other laws generally affecting creditors' rights or by the laws of the State relating to judicial foreclosure.

On July 30, 1992, the United States Court of Appeals for the Ninth Circuit issued its opinion in a bankruptcy case entitled *In re Glasply Marine Industries*. In that case, the court held that *ad valorem* property taxes levied by Snohomish County in the State of Washington after the date that the property owner filed a petition for bankruptcy were not entitled to priority over a secured creditor with a prior lien on the property. The court upheld the priority of unpaid taxes imposed after the filing of the bankruptcy petition as "administrative expenses" of the bankruptcy estate, payable after all secured creditors. As a result, the secured creditor was to foreclose on the property and retain all of the proceeds of the sale except the amount of the pre-petition taxes.

According to the court's ruling, as administrative expenses, post-petition taxes would have to be paid, assuming that the debtor has sufficient assets to do so. In certain circumstances, payment of such administrative expenses may be allowed to be deferred. Once the property is transferred out of the bankruptcy estate (through foreclosure or otherwise) it would at that time become subject to current *ad valorem* taxes.

The Act provides that the Special Taxes are secured by a continuing lien, which is subject to the same lien priority in the case of delinquency as *ad valorem* taxes. No case law exists with respect to how a bankruptcy court would treat the lien for the Special Taxes levied after the filing of a petition in bankruptcy. *Glasply* is controlling precedent for bankruptcy courts in the State. If the *Glasply* precedent was applied to the levy of the Special Tax, the amount of Special Tax received from parcels whose owners declared bankruptcy could be reduced.

It should also be noted that on October 22, 1994, Congress enacted 11 U.S. C. Section 362(b)(18), which added a new exception to the automatic stay for *ad valorem* property taxes imposed by a political subdivision after the filing of a bankruptcy petition. Pursuant to this new provision of law, in the event of a bankruptcy petition filed on or after October 22, 1994, the lien for *ad valorem* taxes in subsequent fiscal years will attach even if the property is part of the bankruptcy estate. Bondowners should be aware that the potential effect of 11 U.S. C. Section 362(b)(18) on the Special Taxes depends upon whether a court were to determine that the Special Taxes should be treated like *ad valorem* taxes for this purpose.

Additional Taxation

On June 3, 1986, California voters approved an amendment to Article XIII A of the California Constitution to allow local governments and school districts to raise their property tax rates above the constitutionally mandated 1% ceiling for the purpose of repaying certain new general obligation debt issued for the acquisition or improvement of real property and approved by at least two-thirds of the votes cast by the qualified electorate. If any such voter-approved debt is issued, it may be on a parity with the lien of the Special Taxes on the parcels within Improvement Area No. 2.

Parity Taxes and Special Assessments

The Special Taxes and any penalties thereon will constitute a lien against the lots and parcels of land within Improvement Area No. 2 on which they will be annually imposed until they are paid in full. Such lien is on a parity with all special taxes and special assessments levied by other public entities, agencies and districts and is co-equal to and independent of the lien for general property taxes regardless of when they are imposed upon the same real property. The Special Taxes have priority over all existing and future private liens imposed on the real property within Improvement Area No. 2, however, the District

has no control over the ability of other public entities, agencies and districts to issue indebtedness secured by special taxes or assessments payable from all or a portion of the real property within Improvement Area No. 2. Any such special taxes or assessments may have a lien on such real property on a parity with the Special Taxes (see “**SPECIAL TAXES AND DEBT SERVICE**” herein).

Accordingly, the liens on the real property within Improvement Area No. 2 could greatly increase, without any corresponding increase in the value of the property within Improvement Area No. 2 and thereby severely reduce the lien-to-value ratio of the land-secured public debt existing at the time the Bonds are issued. The imposition of such additional indebtedness could also reduce the willingness and ability of the property owners within Improvement Area No. 2 to pay the Special Taxes when due.

Disclosure to Future Land Buyers

A “Notice of Special Tax Lien” for Improvement Area No. 2 (the “Notice”) was recorded pursuant to Section 53328.3 of the Act and Section 3114.5 of the Streets and Highways Code, with the County Recorder for the County (the “County Recorder”). The Notice sets forth, among other things, the Rate and Method of Apportionment, the Assessor’s Parcel Numbers within Improvement Area No. 2 as of the date of recording the Notice, and the boundaries of Improvement Area No. 2 by reference to the map(s) recorded with the County Recorder. While title insurance and search companies normally refer to such notices in title reports, and sellers of property within Improvement Area No. 2 are required to give prospective buyers a notice of special tax in accordance with Sections 53360.2 or 53341.5 of the Act, there can be no assurances that such reference will be made or notice given, or if made or given, that prospective purchasers or lenders will consider such Special Tax obligation in the purchase of land within Improvement Area No. 2 or the lending of money thereon. Failure to disclose the existence of the Special Tax may affect the willingness and ability of future landowners within Improvement Area No. 2 to pay the Special Tax when due.

Billing of Special Taxes

A special tax can result in a substantially heavier property tax burden being imposed upon properties within a community facilities district than elsewhere in a city or county, and this in turn can lead to problems in the collection of the special tax. In some community facilities districts the taxpayers have refused to pay the special tax and have commenced litigation challenging the special tax, the community facilities district and the bonds issued by the District.

Under provisions of the Act, the Special Taxes are billed to the properties within Improvement Area No. 2 which were entered on the Assessment Roll of the County Assessor by January 1 of the previous fiscal year on the regular property tax bills sent to owners of such properties. Such Special Tax installments are due and payable, and bear the same penalties and interest for non-payment, as do regular property tax installments. These Special Tax installment payments cannot be made separately from property tax payments. Therefore, the unwillingness or inability of a property owner to pay regular property tax bills as evidenced by property tax delinquencies may also indicate an unwillingness or inability to make regular property tax payments and installment payments of Special Taxes in the future. See “**SOURCES OF PAYMENT FOR THE BONDS - Covenant for Superior Court Foreclosure**” for a discussion of the provisions which apply, and procedures which the District is obligated to follow, in the event of delinquency in the payment of installments of Special Taxes.

Collection of Special Tax

In order to pay debt service on the Bonds, it is necessary that the Special Tax levied against land within Improvement Area No. 2 be paid in a timely manner. The District has covenanted in the Fiscal Agent Agreement under certain conditions to institute foreclosure proceedings against property with delinquent Special Tax in order to obtain funds to pay debt service on the Bonds. If foreclosure proceedings were instituted, any mortgage or deed of trust holder could, but would not be required to, advance the amount of the delinquent Special Tax to protect its security interest. In the event such superior court foreclosure

is necessary, there could be a delay in principal and interest payments on the Bonds pending prosecution of the foreclosure proceedings and receipt of the proceeds of the foreclosure sale, if any. No assurances can be given that the real property subject to foreclosure and sale at a judicial foreclosure sale will be sold or, if sold, that the proceeds of such sale will be sufficient to pay any delinquent Special Tax installment. Although the Act authorizes the District to cause such an action to be commenced and diligently pursued to completion, the Act does not specify the obligations of the District with regard to purchasing or otherwise acquiring any lot or parcel of property sold at the foreclosure sale if there is no other purchaser at such sale. See **“SOURCES OF PAYMENT FOR THE BONDS - Covenant for Superior Court Foreclosure.”**

Maximum Rates

Within the limits of the Rate and Method of Apportionment, the District may adjust the Special Tax levied on all property within Improvement Area No. 2 to provide an amount required to pay debt service on the Bonds and other obligations of Improvement Area No. 2, and the amount, if any, necessary to pay all annual Administrative Expenses and make rebate payments to the United States government. However, the amount of the Special Tax that may be levied against particular categories of property within Improvement Area No. 2 is subject to the maximum rates provided in the Rate and Method of Apportionment. There is no assurance that the maximum rates will at all times be sufficient to pay the amounts required to be paid by the Fiscal Agent Agreement. See **“SPECIAL TAXES AND DEBT SERVICE.”**

Exempt Properties

Certain properties are exempt from the Special Tax in accordance with the Rate and Method of Apportionment and provisions of the Act. The Act provides that properties or entities of the State, federal or local government at the time of formation of Improvement Area No. 2 are exempt from the Special Tax; provided, however, that property within Improvement Area No. 2 acquired by a public entity through negotiated transactions, or by gift or devise, which is not otherwise exempt from the Special Tax, will continue to be subject to the Special Tax. In addition, the Act provides that if property subject to the Special Tax is acquired by a public entity through eminent domain proceedings, the obligation to pay the Special Tax with respect to that property is to be treated as if it were a special assessment and be paid from the eminent domain award. The constitutionality and operation of these provisions of the Act have not been tested. If for any reason property subject to the Special Tax becomes exempt from taxation by reason of ownership by a non-taxable entity such as the federal government, or another public agency, subject to the limitation of the maximum authorized rate of levy, the Special Tax may be reallocated to the remaining taxable properties within Improvement Area No. 2. This would result in the owners of such property paying a greater amount of the Special Tax and could have an adverse impact upon the timely payment of the Special Tax; however, the amount of Special Tax to be levied and collected from the property owner is subject to the Maximum Special Tax as set forth in the Rate and Method of Apportionment and to the limitation in the Act that under no circumstances may the Special Taxes levied on any residential parcel be increased by more than ten percent as a consequence of delinquency by the owner of any parcel. If a substantial portion of land within Improvement Area No. 2 became exempt from the Special Tax because of public ownership, or otherwise, the maximum Special Tax which could be levied upon the remaining acreage might not be sufficient to pay principal of and interest on the Bonds when due and a default will occur with respect to the payment of such principal and interest.

The Act further provides that no other properties or entities are exempt from the Special Tax unless the properties or entities are expressly exempted in a resolution of consideration to levy a new special tax or to alter the rate or method of apportionment of an existing special tax. The Act would prohibit the City Council, acting as the legislative body of the District, from adopting a resolution to reduce the rate of the Special Tax or terminate the levy of the Special Tax unless the City Council, acting as the legislative body of the District determined that the reduction or termination of the Special Tax “would not interfere with the timely retirement” of the Bonds. See **“BONDOWNERS’ RISKS - Right to Vote on Taxes Act”** below.

Insufficient Special Taxes

Under the Rate and Method of Apportionment, the annual amount of Special Tax to be levied on each taxable parcel in Improvement Area No. 2 will be based primarily on whether such parcel is developed or not and, for Developed Property, on the type of structure and square footage of buildings constructed. See “APPENDIX E”. Accordingly, to the extent Undeveloped Property does not become Developed Property, the collection of the Special Taxes will be dependent on the willingness and ability of the owners of Undeveloped Property to pay such Special Taxes when due. Such event may result in an unwillingness of such owners of the Undeveloped Property to pay additional Special Taxes.

No Acceleration Provision

The Fiscal Agent Agreement does not contain a provision allowing for the acceleration of the principal of the Bonds in the event of a payment default or other default under the terms of the Bonds or the Fiscal Agent Agreement.

Property Controlled by Federal Deposit Insurance Corporation and other Federal Agencies

The District’s ability to collect interest and penalties specified by State law and to foreclose the lien of a delinquent Special Tax payment may be limited in certain respects with regard to properties in which the Internal Revenue Service, the Drug Enforcement Agency, the Federal Deposit Insurance Corporation (the “FDIC”) or other similar federal agencies has or obtains an interest. Specifically, with respect to the FDIC, on June 4, 1991, the FDIC issued a Statement of Policy Regarding the Payment of State and Local Real Property Taxes (the “1991 Policy Statement”). The 1991 Policy Statement was revised and superseded by a new Policy Statement effective January 9, 1997 (the “Policy Statement”). The Policy Statement provides that real property owned by the FDIC is subject to state and local real property taxes only if those taxes are assessed according to the property’s value, and that the FDIC is immune from real property taxes assessed on any basis other than property value. According to the Policy Statement, the FDIC will pay its proper tax obligations when they become due and payable and will pay claims for delinquent property taxes as promptly as is consistent with sound business practice and the orderly administration of the institution’s affairs, unless abandonment of the FDIC’s interest in the property is appropriate. The FDIC will pay claims for interest on delinquent property taxes owed at the rate provided under state law, to the extent the interest payment obligation is secured by a valid lien. The FDIC will not pay any amounts in the nature of fines or penalties and will not pay nor recognize liens for such amounts. If any property taxes (including interest) on FDIC owned property are secured by a valid lien (in effect before the property became owned by the FDIC), the FDIC will pay those claims. The Policy Statement further provides that no property of the FDIC is subject to levy, attachment, garnishment, foreclosure or sale without the FDIC’s consent. In addition, the FDIC will not permit a lien or security interest held by the FDIC to be eliminated by foreclosure without the FDIC’s consent.

The Policy Statement states that FDIC generally will not pay non *ad valorem* taxes, including special assessments, on property in which it has a fee interest unless the amount of tax is fixed at the time that the FDIC acquires its fee interest in the property, nor will it recognize the validity of any lien to the extent it purports to secure the payment of any such amounts. Special taxes imposed under the Mello-Roos Act and a special tax formula which determines the special tax due each year, are specifically identified in the Policy Statement as being imposed each year and therefore covered by the FDIC’s federal immunity. With respect to property in California owned by the FDIC on January 9, 1997, and that was owned by the Resolution Trust Corporation (the “RTC”) on December 31, 1995, or that became property of the FDIC through foreclosure of a security interest held by the RTC on that date, the FDIC will continue the RTC’s prior practice of paying special taxes imposed pursuant to the Mello-Roos Act if the taxes were imposed prior to the RTC’s acquisition of an interest in the property. All other special taxes, including the Special Taxes which secure the Bonds may be challenged by the FDIC.

The FDIC has filed claims against the County of Orange with respect to Mello-Roos community facilities district special taxes in the United States Bankruptcy Court and in Federal District Court in which the FDIC has taken a position similar to the position outlined in the Policy Statement. While all of such claims have not been resolved, the Bankruptcy Court has issued a tentative ruling in favor of the FDIC on certain of such claims. The County of Orange has appealed such ruling and the FDIC has cross-appealed. The decision of the United States Court of Appeals for the 9th Circuit (the “9th Circuit Court”) was filed on August 28, 2001. In its decision, the 9th Circuit Court stated that the FDIC, as a federal agency, is exempt from the Mello-Roos special tax. The FDIC has also filed suit (the “post-bankruptcy” suit) regarding special taxes imposed after 1994. However, such action has been stayed pending resolution of the 9th Circuit Court appeal by the FDIC regarding the bankruptcy case. The post-bankruptcy suit has recently been consolidated with the cases filed by the FDIC against other California counties and is pending in the United States District Court in Los Angeles. The FDIC has filed a motion to lift the bankruptcy stay.

The District is unable to predict what effect the application of the Policy Statement would have in the event of a delinquency with respect to a parcel in which the FDIC has an interest, although prohibiting the lien of the FDIC to be foreclosed on at a judicial foreclosure sale would likely reduce the number of or eliminate the persons willing to purchase such a parcel at a foreclosure sale. Owners of the Bonds should assume that the District will be unable to foreclose on any parcel owned by the FDIC. The District has not undertaken to determine whether the FDIC currently has, or is likely to acquire, any interest in any of the parcels, and therefore expresses no view concerning the likelihood that the risks described above will materialize while the Bonds are outstanding.

Limitations on Remedies

Remedies available to the Owners may be limited by a variety of factors and may be inadequate to assure the timely payment of principal of and interest on the Bonds or to preserve the tax-exempt status of the Bonds. Bond Counsel has limited its opinion as to the enforceability of the Bonds and of the Fiscal Agent Agreement to the extent that enforceability may be limited by bankruptcy, insolvency, reorganization, fraudulent conveyance or transfer, moratorium, or other similar laws affecting generally the enforcement of creditor’s rights, by equitable principles and by the exercise of judicial discretion. Additionally, the Bonds are not subject to acceleration in the event of the breach of any covenant or duty under the Fiscal Agent Agreement. The lack of availability of certain remedies or the limitation of remedies may entail risks of delay, limitation or modification of the rights of the Owners.

Enforceability of the rights and remedies of the owners of the Bonds, and the obligations incurred by the District, may become subject to the federal bankruptcy code and bankruptcy, insolvency, reorganization, moratorium, or similar laws relating to or affecting the enforcement of creditor’s rights generally, now or hereafter in effect, equity principles which may limit the specific enforcement under State law of certain remedies, the exercise by the United States of America of the powers delegated to it by the Constitution, the reasonable and necessary exercise, in certain exceptional situations, of the police powers inherent in the sovereignty of the State and its governmental bodies in the interest of serving a significant and legitimate public purpose and the limitations on remedies against joint powers authorities in the State. See **“BONDOWNERS’ RISKS - Bankruptcy and Foreclosure Delays,” “-Billing of Special Taxes” and “-Property Controlled by Federal Deposit Insurance Corporation and other Federal Agencies”** herein.

Right to Vote on Taxes Act

An initiative measure commonly referred to as the “Right to Vote on Taxes Act” was approved by the voters of the State of California at the November 5, 1996 general election (“Proposition 218”). Proposition 218 added Article XIIC (“Article XIIC”) and Article XIID to the California Constitution. According to the “Title and Summary” of Proposition 218 prepared by the California Attorney General, Proposition 218 limits “the authority of local governments to impose taxes and property-related assessments, fees and charges.” Generally, the provisions of Proposition 218 have not yet been interpreted by the courts, although a number of lawsuits have been filed requesting the courts to interpret various aspects of Proposition 218.

Among other things, Section 3 of Article XIIC states that “the initiative power shall not be prohibited or otherwise limited in matters of reducing or repealing any local tax, assessment, fee or charge.” Proposition 218 provides for a procedure, which includes notice, hearing, protest and voting requirements to alter the rate and method of apportionment of an existing special tax. However, Proposition 218 prohibits a legislative body from adopting any resolution to reduce the rate of any special tax or terminate the levy of any special tax pledged to repay any debt incurred pursuant to Proposition 218 unless such legislative body determines that the reduction or termination of the special tax would not interfere with the timely retirement of that debt. Although the matter is not free from doubt, it is likely that the exercise by the voters in Improvement Area No. 2 of the initiative power referred to in Article XIIC to reduce or terminate the Special Tax is subject to the same restrictions as are applicable to the District, pursuant to the Act. Accordingly, although the matter is not free from doubt, it is likely that Proposition 218 has not conferred on the voters in Improvement Area No. 2 the power to repeal or reduce the Special Taxes if such reduction would interfere with the timely retirement of the Bonds.

It may be possible, however, for voters or the District to reduce the Special Taxes in a manner which does not interfere with the timely repayment of the Bonds, but which does reduce the maximum amount of Special Taxes that may be levied in any year below the existing levels. Therefore, no assurance can be given with respect to the levy of Special Taxes for Administrative Expenses. Furthermore, no assurance can be given with respect to the future levy of the Special Taxes in amounts greater than the amount necessary for the timely retirement of the Bonds.

The interpretation and application of Proposition 218 will ultimately be determined by the courts with respect to a number of the matters discussed above, and it is not possible at this time to predict with certainty the outcome of such determination or the timeliness of any remedy afforded by the courts.

Ballot Initiatives and Legislative Measures

Proposition 218 was adopted pursuant to a measure qualified for the ballot pursuant to California’s constitutional initiative process and the State Legislature has in the past enacted legislation which has altered the spending limitations or established minimum funding provisions for particular activities. From time to time, other initiative measures could be adopted by California voters or legislation enacted by the State Legislature. The adoption of any such initiative or enactment of legislation might place limitations on the ability of the State, the City or local districts to increase revenues or to increase appropriations or on the ability of a property owner to complete the development of the property.

Early Bond Redemption

The Bonds are subject to optional, special mandatory and mandatory redemption prior to their respective stated maturities. Special mandatory redemption from prepayment of Bonds from amounts constituting prepayments of Special Taxes may occur on any date (see “**THE BONDS - Redemption**” herein).

Loss of Tax Exemption

As discussed under the caption “**LEGAL MATTERS - Tax Exemption**” herein, interest on the Bonds could become includable in gross income for purposes of federal income taxation retroactive to the date the Bonds were issued as a result of future acts or omissions of the District in violation of its covenants contained in the Fiscal Agent Agreement. Should such an event of taxability occur, the Bonds are not subject to special redemption or any increase in interest rate and will remain outstanding until maturity or until redeemed under one of the redemption provisions contained in the Fiscal Agent Agreement.

IRS Audits

The Internal Revenue Service (the “IRS”) has initiated an expanded program for the auditing of tax-exempt bond issues, including both random and targeted audits. It is possible that the Bonds will be

selected for audit by the IRS. It is also possible that the market value of the Bonds might be affected as a result of such an audit of the Bonds (or by an audit of similar bonds).

Secondary Market

There can be no guarantee that there will be a secondary market for the Bonds or, if a secondary market exists, that such Bonds can be sold for any particular price. Occasionally, because of general market conditions or because of adverse history or economic prospects connected with a particular issue, secondary marketing practices in connection with a particular issue are suspended or terminated. Additionally, prices of issues for which a market is being made will depend upon then prevailing circumstances. Such prices could be substantially different from the original purchase price.

SPECIAL TAXES AND DEBT SERVICE

Administration of the Special Tax

The District is required each Fiscal Year to determine the amount of Special Taxes within Improvement Area No. 2 needed to pay debt service on the Bonds and Administrative Expenses of the District related to Improvement Area No. 2 (the “Special Tax Requirement”). The District is expected to incur Administrative Expenses within Improvement Area No. 2 for the levy and collection of the Special Taxes, foreclosure proceedings, Fiscal Agent fees and arbitrage rebate calculations.

The District is required to communicate with the County Auditor to ascertain the relevant parcels within Improvement Area No. 2 on which the Special Taxes are to be levied, taking into account any parcel splits during the preceding and then current Fiscal Year. The District is required by resolution to provide for the levy of the Special Taxes within Improvement Area No. 2 in the then current Fiscal Year. A certified list of all parcels subject to the Special Tax, including the amount of the Special Tax to be levied on each such parcel, is filed by the District with the County Auditor on or before the tenth (10th) day of August of that tax year. The Special Taxes so levied may not exceed the authorized amounts as provided in the Rate and Method of Apportionment relating to Improvement Area No. 2 (see “**Rate and Method of Apportionment**” below).

The Special Taxes are payable and are collected in the same manner and at the same time and in the same installment as the general taxes on real property are payable and have the same priority, become delinquent at the same times and in the same proportionate amounts and bear the same proportionate penalties and interest after delinquency as do the general taxes on real property.

Special Taxes are due in two equal installments. Special Taxes levied become delinquent on the following December 10th and April 10th. Currently a 10% penalty is added to delinquent taxes.

When received, the Special Taxes are required to be deposited in a separate Special Tax Fund for Improvement Area No. 2 to be held by the City and transferred by the City to the Fiscal Agent as provided in the Fiscal Agent Agreement.

As of the delivery date of the Bonds, the District has retained Harris & Associates to assist in the preparation of the Special Tax roll and the determination of the amount of Special Taxes required in each Fiscal Year.

Rate and Method of Apportionment

The District levies the Special Taxes in accordance with the Rate and Method of Apportionment (see “**APPENDIX E - RATE AND METHOD OF APPORTIONMENT**”). Because the Special Taxes have been authorized by a two-thirds (2/3) vote of the qualified electorate within Improvement Area No. 2, the Special Taxes are a special tax imposed within the limitations of Section 4 of Article XIII A of the State Constitution. The City Council, as the legislative body of the District, has the power and is obligated, pursuant to the covenants contained in the Fiscal Agent Agreement, to cause the levy and collection of the Special Taxes annually.

The Rate and Method of Apportionment may be modified pursuant to the provisions of the Act provided that the District determines that such modification will not impair the timely payment of the Bonds.

The District has covenanted that no modification of the maximum authorized Special Tax shall be approved which would prohibit the District from levying the Special Tax in any Fiscal Year at such a rate as could generate Maximum Special Tax Revenues in each Fiscal Year at least equal to 110% of annual debt service in such Fiscal Year.

When a community facilities district is formed, a special tax may be levied on each parcel of taxable property within the community facilities district to pay for the construction, acquisition and rehabilitation of public facilities, to pay for authorized services or to repay bonded indebtedness or other related expenses incurred by the community facilities district. This special tax may be apportioned in any reasonable manner; however, the tax may not be apportioned on an *ad valorem* basis. Pursuant to Section 53325.3 of the Act, the tax imposed “is a Special Tax and not a special assessment, and there is no requirement that the tax be apportioned on the basis of benefit to any property.”

When more than one type of land use or houses of different sizes are present within a community facilities district, several criteria may be considered when apportioning the special tax. Generally, criteria are based on building square footage or residential floor area, acreage, and land use. Categories based on such criteria are established to differentiate between parcels of property. Specific special tax levels are assigned to each category, with all parcels within a category assigned the same special tax rate.

In Improvement Area No. 2 categories have been established for Developed Property, as shown in the tables below. The Special Tax for a single family residential property will vary directly with the amount of residential floor area on each parcel.

Assigned Special Tax Rates

The tables below show the Assigned Special Tax rates for Fiscal Year 2006/07 that are to be levied against Developed Property within Improvement Area No. 2. The Maximum Special Taxes for Developed Property cannot exceed the rates shown for Fiscal Year 2006/07, except when the Backup Special Tax is used as discussed below. The Assigned Special Taxes and Backup Special Taxes will increase at a rate of two percent per year.

Each year, the District shall levy the Special Tax within Improvement Area No. 2, subject to the methodology and Maximum Special Taxes set forth in the Rate and Method of Apportionment, in an amount sufficient to meet the Special Tax Requirement.

Backup Special Tax

Pursuant to the Rate and Method of Apportionment, the Maximum Special Tax for Developed Property within Improvement Area No. 2 is the greater of (i) the amount derived by application of the Assigned Special Tax or (ii) the amount derived by application of the Backup Special Tax. The Backup Special Tax will increase at a rate of two percent per year.

Under certain circumstances, the Special Tax for some parcels classified as Developed Property will be increased above the Assigned Special Tax until the Special Tax Requirement is met. However, under no circumstances will the Special Tax on an Assessor’s Parcel of Developed Property be increased above the greater of the Backup Special Tax or the applicable Assigned Special Tax.

The Assigned Special Tax Rates under the Rate and Method of Apportionment have been designed pursuant to City policy not to exceed a total tax rate percentage of 2% when taking into account all taxes and assessments on property of all jurisdictions. The following tables shows the assumptions used in setting the Assigned Tax Rates and the effective tax rate within Improvement Area No. 2.

Delinquencies and Foreclosure Actions

No parcels within Improvement Area No. 2 have experienced any delinquencies.

The District has covenanted to initiate foreclosure action in the superior court against parcels with delinquent Special Taxes as provided in the Fiscal Agent Agreement.

Foreclosure proceedings are directed by the District through a notification to foreclosure counsel as to the delinquent assessor parcel numbers for which foreclosure proceedings are to be initiated. The District first removes the delinquent Special Taxes from the County Tax Roll, as required by law. Foreclosure

counsel then initiates a request for a title search to identify the current legal owner of a delinquent parcel. Foreclosure counsel also sends a written demand for payment to the owner shown on the County Tax Roll, followed by the filing of a complaint with the Superior Court (the “Court”) in Riverside County and recording a *lis pendens* against the property at the office of the County Recorder.

Each legal owner and all holders of any other interest in the land must file an answer to the complaint within 30 days following the completion of service of process on them. If no answer is filed within such 30-day period, foreclosure counsel files a request that a default judgment be entered by the Court. If any party files an answer, then the case must be litigated, and foreclosure counsel will typically file a motion for summary judgment.

Following the entry of a judgment, whether by default or otherwise, against all defendants, foreclosure counsel requests a writ of sale from the Court for delivery to the Riverside County Sheriff’s Department (the “Sheriff”). The writ of sale is delivered to the Sheriff with instructions to execute on the delinquent parcel. Levy by the Sheriff consists of posting notice on the delinquent property, followed by mailing of notice to the last known address of the legal owner and publication of the notice of levy.

Thereafter, the delinquent property owner is entitled to a redemption period of 120 days. Following such 120-day period, foreclosure proceedings can continue following the publication and mailing of a notice of sale of the delinquent parcel or parcels, which sale must be at least 20 days following such notice. The foreclosure process described above typically takes at least six months from the date on which a judgment is entered and can take substantially longer.

CITY OF LAKE ELSINORE
COMMUNITY FACILITIES DISTRICT 2004-3 (ROSETTA CANYON)
IMPROVEMENT AREA NO. 2
EFFECTIVE TAX RATES
Fiscal Year 2006-2007

Zone 1

Home Square Footage	1,951 - 2,200	2,201 - 2,450	2,451 - 2,700	2,701 - 2,950	2,951 - 3,200
Lowest Base Price*	\$359,990.00	\$379,990.00	\$386,990.00	\$399,990.00	\$417,990.00
Less \$7,000 Homeowners Exemption	<u>(\$7,000.00)</u>	<u>(\$7,000.00)</u>	<u>(\$7,000.00)</u>	<u>(\$7,000.00)</u>	<u>(\$7,000.00)</u>
Net Assessed Value	\$352,990.00	\$372,990.00	\$379,990.00	\$392,990.00	\$410,990.00

Ad Valorem

Base Property Tax (1.0052%)	\$3,548.26	\$3,749.30	\$3,819.66	\$3,950.34	\$4,131.27
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Fixed Charges

Other Fixed Charges, Assessment and Special Taxes	\$517.53	\$517.53	\$517.53	\$517.53	\$517.53
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Assessments and Special Taxes

CFD 2005-1 IA No. B (School District)	\$689.00	\$727.00	\$741.00	\$756.00	\$788.00
CFD 2004-3 IA No. 2	<u>\$2,460.18</u>	<u>\$2,642.48</u>	<u>\$2,712.45</u>	<u>\$2,782.41</u>	<u>\$2,938.32</u>

Total Property Taxes	\$7,214.97	\$7,636.31	\$7,790.64	\$8,006.28	\$8,375.12
Annual Home Tax Rate (%)**	2.00%	2.01%	2.01%	2.00%	2.00%

*Base price subject to change by the Developer to reflect market conditions.

** Based upon debt Service coverage on the Bonds of 125%, the expected effective tax rate is less than 2%.

**CITY OF LAKE ELSINORE
COMMUNITY FACILITIES DISTRICT 2004-3 (ROSETTA CANYON)
IMPROVEMENT AREA NO. 2
EFFECTIVE TAX RATES
FISCAL YEAR 2006-2007**

Zone 2

	2,201 - 2,450	2,451 - 2,700	2,701 - 2,950	3,201 - 3,450	3,451 - 3,700	Greater 3,950
Home Square Footage						
Lowest Base Price	\$376,990.00	\$419,990.00	\$407,990.00	\$429,990.00	\$459,990.00	\$537,990.00
Less \$7,000 Homeowners Exemption	<u>(\$7,000.00)</u>	<u>(\$7,000.00)</u>	<u>(\$7,000.00)</u>	<u>(\$7,000.00)</u>	<u>(\$7,000.00)</u>	<u>(\$7,000.00)</u>
Net Assessed Value	\$369,990.00	\$412,990.00	\$400,990.00	\$422,990.00	\$452,990.00	\$530,990.00
Ad Valorem						
Base Property Tax (1.0052%)	\$3,719.14	\$4,151.38	\$4,030.75	\$4,251.90	\$4,553.46	\$5,337.51
Fixed Charges						
Other Fixed Charges, Assessment and Special Taxes	\$517.53	\$517.53	\$517.53	\$517.53	\$517.53	\$517.53
Assessments and Special Taxes						
CFD 2005-1 IA No. B (School District)	\$773.46	\$801.57	\$817.73	\$867.41	\$899.81	\$925.03
CFD 2004-3 IA No. 2	<u>\$2,900.98</u>	<u>\$3,035.30</u>	<u>\$3,116.16</u>	<u>\$3,356.45</u>	<u>\$3,512.65</u>	<u>\$3,636.78</u>
Total Property Taxes	\$7,911.11	\$8,505.78	\$8,482.17	\$8,993.29	\$9,483.45	\$10,416.85
Annual Home Tax Rate (%)**	2.10%	2.03%	2.08%	2.09%	2.06%	1.94%

*Base price subject to change by the Developer to reflect market conditions

** Based upon debt Service coverage on the Bonds of 125%, the expected effective tax rate is less than 2%.

Debt Service Coverage

The following table presents the projected annual coverage on the Bonds based upon the realization of certain assumptions and the aggregate Assigned Special Tax Rates. No allowance was made for delinquencies. The projection assumes build out at the unit mix shown on the tables. Unit mix is subject to change to reflect then current market conditions.

Until such time as the receipt of Special Taxes from the levy of the assigned tax rate is sufficient to pay debt service on Bonds, the Rate and Method Apportionment provides for the levy of an undeveloped property tax (see “**APPENDIX E - Rate and Method of Apportionment**” and “**Concentration of Property Ownership**” above).

The receipt of Special Taxes is subject to several variables described herein. The District provides no assurance that the Special Taxes and the coverage ratios shown will be achieved.

**TABLE NO. 1
CITY OF LAKE ELSINORE
COMMUNITY FACILITIES DISTRICT 2004-3
(ROSETTA CANYON) IMPROVEMENT AREA NO. 2
PROJECTION OF THE ASSIGNED SPECIAL TAX
FISCAL YEAR 2006/07**

Zone 1			
Residential Floor Area	Assigned Special Tax	Number of Units*	Total Special Taxes
2,951 - 3,200	\$2,938.32	47	\$138,101.24
2,701 - 2,950	\$2,782.41	88	\$244,851.82
2,451 - 2,700	\$2,712.45	32	\$86,798.25
2,201 - 2,450	\$2,642.48	23	\$60,777.12
1,951 - 2,200	\$2,460.18	<u>23</u>	<u>\$56,584.11</u>
SUBTOTAL		213	\$587,112.53
Zone 2			
Residential Floor Area	Assigned Special Tax	Number of Units*	Total Special Taxes
Greater Than 3,950	\$3,636.78	43	\$156,381.51
3,451 - 3,700	\$3,512.65	65	\$228,321.95
3,201 - 3,450	\$3,356.45	90	\$302,080.75
2,951 - 3,200	\$3,236.05	0	\$0.00
2,701 - 2,950	\$3,116.16	45	\$140,227.25
2,451 - 2,700	\$3,035.30	23	\$69,811.80
2,201 - 2,450	\$2,900.98	<u>24</u>	<u>\$69,623.57</u>
SUBTOTAL		290	\$966,446.84
TOTAL		<u>503</u>	<u>\$1,553,559.37</u>

*Unit mix may be changed by the Developer to reflect then current market conditions.

TABLE NO. 2
COMMUNITY FACILITIES DISTRICT NO. 2004-3
(ROSETTA CANYON) SPECIAL TAX BONDS (IMPROVEMENT AREA NO. 2)
2006 SERIES A
DEBT SERVICE COVERAGE

Fiscal	Special Taxes					
Year	Assumed	Administrative	Net Special	Debt Service	Coverage	
	Assigned Rate	Expense	Taxes		Ratio	
2007	\$1,553,559	(\$25,150)	\$1,528,409	\$1,154,319	1.32	
2008	1,584,631	(25,653)	1,558,978	1,245,073	1.25	
2009	1,616,323	(26,166)	1,590,157	1,268,873	1.25	
2010	1,648,650	(26,689)	1,621,960	1,291,590	1.26	
2011	1,681,623	(27,223)	1,654,399	1,318,190	1.26	
2012	1,715,255	(27,768)	1,687,487	1,348,378	1.25	
2013	1,749,560	(28,323)	1,721,237	1,371,853	1.25	
2014	1,784,551	(28,889)	1,755,662	1,398,978	1.25	
2015	1,820,242	(29,467)	1,790,775	1,429,318	1.25	
2016	1,856,647	(30,057)	1,826,591	1,457,568	1.25	
2017	1,893,780	(30,658)	1,863,122	1,488,793	1.25	
2018	1,931,656	(31,271)	1,900,385	1,517,043	1.25	
2019	1,970,289	(31,896)	1,938,393	1,548,043	1.25	
2020	2,009,695	(32,534)	1,977,160	1,576,543	1.25	
2021	2,049,889	(33,185)	2,016,704	1,612,543	1.25	
2022	2,090,886	(33,849)	2,057,038	1,640,543	1.25	
2023	2,132,704	(34,526)	2,098,179	1,674,603	1.25	
2024	2,175,358	(35,216)	2,140,142	1,710,283	1.25	
2025	2,218,865	(35,920)	2,182,945	1,742,323	1.25	
2026	2,263,243	(36,639)	2,226,604	1,780,723	1.25	
2027	2,308,508	(37,372)	2,271,136	1,814,963	1.25	
2028	2,354,678	(38,119)	2,316,559	1,849,563	1.25	
2029	2,401,771	(38,881)	2,362,890	1,884,700	1.25	
2030	2,449,807	(39,659)	2,410,148	1,925,113	1.25	
2031	2,498,803	(40,452)	2,458,351	1,965,275	1.25	
2032	2,548,779	(41,261)	2,507,518	2,004,925	1.25	
2033	2,599,754	(42,086)	2,557,668	2,043,800	1.25	
2034	2,651,749	(42,928)	2,608,821	2,081,638	1.25	
2035	2,704,784	(43,787)	2,660,998	2,123,175	1.25	
2036	2,758,880	(44,662)	2,714,218	2,167,888	1.25	
2037	2,814,058	(45,556)	2,768,502	2,210,250	1.25	

THE CITY

The City of Lake Elsinore (the “City”) was founded in 1883 and incorporated on April 23, 1888, and in 1893 the Elsinore Valley, previously in San Diego County, became a part of the new County of Riverside. The City is located 73 miles east of Los Angeles, 472 miles south of San Francisco, and 74 miles north of San Diego. It covers an area of approximately 39.1 square miles with 10.5 miles of lake shore and has an elevation of 1,258 feet above sea level.

The City is incorporated as a general law city. The City has a Council/Manager form of municipal government. The City Council appoints the City Manager who is responsible for the day-to-day administration of City business and the coordination of all departments of the City. The City Council is composed of five members elected bi-annually at large to four-year alternating terms. The mayor is selected by the City Council from among its members. The City employs a staff of 37 full-time employees and 18 part-time employees under the direction of the City Manager.

The City Council members and term expiration dates are as follows:

<u>Council Members</u>	<u>Term Expires</u>
Robert Magee, Mayor	November, 2008
Robert Schiffner, Mayor Pro Tem	November, 2008
Genie Kelley, Member	November, 2008
Thomas Buckley, Member	November, 2006
Daryl Hickman, Member	November, 2006

Current City administrative staff include:

Robert Brady, *City Manager*

Matt N. Pressey, *Director of Administrative Services*

Frederick Ray, *City Clerk*

As of the delivery date of the Bonds, the District has retained Harris & Associates to assist in the preparation of the Special Tax roll and the determination of the amount of Special Taxes required in each Fiscal Year.

IMPROVEMENT AREA NO. 2

The information set forth herein regarding ownership of real property in Improvement Area No. 2, the Developer and any proposed development of property in Improvement Area No. 2 was provided by the Developer and has not been independently verified. The District makes no representation as to the accuracy or completeness of any such information. This information has been included because it is considered relevant to an informed evaluation of Improvement Area No. 2. As development of property in Improvement Area No. 2 has not been completed, no assurance can be given that it will occur, that it will occur as described herein, or that it will occur in a timely manner. The information should not be construed to suggest that the Bonds or the Special Taxes that will be used to pay the Bonds are personal obligations of the Developer.

The owner of property within Improvement Area No. 2 will not be personally liable for payments of the Special Taxes to be applied to pay the principal of and interest on the Bonds. Accordingly, the Developer's financial statements have not been included in this Official Statement. Furthermore, no representation is made that the Developer will have funds available to complete the development within Improvement Area No. 2.

Boundaries of Improvement Area No. 2

The boundaries of the District coincide with the development generally known as Rosetta Canyon. The District is located 1 1/2 miles east of the Interstate 15 freeway and south of Highway 74. Development within Improvement Area No. 2 is planned for 503 single family homes on approximately 153.31 gross acres (the "Development").

The boundaries of the District are described on the reduced scale map entitled "Boundary Map of Community Facilities District No. 2004-3 (Rosetta Canyon)." A full scale map is on file with the Clerk of the City of Lake Elsinore and was recorded with the County Recorder, County of Riverside in Book 60 Page 46-47 of Maps of Assessment and Community Facilities Districts, Document Number 2005-0006006.

Facilities and Fees to be Financed by the District

The District is authorized to issue the Bonds to fund the planning, design, permitting and construction of public infrastructure consisting primarily of street, sewer and water, as well as the funding of facilities included in the City and Elsinore Valley Municipal Water District fee programs. Table No. 3 summarizes authorized District facilities which are to be designed, acquired or constructed from proceeds of the Bonds.

City of Lake Elsinore
Community Facilities District No 2004-3
Improvement Area 2
Rosetta Canyon

Interstate  Frwy

Hwy 74

Wasson Canyon Rd

Boundaries Approximate

9901 080506



**TABLE NO. 3
CITY OF LAKE ELSINORE
COMMUNITY FACILITIES DISTRICT 2004-3 (ROSETTA CANYON)
ELIGIBLE FACILITIES COSTS
(Estimated Costs)**

Facilities	<u>Estimated Cost</u>
Street Improvements	\$2,637,285
Storm Drain Improvements	\$4,902,831
Sewer Improvements	\$2,884,755
Domestic Water Improvements	\$13,441,285
Reclaimed Water Improvements	\$889,104
Fire Facilities & Equipment	\$4,570,000
City Development Impact Fees	\$8,753,418
EVMWD Sewer & Water Master Planning	\$103,000
EVMWD Sewer & Water Connection Fees	<u>\$7,851,348</u>
Total	\$46,033,026

The City has entered into a Joint Community Facilities Agreement with the Elsinore Valley Municipal Water District with respect to the portion of the facilities to be owned by that agency.

To the extent the proceeds of the Bonds are insufficient to fund all of the eligible costs for all of the Facilities, such costs will be borne by the Developer.

The Developer

Centex Homes, a Nevada general partnership (“Centex Homes” or “Developer”), is one of the nation’s largest home builders, operating in major markets in 25 states. Centex Homes constructed approximately 39,000 homes in its most recent fiscal year ended March 31, 2006. In general, Centex Homes buys and develops lots and land and builds single family detached homes, townhomes and low rise condominiums for sale to both first time and move up buyers. Centex Homes has operated in the Inland Empire (comprising portions of San Bernardino and Riverside Counties) since 1987.

Further information regarding the Developer is available from its internet website www.centexhomes.com. *This Internet address is included for reference only and the information on the Internet site is not a part of this Official Statement or incorporated by reference into this Official Statement. No representation is made in this Official Statement as to the accuracy or adequacy of the information contained on the Internet site.*

Centex Homes is the home building subsidiary of Centex Home Corporation (“Centex Corporation”), a publicly traded company whose common stock is traded on the New York Stock Exchange under the symbol “CTX.” The managing general partner of Centex Homes is Centex Homes Real Estate Corporation, a Nevada Corporation (“Centex Homes Real Estate Corporation”), another subsidiary of Centex Corporation. Centex Corporation’s Annual Report on Form 10-K for fiscal year ended March 31, 2006, as filed by Centex Corporation with the Commission pursuant to the Exchange Act, as amended, sets forth certain data relative to the consolidated financial position of Centex Corporation and its subsidiaries as of that date. The Securities and Exchange Commission (the “Commission”) maintains an Internet website that contains reports, proxy and information statements and other information regarding registrants that file electronically with the Commission, including Centex Corporation. The address of such Internet website is www.sec.gov. Information may also be obtained from the company itself at Centex Homes Headquarters, 2728 North Harwood, Dallas, Texas 75201, telephone number: (214) 981-5000.

Description of Development

The following section describes the proposed development in terms of the size and prices of the units. There can be no assurance that the development plan described herein will be completed or that it will not be modified in the future. In addition, there can be no assurance that sufficient funds will or can be made available to complete the development plan or pay special taxes as described.

There are 503 homes proposed to be built within 4 residential communities in Improvement Area No. 2. The residential communities are known as Fox & Jacobs, 213 homes; Santa Rosa, 98 homes; Caraway, 78 homes; and Augusta II, 114 homes and are described below.

TRACT NO. 25477 FOX & JACOBS

	Number of Homes	Square Footage	Base Price
	23	1,979	\$359,990
	23	2,400	\$379,990
	32	2,613	\$386,990
	43	2,710	\$386,990
	45	2,873	\$399,990
	47	3,113	\$417,990
Total or Average	213	2,706	\$388,657

TRACT NO. 25476 SANTA ROSA

	Number of Homes	Square Footage	Base Price
	24	2,266	\$376,990
	17	2,710	\$407,990
	30	3,206	\$429,990
	27	3,487	\$459,990
Total or Average	98	2,967	\$418,740

TRACT NO. 25476 CARAWAY

	Number of Homes	Square Footage	Base Price
	23	2,648	\$419,990
	28	2,916	\$449,990
	27	3,258	\$469,990
Total or Average	78		

TRACT NO. 25476 AUGUSTA II

	Number of Homes	Square Footage	Base Price
	33	3,242	\$486,990
	38	3,613	\$519,990
	43	4,063	\$537,990
Total or Average	114		

STATUS OF DEVELOPMENT

	Fox & Jacobs	Santa Rosa	Caraway	Augusta II	Total
Blue Top Lots			12	45	57
Finished Lots	180	98	66	69	413
Building Permits Issued	213	3	78	114	408
Model Homes	N/A	3	N/A	N/A	3
Production Units Started	33				33
Production Units Completed	0				0
Homes Sold	45	9	3	2	59
Escrows Closed	0	0	0	0	0

Financing Plan

The Developer estimates a total cost of approximately \$54,018,370 to develop finished lots. As of July 15, 2006, the Developer has spent approximately \$28,805,427 on planning, engineering, grading and infrastructure.

Bond proceeds are expected to finance \$19,150,000 of the \$25,212,943 remaining. The Developer expects to finance the balance from internal sources.

There is no assurance that amounts necessary to finance the Developer's remaining site development costs within Improvement Area No. 2 will be available from the Developer or any other source, when needed. Neither the Developer nor any of its members or affiliates, or any lender, is under any legal obligation of any kind to expend funds for the development of the property in Improvement Area No. 2. Any internal funding by the Developer or its members or affiliates, or borrowing under any loan arrangement, to finance its development and home construction costs is entirely voluntary.

History of Property Tax Payment; Loan Defaults; Bankruptcy.

Centex Homes has numerous divisions and affiliates consisting of various entities that are developing or have been involved in the development of numerous projects over an extended period of time. As a large, nation-wide developer of residential projects, Centex Homes cannot represent with assurance that neither it nor any affiliate has ever been delinquent in the payment of *ad valorem* property taxes. However, to the actual knowledge of Centex Homes, the Inland Empire division of Centex Homes has never been delinquent in a material payment of any *ad valorem* property tax, special assessment or special taxes on property included within the boundaries of (i) one of its residential developments within the County, (ii) a community facilities district within the County, or (iii) an assessment district within the County.

Centex Homes also represents that neither it nor any entity in which it has an ownership interest is in default on any loans, lines of credit or other obligation related to its development in the District or its other projects in the County which default would in any way materially and adversely affect its ability to develop its property within the District or to pay the Special Taxes for which it is responsible.

Centex Homes also represents that there is no action, suit, proceeding, inquiry or investigation at law or in equity, before or by any court, regulatory agency, public board or body, pending against it (with service of process having been accomplished), or, to the actual knowledge of Centex Homes, pending against any affiliate or, to the actual knowledge of Centex Homes, threatened, which if successful, would materially adversely affect the ability of Centex Homes to complete the development of its property within the District or to pay Special Taxes or *ad valorem* tax obligations on its property within the District when due.

LEGAL MATTERS

Enforceability of Remedies

The remedies available to the Fiscal Agent and the Owners of the Bonds upon an event of default under the Fiscal Agent Agreement or 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 certain legal rights related to the Fiscal Agent Agreement is 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.

Approval of Legal Proceedings

Fulbright & Jaworski L.L.P., Los Angeles, California, as Bond Counsel, will render an opinion which states that the Fiscal Agent Agreement and the Bonds are valid and binding contracts of the City and are enforceable in accordance with their terms. Fulbright & Jaworski L.L.P. will render an opinion which states that the Fiscal Agent Agreement and the Bonds are valid and binding contracts of the District and are enforceable in accordance with their terms. The legal opinions of Bond Counsel will be subject to the effect of bankruptcy, insolvency, moratorium and other similar laws affecting creditors' rights and to the exercise of judicial discretion in accordance with general principles of equity. Bond Counsel undertakes no responsibility for the accuracy, completeness or fairness of this Official Statement.

The City has no knowledge of any fact or other information which would indicate that the Fiscal Agent Agreement is not so enforceable against the District, except to the extent such enforcement is limited by principles of equity and by state and federal laws relating to bankruptcy, reorganization, moratorium or creditors' rights generally.

Certain legal matters will be passed on for the City and the District by Leibold, McClendon & Mann, P.C., Laguna Hills, California, as City Attorney. In addition, certain legal matters will be passed on by Fulbright & Jaworski L.L.P., Los Angeles, California, Disclosure Counsel. Certain legal matters will be passed on for the Underwriter by McFarlin & Anderson LLP, Lake Forest, California, as Underwriter's Counsel.

Fees payable to Bond Counsel, City Attorney, Disclosure Counsel and Underwriter's Counsel are contingent upon the sale and delivery of the Bonds.

Tax Exemption

The Internal Revenue Code of 1986 (the "Code") imposes certain requirements that must be met subsequent to the issuance and delivery of the Bonds for interest thereon to be and remain excluded pursuant to section 103(a) of the Code from the gross income of the owners thereof for federal income tax purposes. Noncompliance with such requirements could cause the interest on the Bonds to be included in the gross income of the owners thereof for federal income tax purposes retroactive to the date of issuance of the Bonds. The District has covenanted to maintain the exclusion of the interest on the Bonds from the gross income of the owners thereof for federal income tax purposes.

In the opinion of Fulbright & Jaworski L.L.P., Bond Counsel, under existing law interest on the Bonds is exempt from personal income taxes of the State of California and, assuming compliance with the aforementioned covenant, interest on the Bonds is excluded pursuant to section 103(a) of the Code from the gross income of the owners thereof for federal income tax purposes. Bond Counsel is also of the opinion that, assuming compliance with the aforementioned covenant, the Bonds are not "specified private activity bonds" within the meaning of section 57(a)(5) of the Code and, therefore, the interest on

the Bonds will not be treated as an item of tax preference for purposes of computing the alternative minimum tax imposed by section 55 of the Code. The receipt or accrual of interest on the Bonds owned by a corporation may affect the computation of its alternative minimum taxable income, upon which the alternative minimum tax is imposed, to the extent that such interest is taken into account in determining the adjusted current earnings of that corporation (75 percent of the excess, if any, of such adjusted current earnings over the alternative minimum taxable income being an adjustment to alternative minimum taxable income (determined without regard to such adjustment or to the alternative tax net operating loss deduction)).

The excess, if any, of the stated redemption price at maturity of Bonds of a maturity over the initial offering price to the public of the Bonds of that maturity set forth on the cover of this Official Statement is “original issue discount” under the Code. Such original issue discount accruing on a Bond is treated as interest excluded from the gross income of the owner thereof for federal income tax purposes and exempt from California personal income tax to the same extent as would be stated interest on the Bond. Original issue discount on any Bond purchased at such initial offering price and pursuant to such initial offering will accrue on a semiannual basis over the term of the Bond on the basis of a constant yield method and, within each semiannual period, will accrue on a ratable daily basis. The amount of original issue discount on such a Bond accruing during each period is added to the adjusted basis of such Bond to determine taxable gain upon disposition (including sale, redemption or payment on maturity) of such Bond. The Code includes certain provisions relating to the accrual of original issue discount in the case of purchasers of Bonds who purchase such Bonds other than at the initial offering price and pursuant to the initial offering.

Any person considering purchasing a Bond of a maturity having original issue discount should consult his or her own tax advisors with respect to the tax consequences of ownership of Bonds with original issue discount, including the treatment of purchasers who do not purchase in the original offering and at the original offering price, the allowance of a deduction for any loss on a sale or other disposition, and the treatment of accrued original issue discount on such Bonds under federal individual and corporate alternative minimum taxes.

Bond Counsel has not undertaken to advise in the future whether any events after the date of issuance of the Bonds may affect the tax status of interest on the Bonds or the tax consequences of the ownership of the Bonds. No assurance can be given that future legislation, or amendments to the Code, if enacted into law, will not contain provisions that could directly or indirectly reduce the benefit of the exemption of interest on the Bonds from personal income taxation by the State of California or of the exclusion of the interest on the Bonds from the gross income of the owners thereof for federal income tax purposes. Furthermore, Bond Counsel expresses no opinion as to any federal, state or local tax law consequences with respect to the Bonds, or the interest thereon, if any action is taken with respect to the Bonds or the proceeds thereof predicated or permitted upon the advice or approval of bond counsel if such advice or approval is given by counsel other than Bond Counsel.

Although Bond Counsel is of the opinion that interest on the Bonds is exempt from State personal income tax and excluded from the gross income of the owners thereof for federal income tax purposes, an owner’s federal, state or local tax liability may be otherwise affected by the ownership or disposition of the Bonds. The nature and extent of these other tax consequences will depend upon the owner’s other items of income or deduction. Without limiting the generality of the foregoing, prospective purchasers of the Bonds should be aware that (i) section 265 of the Code denies a deduction for interest on indebtedness incurred or continued to purchase or carry the Bonds or, in the case of a financial institution, that portion of an owner’s interest expense allocated to interest on the Bonds, (ii) with respect to insurance companies subject to the tax imposed by section 831 of the Code, section 832(b)(5)(B)(i) reduces the deduction for loss reserves by 15 percent of the sum of certain items, including interest on the Bonds, (iii) interest on the Bonds earned by certain foreign corporations doing business in the United States could be subject to a branch profits tax imposed by section 884 of the Code, (iv) passive investment income, including interest on the Bonds, may be subject to federal income taxation under section 1375 of the Code for Subchapter S corporations that have Subchapter C earnings and profits at the close of the taxable year if greater than 25% of the gross receipts of such Subchapter S corporation is passive investment income, (v) section 86

of the Code requires recipients of certain Social Security and certain Railroad Retirement benefits to take into account, in determining the taxability of such benefits, receipts or accruals of interest on the Bonds and (vi) under section 32(i) of the Code, receipt of investment income, including interest on the Bonds, may disqualify the recipient thereof from obtaining the earned income credit. Bond Counsel has expressed no opinion regarding any such other tax consequences.

Bond Counsel's opinion is not a guarantee of a result, but represents their legal judgment based upon their review of existing statutes, regulations, published rulings and court decisions and the covenants of the District described above. No ruling has been sought from the Internal Revenue Service (the "Service") with respect to the matters addressed in the opinion of Bond Counsel, and Bond Counsel's opinion is not binding on the Service. The Service has an ongoing program of auditing the tax-exempt status of the interest on municipal obligations. If an audit of the Bonds is commenced, under current procedures the Service is likely to treat the District as the "taxpayer," and the owners would have no right to participate in the audit process. In responding to or defending an audit of the tax-exempt status of the interest on the Bonds, the District may have different or conflicting interests from the owners of the Bonds. Public awareness of any future audit of the Bonds could adversely affect the value and liquidity of the Bonds during the pendency of the audit, regardless of the ultimate outcome.

Absence of Litigation

The City will furnish a certificate dated as of the date of delivery of the Bonds that there is not now known to be pending or threatened any litigation restraining or enjoining the execution or delivery of the Fiscal Agent Agreement or the sale or delivery of the Bonds or in any manner questioning the proceedings and authority under which the Fiscal Agent Agreement is to be executed or delivered or the Bonds are to be delivered or affecting the validity thereof.

CONCLUDING INFORMATION

No Rating on the Bonds

The District has not made, and does not contemplate making, any application for a rating on the Bonds. No such rating should be assumed based upon any other City rating that may be obtained. Prospective purchasers of the Bonds are required to make independent determinations as to the credit quality of the Bonds and their appropriateness as an investment. Should a Bondowner elect to sell a Bond prior to maturity, no representations or assurances can be made that a market will have been established or maintained for the purchase and sale of the Bonds. The Underwriter assumes no obligation to establish or maintain such a market and is not obligated to repurchase any of the Bonds at the request of the owner thereof.

Underwriting

Southwest Securities, Inc., Newport Beach, California (the “Underwriter”) is offering the Bonds at the prices set forth on the cover page hereof. The initial offering prices may be changed from time to time and concessions from the offering prices may be allowed to dealers, banks and others. The Underwriter has agreed to purchase the Bonds at a price equal to approximately 97.894519% (\$22,966,054.05) of the aggregate principal amount of the Bonds, which amount represents the principal amount of the Bonds, less the Underwriter’s discount of \$469,200.00 and an original issue discount of \$24,745.95. The Underwriter will pay certain of its expenses relating to the offering.

Experts

The Market Absorption Study prepared by Empire Economics, Inc., Capistrano Beach, California, and the Appraisal prepared by Harris Realty Appraisal, Newport Beach, California, as well as the Special Tax projections prepared by Harris & Associates, Irvine, California, Special Tax Consultant, have been included in this Official Statement in reliance on and upon the authority of said firms as experts in the matters covered therein.

The Financing Consultant

The material contained in this Official Statement was prepared by Rod Gunn Associates, Inc., Huntington Beach, California, an independent financial consulting firm, who advised the City as to the financial structure and certain other financial matters relating to the Bonds. The information set forth herein has been obtained by Rod Gunn Associates, Inc. from sources which are believed to be reliable, but such information is not guaranteed by Rod Gunn Associates, Inc. as to accuracy or completeness, nor has it been independently verified. Fees paid to Rod Gunn Associates, Inc. are contingent upon the sale and delivery of the Bonds.

Additional Information

The summaries and references contained herein with respect to the Fiscal Agent Agreement, the Bonds, statutes and other documents, do not purport to be comprehensive or definitive and are qualified by reference to each such document or statute and references to the Bonds are qualified in their entirety by reference to the form hereof included in the Fiscal Agent Agreement. Definitions of certain terms used herein are set forth in “APPENDIX A-Definitions of Certain Terms Used In the Fiscal Agent Agreement.” Copies of the Fiscal Agent Agreement are available for inspection during the period of initial offering on the Bonds at the offices of the Underwriter, Southwest Securities, Inc., 620 Newport Center Drive, Suite 300, Newport Beach, California 92660, telephone (949) 717-2000. Copies of these documents may be obtained after delivery of the Bonds from the City through the City Manager, City of Lake Elsinore, 130 S. Main Street, Lake Elsinore, California 92530.

References

Any statements 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 City and the purchasers or Owners of any of the Bonds.

Execution

The execution of this Official Statement by the City Manager has been duly authorized by the City of Lake Elsinore.

CITY OF LAKE ELSINORE

By: /s/ Robert Brady
City Manager of the City,
Acting on behalf of Community Facilities
District No. 2004-3 (Rosetta Canyon)

APPENDIX A

DEFINITIONS OF CERTAIN TERMS USED IN THE FISCAL AGENT AGREEMENT

Unless otherwise defined in this Official Statement, the following terms have the following meanings.

“Act” means the Mello-Roos Community Facilities Act of 1982, as amended, Sections 53311 et seq. of the California Government Code.

“Administrative Expenses” means the administrative costs with respect to the calculation and collection of the Special Taxes, including all attorneys’ fees and other costs related thereto, the fees and expenses of the Fiscal Agent, any fees for credit enhancement for the Bonds which are not otherwise paid as Costs of Issuance, any costs related to the CFD’s compliance with State and federal laws requiring continuing disclosure of information concerning the Bonds and the CFD, and any other costs otherwise incurred by the City’s staff on behalf of the CFD in order to carry out the purposes of the CFD as set forth in the Resolution of Formation and any obligation of the CFD under the Fiscal Agent Agreement.

“Annual Debt Service” means the principal amount of any Outstanding Bonds payable in a Bond Year either at maturity or pursuant to a Sinking Fund Payment and any interest payable on any Outstanding Bonds in such Bond Year, if the Bonds are retired as scheduled.

“Authorized Investments” means any of the following which at the time of investment are legal investments under the laws of the State for the moneys proposed to be invested therein:

(1) Direct obligations of the United States of America (including obligations issued or held in book-entry form on the books of the Department of the Treasury, and CATS and TIGRS) or obligations the principal of and interest on which are unconditionally guaranteed by the United States of America (“Direct Obligations”).

(2) Bonds, debentures, notes or other evidence of indebtedness issued or guaranteed by any of the following federal agencies and provided such obligations are backed by the full faith and credit of the United States of America (stripped securities are only permitted if they have been stripped by the agency itself):

U.S. Export-Import Bank (“Eximbank”)

Direct obligations or fully guaranteed certificates of beneficial ownership

Farmers Home Administration (“FmHA”)

Certificates of beneficial ownership

Federal Financing Bank

Federal Housing Administration Debentures (“FHA”)

General Services Administration

Participation certificates

Government National Mortgage Association (“GNMA” or “Ginnie Mae”)

GNMA-guaranteed mortgage-backed bonds

GNMA-guaranteed pass-through obligations

U.S. Maritime Administration

Guaranteed Title XI financing

U.S. Department of Housing and Urban Development (HUD)

Project Notes

Local Authority Bonds

New Communities Debentures - U.S. government guaranteed debentures

U.S. Public Housing Notes and Bonds - U.S. government guaranteed public housing notes and bonds

(3) Bonds, debentures, notes or other evidence of indebtedness issued or guaranteed by any of the following non-full faith and credit U.S. government agencies (stripped securities are only permitted if they have been stripped by the agency itself):

Federal Home Loan Bank System

Senior debt obligations

Federal Home Loan Mortgage Corporation (“FHLMC” or “Freddie Mac”)

Participation certificates

Senior debt obligations

Federal National Mortgage Association (“FNMA” or “Fannie Mae”)

Mortgage-backed securities and senior debt obligations

Student Loan Marketing Association (“SLMA” or “Sallie Mae”)

Senior debt obligations

Resolution Funding Corp. (“REFCORP”) obligations

Farm Credit System CM. - Consolidated system-wide bonds and notes

(4) Money market funds registered under the Federal Investment Company Act of 1940, whose shares are registered under the Securities Act of 1933, and having a rating by Standard & Poor’s of “AAAm-G”, “AAAm” or “AAm”, and, if rated by Moody’s, rated “Aaa”, “Aa1” or “Aa2” (including those of the Fiscal Agent and its affiliates).

(5) Certificates of deposit secured at all times by collateral described in (1) and/or (2) above. Such certificates must be issued by commercial banks, savings and loan associations or mutual savings banks. The collateral must be held by a third party and the Bondholders must have a perfected first security interest in the collateral.

(6) Certificates of deposit, savings accounts, deposit accounts or money market deposits which are fully insured by FDIC or which are with a bank rated “AA” or better by Standard & Poor’s and “Aa” or better by Moody’s (including those of the Fiscal Agent and its affiliates).

(7) Investment Agreements with any corporation, including banking or financial institutions, provided that

(a) the long-term debt of the provider of any such investment agreement is rated, at the time of investment, at least “AA” and “Aa” by the Rating Agency (without regard to gradations of plus or minus within such category), and

(b) any such investment agreement is collateralized with United States Treasury or agency obligations which at least equal 102% of the principal amount invested thereunder, and

(c) any such agreement shall include a provision to the effect that, in the event the long-term debt rating of the provider of such agreement is downgraded below “AA-” or below “Aa” by the applicable Rating Agency, the CFD has the right to withdraw or cause the Fiscal Agent to withdraw all funds invested in such agreement and thereafter to invest such funds pursuant to the Fiscal Agent Agreement.

(8) Commercial paper rated, at the time of purchase, “Prime - 1” by Moody’s and “A-1” or better by Standard & Poor’s.

(9) Bonds or notes issued by any state or municipality which are rated by Moody’s and Standard & Poor’s in one of the two highest rating categories assigned by such agencies.

(10) Federal funds or bankers acceptances with a maximum term of one year of any bank which has an unsecured, uninsured or unguaranteed obligation rating of “Prime - 1” or “A3” or better by Moody’s and “A-1” or “A” or better by Standard & Poor’s.

(11) Repurchase agreements collateralized by Direct Obligations, GNMA’s, FNMA’s or FHLMC’s with any registered broker/dealer subject to the Securities Investors’ Protection Corporation jurisdiction or any commercial bank insured by the FDIC, if such broker/dealer or bank has an uninsured, unsecured and unguaranteed obligation rated “P-1” or “A3” or better by Moody’s, and “A-1” or “A-” by Standard & Poor’s; provided:

- (a) a master repurchase agreement or specific written repurchase agreement governs the transaction; and
- (b) the securities are held free and clear of any lien by the Fiscal Agent or an independent third party acting solely as agent (“Agent”) for the Fiscal Agent, and such third party is (i) a Federal Reserve Bank, (ii) a bank which is a member of the Federal Deposit Insurance Corporation and which has combined capital, surplus and undivided profits of not less than \$50 million, or (iii) a bank approved in writing for such purpose by Financial Guaranty Insurance Company, and the Fiscal Agent shall have received written confirmation from such third party that it holds such securities, free and clear of any lien, as agent for the Fiscal Agent; and
- (c) a perfected first security interest under the Uniform Commercial Code, or book-entry procedures prescribed at 31 C.F.R. 306.1 et seq. or 31 C.F.R. 350.0 et seq. in such securities is created for the benefit of the Fiscal Agent; and
- (d) the repurchase agreement has a term of 180 days or less, and the Fiscal Agent or the Agent will value the collateral securities no less frequently than weekly and will liquidate the collateral securities if any deficiency in the required collateral percentage is not restored within two business days of such valuation; and
- (e) the fair market value of the securities in relation to the amount of the repurchase obligation, including principal and interest, is equal to at least 103%.

(12) Local Agency Investment Fund (“LAIF”) of the State of California.

(13) Any other investment which the CFD is permitted by law to make.

“Authorized Representative of the CFD” means the Mayor, City Manager, Administrative Services Director, or any other person or persons designated by the Council and authorized to act on behalf of the CFD by a written certificate signed on behalf of the CFD by the Mayor or the City Manager and containing the specimen signature of each such person.

“Bond Counsel” means an attorney at law or a firm of attorneys selected by the CFD of nationally recognized standing in matters pertaining to the tax-exempt nature of interest on bonds issued by states and their political subdivisions duly admitted to the practice of law before the highest court of any state of the United States of America or the District of Columbia.

“Bond Register” means the books which the Fiscal Agent shall keep or cause to be kept on which the registration and transfer of the Bonds shall be recorded.

“Bondowner” or “Owner” means the person or persons in whose name or names any Bond is registered.

“Bond Year” means the twelve-month period commencing on September 2 of each year and ending on September 1 of the following year, except that the first Bond Year for the Bonds shall begin on the Delivery Date and end the first September 1 which is not more than 12 months after the Delivery Date.

“Business Day” means a day which is not a Saturday or Sunday or a day of the year on which banks in New York, New York, Los Angeles, California, or the city where the corporate trust office of the Fiscal Agent is located, are not required or authorized to remain closed.

“Certificate of Authorized Representative of the CFD” means a written certificate or warrant request executed by an Authorized Representative of the CFD.

“CFD” means the City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon) established pursuant to the Act and the Resolution of Formation.

“Code” means the Internal Revenue Code of 1986 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.

“Costs of Issuance” means the costs and expenses incurred in connection with the issuance and sale of the Bonds, including the acceptance and initial annual fees and expenses of the Fiscal Agent and its counsel, legal fees and expenses, costs of printing the Bonds and the preliminary and final official statements for the Bonds, fees of financial consultants and all other related fees and expenses, as set forth in a Certificate of Authorized Representative of the CFD.

“Council” means the City Council of the City of Lake Elsinore.

“Defeasance Securities” means any of the following:

- (a) Cash.
- (b) United States Treasury Certificates, Notes and Bonds (including State and Local Government Series - “SLGS”).
- (c) Direct obligations of the U.S. Treasury which have been stripped by the U.S. Treasury itself, e.g., CATS, TIGRS and similar securities.
- (d) The interest component of Resolution Funding Corp. strips which have been stripped by request to the Federal Reserve Bank of New York and are in book-entry form.
- (e) Pre-refunded municipal bonds rated “Aaa” by Moody’s and “AAA” by Standard & Poor’s.
- (f) Obligations issued by the following agencies which are backed by the full faith and credit of the United States:

U.S. Export-Import Bank - direct obligations or fully guaranteed certificates of beneficial ownership

Farmers Home Administration - certificates of beneficial ownership

Federal Financing Bank

General Services Administration - participation certificates

U.S. Maritime Administration - guaranteed Title XI financing

U.S. Department of Housing and Urban Development (HUD) - Project Notes, Local Authority Bonds, New Communities Debentures - U.S. government guaranteed debentures, U.S. Public Housing Notes and Bonds - U.S. government guaranteed public housing notes and bonds.

“Delivery Date” means, with respect to the Bonds, the date on which the bonds of such issue were issued and delivered to the initial purchasers thereof.

“Depository” shall mean The Depository Trust Company, New York, New York, and its successors and assigns as securities depository for the Certificates, or any other securities depository acting as Depository under the Fiscal Agent Agreement.

“Fiscal Agent” means Union Bank of California, N.A., a national banking association duly organized and existing under and by virtue of the laws of the United States of America, at its principal corporate trust office in Los Angeles, California, and its successors or assigns, or any other bank or trust company which may at any time be substituted in its place as provided in the Fiscal Agent Agreement and any successor thereto.

“Fiscal Agent Agreement” means the Fiscal Agent Agreement, together with any Supplemental Fiscal Agent Agreement approved pursuant to the Fiscal Agent Agreement.

“Fiscal Year” means the period beginning on July 1 of each year and ending on the next following June 30.

“Independent Financial Consultant” means a financial consultant or special tax consultant or firm of either such consultants generally recognized to be well qualified in the financial consulting or special tax consulting field, appointed and paid by the CFD, who, or each of whom:

- (1) is, in fact, independent and not under the domination of the CFD;
- (2) does not have any substantial interest, direct or indirect, in the CFD; and
- (3) is not connected with the CFD as a member, officer or employee of the CFD, but who may be regularly retained to make annual or other reports to the CFD.

“Interest Payment Date” means each March 1 and September 1, commencing March 1, 2007, provided, however, that, if any such day is not a Business Day, interest up to the Interest Payment Date will be paid on the Business Day next succeeding such date.

“Investment Agreement” means one or more agreements for the investment of funds of the CFD complying with the criteria therefor as set forth in Subsection (7) of the definition of Authorized Investments.

“Maximum Annual Debt Service” means the maximum sum obtained for any Bond Year prior to the final maturity of the Bonds by adding the following for each Bond Year:

- (1) the principal amount of all Outstanding Bonds payable in such Bond Year either at maturity or pursuant to a Sinking Fund Payment; and
- (2) the interest payable on the aggregate principal amount of all Bonds Outstanding in such Bond Year if the Bonds are retired as scheduled.

“Moody’s” means Moody’s Investors Service, its successors and assigns.

“Nominee” shall mean the nominee of the Depository, which may be the Depository, as determined from time to time pursuant to the Fiscal Agent Agreement.

“Outstanding” or “Outstanding Bonds” means all Bonds theretofore issued by the CFD, except:

- (1) Bonds theretofore cancelled or surrendered for cancellation in accordance with the Fiscal Agent Agreement;
- (2) Bonds for payment or redemption of which monies shall have been theretofore deposited in trust (whether upon or prior to the maturity or the redemption date of such Bonds), provided that, if such Bonds are to be redeemed prior to the maturity thereof, notice of such redemption shall have been given as provided in the Fiscal Agent Agreement; and
- (3) Bonds which have been surrendered to the Fiscal Agent for transfer or exchange pursuant to the Fiscal Agent Agreement or for which a replacement has been issued pursuant to the Fiscal Agent Agreement.

“Participants” shall mean those broker-dealers, banks and other financial institutions from time to time for which the Depository holds Bonds as securities depository.

“Person” means natural persons, firms, corporations, partnerships, associations, trusts, public bodies and other entities.

“Principal Office of the Fiscal Agent” means the office of the Fiscal Agent located in Los Angeles, California or such other office or offices as the Fiscal Agent may designate from time to time, or the office of any successor Fiscal Agent where it principally conducts its business of serving as Fiscal Agent under indentures pursuant to which municipal or governmental obligations are issued.

“Project” means those public facilities described in the Resolution of Formation which are to be acquired or constructed within Improvement Area No. 2, including all engineering, planning and design services and other incidental expenses related to such facilities and other facilities, if any, authorized by the qualified electors within the CFD from time to time.

“Project Costs” means the amounts necessary to finance the Project, to create and replenish any necessary reserve funds, to pay the initial and annual costs associated with the Bonds, including, but not limited to, remarketing, credit enhancement, Fiscal Agent and other fees and expenses relating to the issuance of the Bonds and the formation of the CFD, and to pay any other “incidental expenses” of the CFD, as such term is defined in the Act.

“Rating Agency” means Moody’s and Standard & Poor’s, or both, as the context requires.

“Record Date” means the fifteenth day of the month preceding an Interest Payment Date, regardless of whether such day is a Business Day.

“Regulations” means the regulations adopted or proposed by the Department of Treasury from time to time with respect to obligations issued pursuant to section 103 of the Code.

“Reserve Requirement” means, as of any date of calculation, an amount equal to the lowest of (1) 10% of the issue price (as defined pursuant to section 148 of the Code), or (2) Maximum Annual Debt Service, or (3) 125% of the average Annual Debt Service of the Outstanding Bonds.

“Resolution of Formation” means Resolution No. 2005-38 adopted by the Council on March 22, 2005 pursuant to which the Council formed the CFD.

“Sinking Fund Payment” means the annual payment to be deposited in the Redemption Account to redeem a portion of the Term Bonds in accordance with the schedule set forth in the Fiscal Agent Agreement.

“Special Taxes” means the taxes authorized to be levied by the CFD on parcels within Improvement Area No. 2 in accordance with the Resolution of Formation, the Act and the voter approval obtained at the July 27, 2006 election in the CFD and any additional special taxes authorized to be levied by the CFD from time to time which are pledged by the CFD to the repayment of the Bonds, together with the prepayment thereof and proceeds collected from the sale of property pursuant to the foreclosure provisions of the Fiscal Agent Agreement for the delinquency of such Special Taxes remaining after the payment of all the costs related to such foreclosure actions, including, but not limited to, all legal fees and expenses, court costs, consultant and title insurance fees and expenses.

“Standard & Poor’s” means Standard & Poor’s, a division of the McGraw-Hill Companies, Inc., its successors and assigns.

“Supplemental Fiscal Agent Agreement” means any supplemental fiscal agent agreement amending or supplementing the Fiscal Agent Agreement.

“Tax Certificate” means the certificate by that name to be executed by the CFD on a Delivery Date to establish certain facts and expectations and which contains certain covenants relevant to compliance with the Code.

“Term Bonds” means the Bonds maturing on September 1, 2026 and September 1, 2037.

“Underwriter” means the institution or institutions, if any, with whom the CFD enters into a purchase contract for the sale of the Bonds.

“Written Request of the CFD” means a request in writing executed by the Mayor, City Manager, City Treasurer, or written designee, on behalf of the CFD.

APPENDIX B

SUMMARY OF THE FISCAL AGENT AGREEMENT

The following is a summary of certain provisions of the Fiscal Agent Agreement and does not purport to be a complete restatement thereof. Reference is hereby made to the Fiscal Agent Agreement for the complete terms thereof. Copies of the Fiscal Agent Agreement are available from the City upon request.

Creation of Funds. There is created and established and shall be maintained by the Fiscal Agent the following funds and accounts:

- (1) The Community Facilities District 2004-3 Special Tax Fund (the “Special Tax Fund”) (in which there shall be established and created an Interest Account, a Principal Account, a Redemption Account, a Reserve Account and an Administrative Expense Account);
- (2) The Community Facilities District 2004-3 Surplus Fund (the “Surplus Fund”); and
- (3) The Community Facilities District 2004-3 Acquisition and Construction Fund (the “Acquisition and Construction Fund”) (in which there shall be established a Costs of Issuance Account).

The amounts on deposit in the foregoing funds, accounts and subaccounts shall be held by the Fiscal Agent in trust and the Fiscal Agent shall invest and disburse the amounts in such funds, accounts and subaccounts in accordance with the provisions of the Fiscal Agent Agreement and shall disburse investment earnings thereon in accordance with the provisions of the Fiscal Agent Agreement. Except as required to be segregated into funds and accounts as described in the Fiscal Agent Agreement, money held by the Fiscal Agent in trust under the Fiscal Agent Agreement need not be segregated from other funds except to the extent required by law.

Deposits to and Disbursements from Special Tax Fund. The CFD shall, on each date on which it receives Special Taxes, transfer the Special Taxes to the Fiscal Agent for deposit in the Special Tax Fund in accordance with the terms of the Fiscal Agent Agreement. The Fiscal Agent shall transfer the amounts on deposit in the Special Tax Fund on the dates and in the amounts set forth in the following Sections, in the following order of priority, to:

- (a) The Interest Account of the Special Tax Fund;
- (b) The Principal Account of the Special Tax Fund;
- (c) The Redemption Account of the Special Tax Fund;
- (d) The Reserve Account of the Special Tax Fund;
- (e) The Administrative Expense Account of the Special Tax Fund; and
- (f) The Surplus Fund.

At the maturity of all of the Bonds and, after all principal and interest then due on the Bonds then Outstanding has been paid or provided for and any amounts owed to the Fiscal Agent have been paid in full, moneys in the Special Tax Fund and any accounts therein shall be transferred to the CFD and may be used by the CFD for any lawful purpose.

Interest Account and Principal Account of the Special Tax Fund. The principal of and interest due on the Bonds until maturity, other than principal due upon redemption, shall be paid by the Fiscal Agent from the Principal Account and the Interest Account of the Special Tax Fund, respectively. For the purpose of assuring that the payment of principal of and interest on the Bonds will be made when due, at least five Business Days prior to each March 1 and September 1, the Fiscal Agent shall make the following transfers from the Special Tax Fund first to the Interest Account and then to the Principal Account; provided, however, that to the extent that deposits have been made in the Interest Account or the Principal Account from the

proceeds of the sale of an issue of the Bonds, or otherwise, the transfer from the Special Tax Fund need not be made; and provided, further, that, if amounts in the Special Tax Fund are inadequate to make the foregoing transfers, then any deficiency shall be made up by an immediate transfer from the Reserve Account:

(1) To the Interest Account, an amount such that the balance in the Interest Account five Business Days prior to each Interest Payment Date shall be equal to the installment of interest due on the Bonds on said Interest Payment Date and any installment of interest due on a previous Interest Payment Date which remains unpaid. Moneys in the Interest Account shall be used for the payment of interest on the Bonds as the same become due.

(2) To the Principal Account, an amount such that the balance in the Principal Account five Business Days prior to September 1 of each year, commencing September 1, 2007 shall at least equal the principal payment due on the Bonds maturing on such September 1 and any principal payment due on a previous September 1 which remains unpaid. Moneys in the Principal Account shall be used for the payment of the principal of such Bonds as the same become due at maturity.

Redemption Account of the Special Tax Fund.

(1) On each September 1 on which a Sinking Fund Payment is due, after the deposits have been made to the Interest Account and the Principal Account of the Special Tax Fund, the Fiscal Agent shall next transfer into the Redemption Account of the Special Tax Fund from the Special Tax Fund the amount needed to make the balance in the Redemption Account five Business Days prior to each September 1 equal to the Sinking Fund Payment due on any Outstanding Bonds on such September 1; provided, however, that, if amounts in the Special Tax Fund are inadequate to make the foregoing transfers, then any deficiency shall be made up by an immediate transfer from the Reserve Account, if funded. Moneys so deposited in the Redemption Account shall be used and applied by the Fiscal Agent to call and redeem Term Bonds in accordance with the Sinking Fund Payment schedule set forth in the Fiscal Agent Agreement.

(2) After making the deposits to the Interest Account and the Principal Account of the Special Tax Fund and to the Redemption Account for Sinking Fund Payments then due, and in accordance with the CFD's election to call Bonds for optional redemption, the Fiscal Agent shall transfer from the Special Tax Fund and deposit in the Redemption Account moneys available for the purpose and sufficient to pay the interest, the principal and the premiums, if any, payable on the Bonds called for optional redemption; provided, however, that amounts in the Special Tax Fund (exclusive of amounts transferred to the Administrative Expense Account) may be applied to optionally redeem Bonds only if immediately following such redemption the amount in the Reserve Account will equal the Reserve Requirement.

(3) All prepayments of Special Tax shall be deposited in the Redemption Account to be used to redeem Bonds on the next date for which notice of redemption can timely be given.

(4) Moneys set aside in the Redemption Account shall be used solely for the purpose of redeeming Bonds and shall be applied on or after the redemption date to the payment of the principal of and premium, if any, on the Bonds to be redeemed upon presentation and surrender of such Bonds and in the case of an optional redemption to pay the interest thereon; provided, however, that in lieu or partially in lieu of such call and redemption, moneys deposited in the Redemption Account as set forth above may be used to purchase Outstanding Bonds. Purchases of Outstanding Bonds may be made by the CFD at public or private sale as and when and at such prices as the CFD may in its discretion determine but only at prices (including brokerage or other expenses) not more than par plus accrued interest, plus, in the case of moneys set aside for an optional redemption, the premium applicable at the next following call date according to the premium schedule established pursuant to the Fiscal Agent Agreement. Any accrued interest payable upon the purchase of Bonds may be paid from the amount reserved in the Interest Account of the Special Tax Fund for the payment of interest on the next following Interest Payment Date.

Reserve Account of the Special Tax Fund. There shall be maintained in the Reserve Account of the Special Tax Fund an amount equal to the Reserve Requirement. The amounts in the Reserve Account shall be applied as follows:

(1) Moneys in the Reserve Account shall be used solely for the purpose of paying the principal of, including Sinking Fund Payments, and interest on any Bonds when due in the event that the moneys in the Interest Account and the Principal Account of the Special Tax Fund are insufficient therefor or moneys in the Redemption Account of the Special Tax Fund are insufficient to make a Sinking Fund Payment when due. If the amounts in the Interest Account, the Principal Account or the Redemption Account of the Special Tax Fund are insufficient to pay the principal of, including Sinking Fund Payments, or interest on any Bonds when due, the Fiscal Agent shall withdraw from the Reserve Account for deposit in the Interest Account, the Principal Account or the Redemption Account of the Special Tax Fund, as applicable, moneys necessary for such purposes.

(2) Whenever moneys are withdrawn from the Reserve Account, after making the required transfers referred to in the Fiscal Agent Agreement, the Fiscal Agent shall transfer to the Reserve Account from available moneys in the Special Tax Fund, or from any other legally available funds which the CFD elects to apply to such purpose, the amount needed to restore the amount of such Reserve Account to the Reserve Requirement. Moneys in the Special Tax Fund shall be deemed available for transfer to the Reserve Account only if the Fiscal Agent determines that such amounts will not be needed to make the deposits required to be made to the Interest Account, the Principal Account or the Redemption Account of the Special Tax Fund. If amounts in the Special Tax Fund or otherwise transferred to replenish the Reserve Account are inadequate to restore the Reserve Account to the Reserve Requirement, then the CFD shall include the amount necessary fully to restore the Reserve Account to the Reserve Requirement in the next annual Special Tax levy to the extent of the maximum permitted Special Tax rates.

(3) In connection with any redemption of the Bonds, or a partial defeasance of the Bonds, amounts in the Reserve Account may be applied to such redemption or partial defeasance so long as the amount on deposit in the Reserve Account following such redemption or partial defeasance equals the Reserve Requirement. To the extent that the Reserve Account is at the Reserve Requirement as of the first day of the final Bond Year for the Bonds, amounts in the Reserve Account may be applied to pay the principal of and interest due on the Bonds in the final Bond Year for such issue. Moneys in the Reserve Account in excess of the Reserve Requirement not transferred in accordance with the preceding provisions of this paragraph shall be withdrawn from the Reserve Account on the fifth Business Day before each March 1 and September 1 and transferred to the Acquisition and Construction Fund until the Fiscal Agent receives a Certificate of Authorized Representative of the CFD that all Project Costs have been funded, and thereafter to the Interest Account of the Special Tax Fund.

Administrative Expense Account of the Special Tax Fund. The Fiscal Agent shall transfer from the Special Tax Fund and deposit in the Administrative Expense Account of the Special Tax Fund amounts necessary to make timely payment of Administrative Expenses and shall be disbursed by the Fiscal Agent to pay Administrative Expenses, all as instructed by the CFD pursuant to a Written Request of the CFD. Moneys in the Administrative Expense Account of the Special Tax Fund may be invested in any Authorized Investments as directed by an Authorized Representative of the CFD.

Surplus Fund. After making the transfers required by the Fiscal Agent Agreement, as soon as practicable after each September 1, the Fiscal Agent shall transfer all remaining amounts in the Special Tax Fund to the Surplus Fund, other than amounts in the Special Tax Fund which the CFD directs the Fiscal Agent by Written Request of the CFD to retain because the CFD has included such funds as being available in the Special Tax Fund in calculating the amount of the levy of Special Taxes for such Fiscal Year pursuant to the Fiscal Agent Agreement. Moneys deposited in the Surplus Fund shall be transferred by the Fiscal Agent at the written request of the CFD (i) to the Administrative Expense Account of the Special Tax Fund to pay Administrative Expenses to the extent that the amounts on deposit in the Administrative Expense Account of the Special Tax Fund are insufficient to pay Administrative Expenses or, (ii) to the Redemption Account for the purpose of redeeming Bonds.

The amounts in the Surplus Fund are not pledged to the repayment of the Bonds. In the event that the CFD reasonably expects to use any portion of the moneys in the Surplus Fund to pay debt service on any Outstanding Bonds, upon the written direction of the CFD, the Fiscal Agent will segregate such amount into a separate subaccount and the moneys on deposit in such subaccount of the Surplus Fund shall be invested in Authorized Investments the interest on which is excludable from gross income under Section 103 of the

Code (other than bonds the interest on which is a tax preference item for purposes of computing the alternative minimum tax of individuals and corporations under the Code) or in Authorized Investments at a yield not in excess of the yield on the issue of Bonds to which such amounts are to be applied, unless, in the opinion of Bond Counsel, investment at a higher yield will not adversely affect the exclusion from gross income for federal income tax purposes of interest on the Bonds which were issued on a tax-exempt basis for federal income tax purposes.

Acquisition and Construction Fund. The moneys in the Acquisition and Construction Fund shall be applied exclusively to pay the Project Costs and Costs of Issuance. Amounts for Project Costs and Costs of Issuance shall be disbursed by the Fiscal Agent from the account in the Acquisition and Construction Fund designated therefor in a requisition signed by an Authorized Representative of the CFD, substantially in the form of Exhibit B to the Fiscal Agent Agreement, which must be submitted in connection with each requested disbursement.

Upon receipt of a Certificate of Authorized Representative of the CFD that all or a specified portion of the amount remaining in the Acquisition and Construction Fund is no longer needed to pay Project Costs or Costs of Issuance, the Fiscal Agent shall redeem Bonds pursuant to the Fiscal Agent Agreement, or transfer all or such specified portion of the moneys remaining on deposit in one or more of the accounts in the Acquisition and Construction Fund to the Special Tax Fund, or to the Surplus Fund if requested in the Certificate and if there shall have been delivered to the Fiscal Agent with such Certificate an opinion of Bond Counsel to the effect that such transfer to the Surplus Fund will not adversely affect the exclusion from gross income for federal income tax purposes of interest on the Bonds which were issued on a tax-exempt basis for federal income tax purposes. Upon transfer of the final amounts on deposit in the Acquisition and Construction Fund or either account in such fund, such accounts and fund shall be closed. Notwithstanding the foregoing, any amount remaining in the Costs of Issuance Account of the Acquisition and Construction Fund on the date 180 days from the Delivery Date shall be transferred to the Acquisition and Construction Fund and such account shall be closed.

Investments. Moneys held in any of the funds and accounts under the Fiscal Agent Agreement shall be invested at the Written Request of the CFD in accordance with the limitations set forth below only in Authorized Investments which shall be deemed at all times to be a part of such funds and accounts. Any loss resulting from such Authorized Investments shall be credited or charged to the fund or account from which such investment was made, and any investment earnings on a fund or account shall be applied as follows: (i) investment earnings on all amounts deposited in the Special Tax Fund (exclusive of amounts transferred to the Reserve Account), Surplus Fund, Acquisition and Construction Fund and each Account therein shall be deposited in those respective funds and accounts, and (ii) all other investment earnings shall be deposited in the Interest Account of the Special Tax Fund; provided, however, to the extent moneys in the Reserve Account exceed the Reserve Requirement, such excess amounts shall be deposited and transferred pursuant to the Fiscal Agent Agreement. Moneys in the funds and accounts held under the Fiscal Agent Agreement may be invested by the Fiscal Agent at the Written Request of the CFD received at least 2 Business Days prior to the investment date, from time to time, in Authorized Investments subject to the following restrictions:

(1) Moneys in the Interest Account, the Principal Account and the Redemption Account of the Special Tax Fund shall be invested only in Authorized Investments which will by their terms mature, or in the case of an Investment Agreement are available for withdrawal without penalty, on such dates so as to ensure the payment of principal of, premium, if any, and interest on the Bonds as the same become due.

(2) Moneys in the Acquisition and Construction Fund shall be invested in Authorized Investments which will by their terms mature, or in the case of an Investment Agreement are available without penalty, as close as practicable to the date the CFD estimates the moneys represented by the particular investment will be needed for withdrawal from the Acquisition and Construction Fund. Notwithstanding anything in the Fiscal Agent Agreement to the contrary, amounts in the Acquisition and Construction Fund on the Delivery Date for the Bonds shall not be invested at yields greater than those set forth in the Tax Certificate.

(3) One-half of the amount in the Reserve Account of the Special Tax Fund may be invested only in Authorized Investments which mature not later than two years from their date of purchase by the Fiscal Agent, and one-half of the amount in the Reserve Account may be invested only in Authorized Investments

which mature not more than three years from the date of purchase by the Fiscal Agent; provided that such amounts may be invested in an Investment Agreement to the final maturity of the Bonds so long as such amounts may be withdrawn at any time, without penalty, for application in accordance with the Fiscal Agent Agreement; and provided that no such Authorized Investment of amounts in the Reserve Account allocable to the Bonds shall mature later than the final maturity date of the Bonds.

(4) In the absence of Written Request of the CFD providing investment directions, the Fiscal Agent shall invest solely in Authorized Investments specified in clause (4) of the definition thereof.

The Fiscal Agent shall sell at the best price obtainable, or present for redemption, any Authorized Investment whenever it may be necessary to do so in order to provide moneys to meet any payment or transfer to such Funds and Accounts or from such Funds and Accounts. For the purpose of determining at any given time the balance in any such Funds and Accounts, any such investments constituting a part of such Funds and Accounts shall be valued at their cost, except that amounts in the Reserve Account shall be valued at the fair market value thereof and marked to market at least annually. Notwithstanding anything in the Fiscal Agent Agreement to the contrary, the Fiscal Agent shall not be responsible for any loss from investments, sales or transfers undertaken in accordance with the provisions of the Fiscal Agent Agreement. The Fiscal Agent or an affiliate may act as principal or agent in connection with the acquisition or disposition of any Authorized Investments and shall be entitled to its customary fees therefor. Any Authorized Investments that are registrable securities shall be registered in the name of the Fiscal Agent. The Fiscal Agent is authorized, in making or disposing of any investment permitted by this Section, to deal with itself (in its individual capacity) or with any one or more of its affiliates, whether it or such affiliate is acting as an agent of the Fiscal Agent or for any third person or dealing as principal for its own account.

Covenants. So long as any of the Bonds issued hereunder are Outstanding and unpaid, the CFD makes the following covenants with the Bondowners under the provisions of the Act and the Fiscal Agent Agreement (to be performed by the CFD or its proper officers, agents or employees), which covenants are necessary and desirable to secure the Bonds and tend to make them more marketable; provided, however, that said covenants do not require the CFD to expend any funds or moneys other than the Special Taxes and other amounts deposited to the Special Tax Fund:

(1) Punctual Payment; Against Encumbrances. The CFD covenants that it will receive all Special Taxes in trust and will immediately deposit such amounts with the Fiscal Agent, and the CFD shall have no beneficial right or interest in the amounts so deposited except as provided by the Fiscal Agent Agreement. All such Special Taxes shall be disbursed, allocated and applied solely to the uses and purposes set forth in the Fiscal Agent Agreement, and shall be accounted for separately and apart from all other money, funds, accounts or other resources of the CFD.

The CFD covenants that it will duly and punctually pay or cause to be paid the principal of and interest on every Bond issued hereunder, together with the premium, if any, thereon on the date, at the place and in the manner set forth in the Bonds and in accordance with the Fiscal Agent Agreement to the extent that Special Taxes are available therefor, and that the payments into the Funds and Accounts created hereunder will be made, all in strict conformity with the terms of the Bonds and the Fiscal Agent Agreement, and that it will faithfully observe and perform all of the conditions, covenants and requirements of the Fiscal Agent Agreement and all Supplemental Fiscal Agent Agreements and of the Bonds issued under the Fiscal Agent Agreement.

The CFD will not mortgage or otherwise encumber, pledge or place any charge upon any of the Special Taxes except as provided in the Fiscal Agent Agreement, and will not issue any obligation or security having a lien or charge upon the Special Taxes superior to or on a parity with the Bonds. Nothing in the Fiscal Agent Agreement shall prevent the CFD from issuing or incurring indebtedness which is payable from a pledge of Special Taxes which is subordinate in all respects to the pledge of Special Taxes to repay the Bonds.

(2) Levy of Special Tax. Beginning in Fiscal Year 2006-07 and so long as any Bonds issued under the Fiscal Agent Agreement are Outstanding, the CFD covenants to levy the Special Tax in an amount sufficient, together with other amounts on deposit in the Special Tax Fund and the Surplus Fund and available for such

purpose, to pay (1) the principal of and interest on the Bonds when due, (2) the Administrative Expenses, and (3) any amounts required to replenish the Reserve Account of the Special Tax Fund to the Reserve Requirement.

(3) Commence Foreclosure Proceedings. The CFD covenants for the benefit of the Owners of the Bonds that it will determine or cause to be determined, no later than March 1 and August 1 of each year, whether or not any owner of the property within Improvement Area No. 2 is delinquent in the payment of Special Taxes and, if such delinquencies exist, the CFD will order and cause to be commenced no later than April 15 (with respect to the March 1 determination date) or September 1 (with respect to the August 1 determination date), and thereafter diligently prosecute, an action in the superior court to foreclose the lien of any Special Taxes or installment thereof not paid when due, provided, however, that the CFD shall not be required to order the commencement of foreclosure proceedings if (i) the total Special Tax delinquency in Improvement Area No. 2 for such Fiscal Year is less than five percent (5%) of the total Special Tax levied in such Fiscal Year, and (ii) the CFD shall have established from any source of lawfully available funds (other than Special Taxes) an escrow fund to provide for the payment of principal of and interest on the Bonds. Notwithstanding the foregoing, if the CFD determines that any single property owner in Improvement Area No. 2 is delinquent in excess of ten thousand dollars (\$10,000) in the payment of the Special Tax, then it will diligently institute, prosecute and pursue foreclosure proceedings against such property owner.

Notwithstanding any provision of the Act or other law of the State to the contrary, in connection with any foreclosure related to delinquent Special Taxes:

(a) The CFD or the Fiscal Agent is authorized to credit bid at any foreclosure sale, without any requirement that funds be set aside in the amount so credit bid, in the amount specified in Section 53356.5 of the Act, or such less amount as determined under clause (b) below or otherwise under Section 53356.6 of the Act.

(b) The CFD may permit, in its sole and absolute discretion, property with delinquent Special Tax payments to be sold for less than the amount specified in Section 53356.5 of the Act, if it determines that such sale is in the interest of the Bond Owners. The Bond Owners, by their acceptance of the Bonds, consent to such sale for such lesser amounts (as such consent is described in Section 53356.6 of the Act), and release the CFD and the City, and their respective officers and agents from any liability in connection therewith. If such sale for lesser amounts would result in less than full payment of principal of and interest on the Bonds, the CFD will use best efforts to seek approval of the Bond Owners.

(c) The CFD is authorized to use amounts in the Special Tax Fund to pay costs of foreclosure of delinquent Special Taxes.

(d) The CFD may forgive all or any portion of the Special Taxes levied or to be levied on any parcel in Improvement Area No. 2 so long as the CFD determines that such forgiveness is not expected to adversely affect its obligation to pay principal of and interest on the Bonds as such payments become due and payable.

(4) Payment of Claims. The CFD will pay and discharge any and all lawful claims for labor, materials or supplies which, if unpaid, might become a lien or charge upon the Special Taxes, or other funds in the Special Tax Fund (exclusive of amounts transferred to the Administrative Expense Account), or which might impair the security of the Bonds then Outstanding; provided that nothing contained in the Fiscal Agent Agreement shall require the CFD to make any such payments so long as the CFD in good faith shall contest the validity of any such claims.

(5) Books and Accounts. The CFD will keep proper books of records and accounts, separate from all other records and accounts of the CFD, in which complete and correct entries shall be made of all transactions relating to the levy of the Special Tax and the deposits to the Special Tax Fund. Such books of records and accounts shall at all times during business hours be subject to the inspection of the Fiscal Agent or of the Owners of the Bonds then Outstanding or their representatives authorized in writing.

(6) Tax Covenants. The CFD covenants that it shall not use, and shall not permit the use of, and shall not omit to use Gross Proceeds or any other amounts (or any property the acquisition, construction or

improvement of which is to be financed directly or indirectly with Gross Proceeds) in a manner that if made or omitted, respectively, could cause the interest on any Bond to fail to be excluded pursuant to section 103(a) of the Code from the gross income of the owner thereof for federal income tax purposes.

(7) Reduction of Maximum Special Taxes. The CFD finds and determines that, historically, delinquencies in the payment of special taxes authorized pursuant to the Act in community facilities districts in Southern California have from time to time been at levels requiring the levy of special taxes at the maximum authorized rates in order to make timely payment of principal of and interest on the outstanding indebtedness of such community facilities districts. For this reason, the CFD determines that a reduction in the maximum Special Tax rates authorized to be levied on parcels in the CFD below the levels provided in the Fiscal Agent Agreement would interfere with the timely retirement of the Bonds. The CFD determines it to be necessary in order to preserve the security for the Bonds to covenant, and, to the maximum extent that the law permits it to do so, the CFD does covenant, that it shall not initiate proceedings to reduce the maximum Special Tax rates for the CFD, unless, in connection therewith, (i) the CFD receives a certificate from one or more Independent Financial Consultants which, when taken together, certify that, on the basis of the parcels of land and improvements existing in Improvement Area No. 2 as of the July 1 preceding the reduction, the maximum amount of the Special Tax which may be levied on then existing Developed Property (as defined in the Rate and Method of Apportionment of Special Taxes then in effect in Improvement Area No. 2) in each Bond Year for any Bonds Outstanding will equal at least 110% of the sum on the estimated Administrative Expenses and gross debt service in that Bond Year on all Bonds to remain Outstanding after the reduction is approved, and (ii) the CFD finds that any reduction made under such conditions will not adversely affect the interests of the Owners of the Bonds. For purposes of estimating Administrative Expenses for the foregoing calculation, the Independent Financial Consultant shall compute the Administrative Expenses for the current Fiscal Year and escalate that amount by two percent (2%) in each subsequent Fiscal Year.

(8) Covenants to Defend. The CFD covenants that in the event that any initiative is adopted by the qualified electors in the CFD which purports to reduce the maximum Special Tax below the levels specified in the Fiscal Agent Agreement or to limit the power of the CFD to levy the Special Taxes for the purposes set forth in the Fiscal Agent Agreement, it will commence and pursue legal action in order to preserve its ability to comply with such covenants.

(9) Annual Reports to CDIAC. Not later than October 30 of each year, commencing October 30, 2006 and until the October 30 following the final maturity of the Bonds, the CFD shall cause the City to supply the information required by Section 53359.5(b) or (c) of the Act to CDIAC (on such forms as CDIAC may specify).

(10) Continuing Disclosure. The CFD covenants to comply with the terms of the Continuing Disclosure Agreement executed by it with respect to the Bonds.

Supplemental Fiscal Agent Agreements or Orders Not Requiring Bondowner Consent. The CFD may from time to time, and at any time, without notice to or consent of any of the Bondowners, adopt Supplemental Fiscal Agent Agreements for any of the following purposes:

(1) to cure any ambiguity, to correct or supplement any provisions in the Fiscal Agent Agreement which may be inconsistent with any other provision in the Fiscal Agent Agreement, or to make any other provision with respect to matters or questions arising under the Fiscal Agent Agreement or in any additional resolution or order, provided that such action is not materially adverse to the interests of the Bondowners;

(2) to add to the covenants and agreements of and the limitations and the restrictions upon the CFD contained in the Fiscal Agent Agreement, other covenants, agreements, limitations and restrictions to be observed by the CFD which are not contrary to or inconsistent with the Fiscal Agent Agreement as theretofore in effect or which further secure Bond payments;

(3) to modify, amend or supplement the Fiscal Agent Agreement in such manner as to permit the qualification hereof under the Trust Indenture Act of 1939, as amended, or any similar federal statute hereafter in effect, or to comply with the Code or regulations issued thereunder, and to add such other terms,

conditions and provisions as may be permitted by said act or similar federal statute, and which shall not materially adversely affect the interests of the Owners of the Bonds then Outstanding;

(4) to modify, alter or amend the rate and method of apportionment of the Special Taxes in any manner so long as such changes do not reduce the maximum Special Taxes that may be levied in each year on property within the CFD to an amount which is less than that permitted under the Fiscal Agent Agreement; or

(5) to modify, alter, amend or supplement the Fiscal Agent Agreement in any other respect which is not materially adverse to the Bondowners.

Events of Default. Any one or more of the following events shall constitute an “event of default:”

(a) Default in the due and punctual payment of the principal of or redemption premium, if any, on any Bond when and as the same shall become due and payable, whether at maturity as therein expressed, by declaration or otherwise;

(b) Default in the due and punctual payment of the interest on any Bond when and as the same shall become due and payable; or

(c) Except as described in (a) or (b), default shall be made by the CFD in the observance of any of the agreements, conditions or covenants on its part contained in the Fiscal Agent Agreement or the Bonds, and such default shall have continued for a period of 30 days after the CFD shall have been given notice in writing of such default by the Fiscal Agent or the Owners of 25% in aggregate principal amount of the Outstanding Bonds.

The CFD agrees to give notice to the Fiscal Agent immediately upon the occurrence of an event of default under (a) or (b) above and within 30 days of the CFD’s knowledge of an event of default under (c) above. The Fiscal Agent shall not be deemed to have knowledge of any event of default unless a responsible officer shall have actual knowledge thereof or the Fiscal Agent shall have received written notice at its Principal Office.

Remedies of Owners. Following the occurrence of an event of default, any Owner shall have the right for the equal benefit and protection of all Owners similarly situated:

(1) By mandamus or other suit or proceeding at law or in equity to enforce his rights against the CFD and any of the members, officers and employees of the CFD, and to compel the CFD or any such members, officers or employees to perform and carry out their duties under the Act and their agreements with the Owners as provided in the Fiscal Agent Agreement;

(2) By suit in equity to enjoin any actions or things which are unlawful or violate the rights of the Owners; or

(3) By a suit in equity to require the CFD and its members, officers and employees to account as the fiscal agent of an express trust.

Nothing in the Fiscal Agent Agreement or the Bonds shall affect or impair the obligation of the CFD, which is absolute and unconditional, to pay the interest on and principal of the Bonds to the respective Owners thereof at the respective dates of maturity, as provided in the Fiscal Agent Agreement, out of the Special Taxes and other amounts pledged for such payment, or affect or impair the right of action, which is also absolute and unconditional, of such Owners to institute suit to enforce such payment by virtue of the contract embodied in the Bonds and in the Fiscal Agent Agreement.

A waiver of any default or breach of duty or contract by any Owner shall not affect any subsequent default or breach of duty or contract, or impair any rights or remedies on any such subsequent default or breach. No delay or omission by any Owner to exercise any right or power accruing upon any default shall impair any such right or power or shall be construed to be a waiver of any such default or an acquiescence therein, and every power and remedy conferred upon the Owners by the Act or by this article may be enforced and exercised from time to time and as often as shall be deemed expedient by the Owners.

If any suit, action or proceeding to enforce any right or exercise any remedy is abandoned or determined adversely to the Owners, the CFD and the Owners shall be restored to their former positions, rights and remedies as if such suit, action or proceeding had not been brought or taken.

No remedy in the Fiscal Agent Agreement conferred upon or reserved to the Owners is intended to be exclusive of any other remedy. Every such remedy shall be cumulative and shall be in addition to every other remedy given hereunder or now or hereafter existing, at law or in equity or by statute or otherwise, and may be exercised without exhausting and without regard to any other remedy conferred by the Act or any other law.

In case the moneys held by the Fiscal Agent after an event of default shall be insufficient to pay in full the whole amount so owing and unpaid upon the Outstanding Bonds, then all available amounts shall be applied to the payment of such principal and interest without preference or priority of principal over interest, or interest over principal, or of any installment of interest over any other installment of interest, ratably to the aggregate of such principal and interest.

Defeasance. If the CFD shall pay or cause to be paid, or there shall otherwise be paid, to the Owner of an Outstanding Bond the interest due thereon and the principal thereof, at the times and in the manner stipulated in the Fiscal Agent Agreement or any Supplemental Fiscal Agent Agreement, then the Owner of such Bond shall cease to be entitled to the pledge of Special Taxes, and, other than as set forth below, all covenants, agreements and other obligations of the CFD to the Owner of such Bond under the Fiscal Agent Agreement shall thereupon cease, terminate and become void and be discharged and satisfied. In the event of a defeasance of all Outstanding Bonds, the Fiscal Agent shall execute and deliver to the CFD all such instruments as may be desirable to evidence such discharge and satisfaction, and the Fiscal Agent shall pay over or deliver to the CFD's general fund all money or securities held by it pursuant to the Fiscal Agent Agreement which are not required for the payment of the principal of, premium, if any, and interest due on such Bonds.

Any Outstanding Bond shall be deemed to have been paid if such Bond is paid in any one or more of the following ways:

(a) by paying or causing to be paid the principal of, premium, if any, and interest on such Bond, as and when the same become due and payable;

(b) by depositing with the Fiscal Agent, in trust, at or before maturity, money which, together with the amounts then on deposit in the Special Tax Fund (exclusive of amounts transferred to the Administrative Expense Account) and available for such purpose, is fully sufficient to pay the principal of, premium, if any, and interest on such Bond, as and when the same shall become due and payable; or

(c) by depositing with the Fiscal Agent or another escrow bank appointed by the CFD, in trust, noncallable Defeasance Securities, in which the CFD may lawfully invest its money, in such amount as will be sufficient, together with the interest to accrue thereon and moneys then on deposit in the Special Tax Fund (exclusive of amounts transferred to the Administrative Expense Account) and available for such purpose, together with the interest to accrue thereon, to pay and discharge the principal of, premium, if any, and interest on such Bond, as and when the same shall become due and payable;

then, at the election of the CFD, and notwithstanding that any Outstanding Bonds shall not have been surrendered for payment, all obligations of the CFD under the Fiscal Agent Agreement and any Supplemental Fiscal Agent Agreement with respect to such Bond shall cease and terminate, except for the obligation of the Fiscal Agent to pay or cause to be paid to the Owners of any such Bond not so surrendered and paid, all sums due thereon and except for the covenants of the CFD contained in the Fiscal Agent Agreement or any covenants in a Supplemental Fiscal Agent Agreement relating to compliance with the Code. Notice of such election shall be filed with the Fiscal Agent not less than ten days prior to the proposed defeasance date, or such shorter period of time as may be acceptable to the Fiscal Agent. In connection with a defeasance under (b) or (c) above, there shall be provided to the CFD a verification report from an independent, nationally recognized, certified public accountant stating its opinion as to the sufficiency of the moneys or securities deposited with the Fiscal Agent or the escrow bank to pay and discharge the principal of, premium, if any, and interest on all Outstanding Bonds to be defeased, as and when the same shall become due and payable,

and an opinion of Bond Counsel (which may rely upon the opinion of the certified public accountant) to the effect that the Bonds being defeased have been legally defeased in accordance with the Fiscal Agent Agreement and any applicable Supplemental Fiscal Agent Agreement. If a forward supply contract is employed in connection with an advance refunding to be effected under (c) above, (i) such verification report shall expressly state that the adequacy of the amounts deposited with the bank under (c) above to accomplish the refunding relies solely on the initial escrowed investments and the maturity principal thereof and interest income thereon and does not assume performance under or compliance with the forward supply contract, and (ii) the applicable escrow agreement executed to effect an advance refunding in accordance with (c) above shall provide that, in the event of any discrepancy or difference between the terms of the forward supply contract and the escrow agreement, the terms of the escrow agreement shall be controlling.

Upon a defeasance, the Fiscal Agent, upon request of the CFD, shall release the rights of the Owners of such Bonds which have been defeased under the Fiscal Agent Agreement and any Supplemental Fiscal Agent Agreement and execute and deliver to the CFD all such instruments as may be desirable to evidence such release, discharge and satisfaction. In the case of a defeasance hereunder of all Outstanding Bonds, the Fiscal Agent shall pay over or deliver to the CFD any funds held by the Fiscal Agent at the time of a defeasance, which are not required for the purpose of paying and discharging the principal of, premium, if any, or interest on the Bonds when due. The Fiscal Agent shall, at the written direction of the CFD, mail, first class, postage prepaid, a notice to the Bondowners whose Bonds have been defeased, in the form directed by the CFD, stating that the defeasance has occurred.

APPENDIX C
MARKET ABSORPTION STUDY

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**MARKET ABSORPTION STUDY
SUMMARY AND CONCLUSIONS**

**CFD NO. 2004-3 IMPROVEMENT AREA NO. 2
(ROSETTA CANYON)**

**CITY OF LAKE ELSINORE
RIVERSIDE COUNTY, CALIFORNIA**



DEVELOPMENT ACTIVITY IN A PORTION OF THE CFD

BY EMPIRE ECONOMICS, INC.

UPDATED: AUGUST 10, 2006

ORIGINAL STUDY: MAY 25, 2006

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CERTIFICATION OF INDEPENDENCE

The Securities & Exchange Commission has recently taken action against Wall Street firms that have utilized their research analysts to promote companies with whom they conduct business, citing this as a potential conflict of interest. Accordingly, Empire Economics (Empire), in order to ensure that its clients are not placed in a situation that could cause such conflicts of interest, provides a Certification of Independence. Specifically, the Certificate states that Empire performs consulting services for **public entities only** in order to avoid potential conflicts of interest that could occur if it also provided consulting services for developer/builder. For example, if a research firm for a specific Community Facilities District or Assessment District were to provide consulting services to both the public entity as well as the property owner/developer/builder, then a potential conflict of interest could be created, given the different objectives of the public entity versus the property owner/developer.

Accordingly, Empire Economics certifies that the Market Absorption Study for the CFD No. 2004-3 IA No. 2 (Rosetta Canyon) of the City of Lake Elsinore was performed in an independent professional manner, as represented by the following statements:

- Empire was retained to perform the Market Absorption Study by the City of Lake Elsinore, not the District's property owner/developer, Centex Homes.
- Empire has not performed any consulting services for the District's property owner or the developer/builder during at least the past five years.
- Empire will not perform any consulting services for the District's property owner or the developer/builder during at least the next three years.
- Empire's compensation for performing the Market Absorption Study for the District is not contingent upon the issuance of Bonds; Empire's fees are paid on a non-contingency basis.

Therefore, based upon the statements set-forth above, Empire hereby certifies that the Market Absorption Study for CFD No. 2004-3 IA No. 2 (Rosetta Canyon) of the City of Lake Elsinore was performed in an independent professional manner.

Empire Economics, Inc.
Joseph T. Janczyk, President

INTRODUCTION TO THE BOND FINANCING PROGRAM

The City of Lake Elsinore was previously petitioned by Centex Homes to form a Community Facilities District to assist with the financing of the infrastructure that is required to support the development of their residential projects in the Planned Community of Rosetta Canyon; this Bond Issue is for the properties/projects in CFD No. 2004-3 Improvement Area (IA) No. 2.

The CFD No. 2004-3 IA No. 2 Bond Issue proceeds will be utilized to provide funds for various infrastructure components, including road, water and sewer improvements, among others. The Bond Issue that is being considered at this time amounts to some \$19 million; however, the specific size of the Bond Issue and the particular improvements included will depend upon various factors which will be finalized when these bonds are sold.

According to Centex Homes, CFD No. 2004-3 IA No. 2 (Rosetta Canyon) is expected to have a total of 503 single-family detached homes in four projects with homes that are priced from some \$359,990 to \$553,990 for some 1,979 to 4,063 sq.ft. of living area; these projects are expected to commence escrow closings to homeowners during the 4th-quarter of 2006 through 1st-quarter 2007.

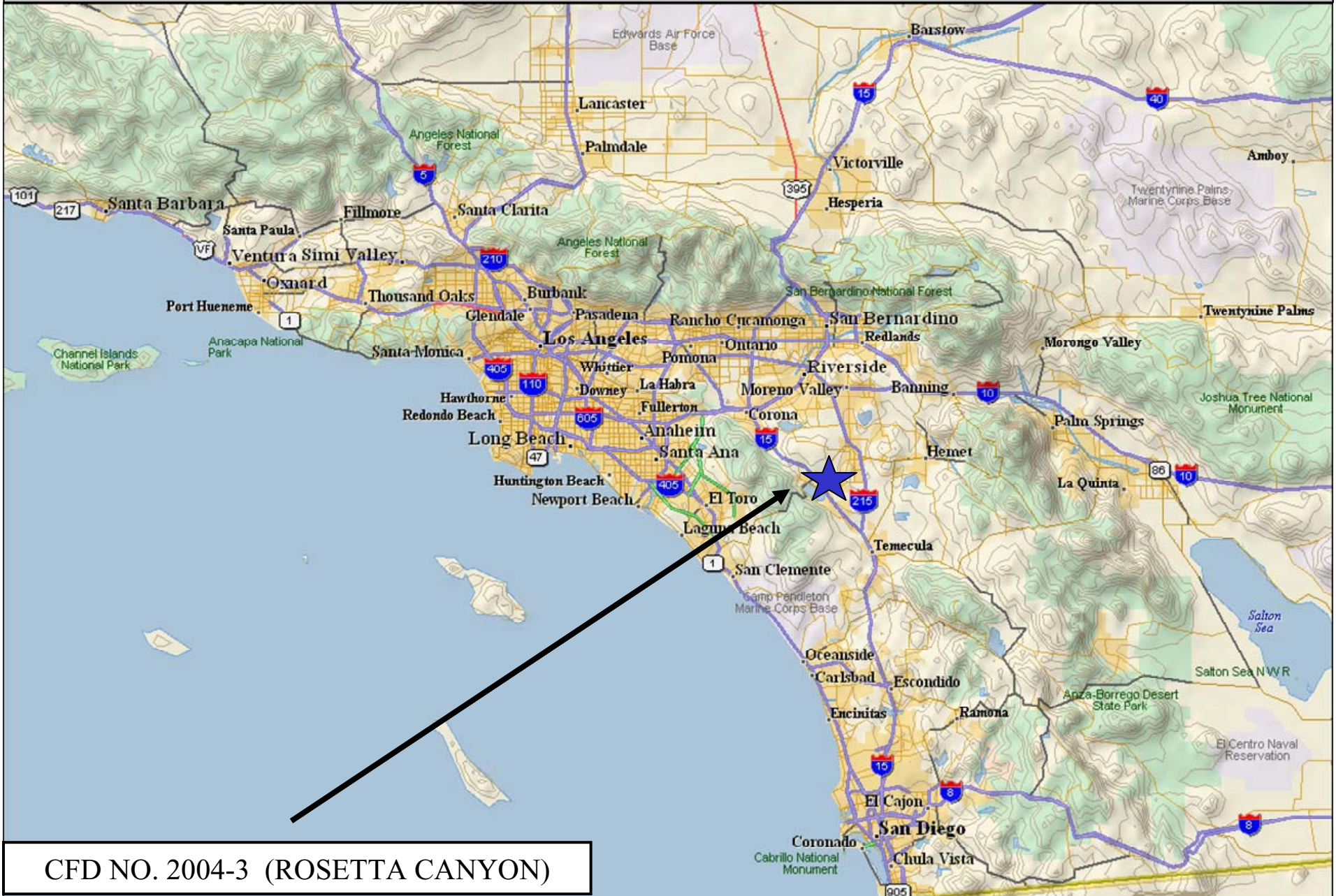
The City of Lake Elsinore has retained Empire Economics, an economic and real estate consulting firm, to perform a Market Absorption Study for the residential projects in CFD No. 2004-3 IA No. 2 (Rosetta Canyon). The purpose of the Market Study for CFD No. 2004-3 IA No. 2 is to provide an estimate of the probable absorption schedule for the residential projects. Specifically, from the viewpoint of prospective Bond Purchasers, the particular components of the infrastructure should be time-phased and location-phased in a manner that approximately coincides with the expected marketability/absorption of the projects/products in the CFD No. 2004-3 IA No. 2. Otherwise, to the extent that the infrastructure is not appropriately phased, then the following types of market inefficiencies may occur:

On the one hand, if certain projects do not have the infrastructure that is required to support their development in a timely manner, then they would not be able to respond to the demand in the marketplace, resulting in a market shortage.

On the other hand, if too much infrastructure is built, then projects for which there is not presently a market demand would incur high carrying costs due to the market surplus, and this could adversely impact their financial feasibility.

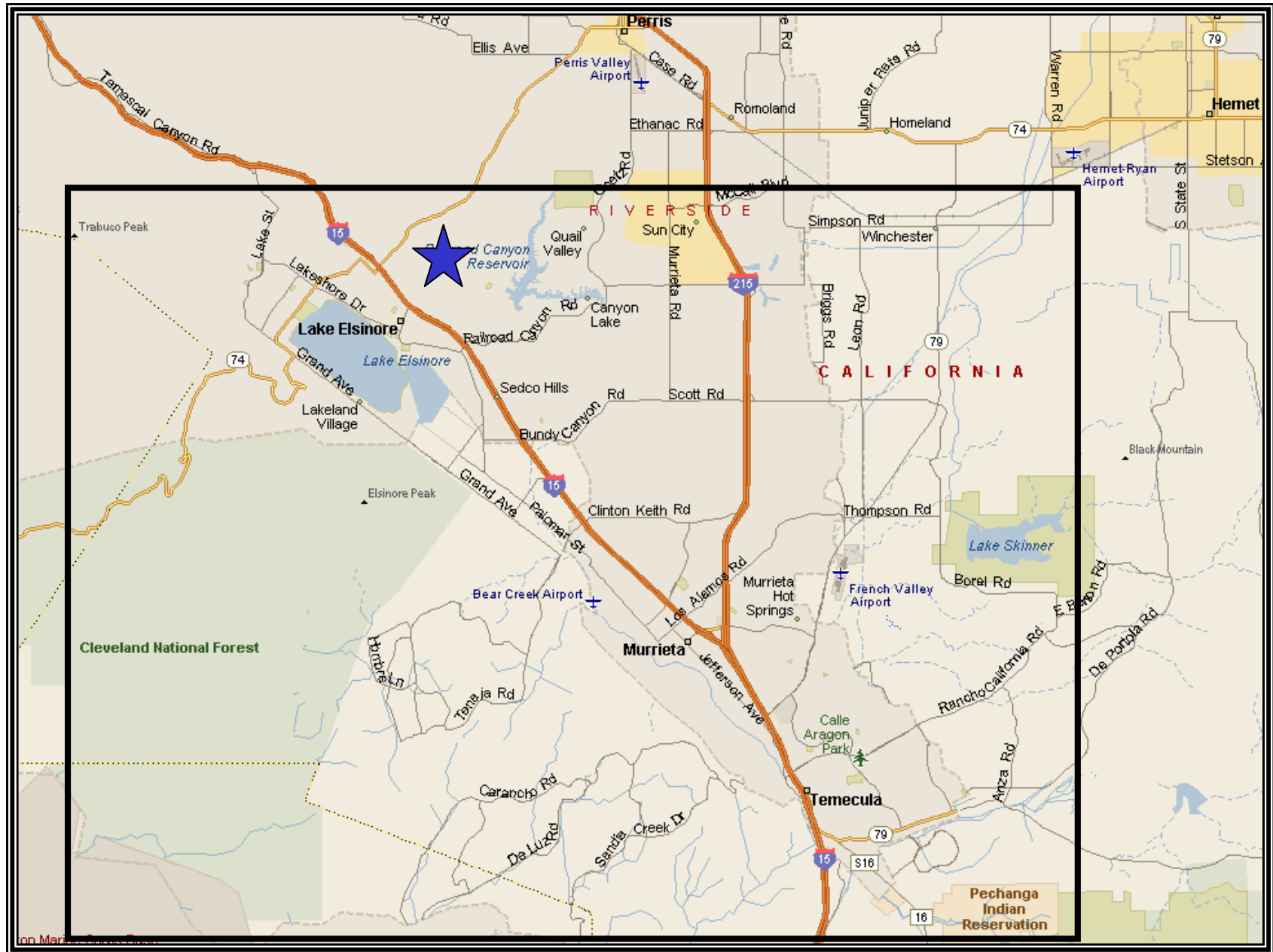
Thus, the Market Absorption Study formulates guidelines on the appropriate or optimal time-phasing and location-phasing of the infrastructure for the projects located in CFD NO. 2004-3 IA No. 2 (Rosetta Canyon) of the City of Lake Elsinore, as a means of providing the Bond Purchasers with a reasonable amount of security from a market absorption perspective.

SOUTHERN CALIFORNIA MARKET REGION



CFD NO. 2004-3 (ROSETTA CANYON)

BOUNDARIES OF THE CFD NO. 2004-3 (ROSETTA CANYON) MARKET AREA



CHARACTERISTICS OF THE EXPECTED PRODUCT MIX FOR THE CITY OF LAKE ELSINORE CFD NO. 2004-3 IA NO. 2

CFD No. 2004-3 IA No. 2 (Rosetta Canyon) is expected to have 503 single-family residential units in four different projects; the expected number of housing units as well as their characteristics, such as prices and sizes of living area, are as follows:

- * Fox & Jacob is expected to have 213 single-family homes (42.3%) that are priced from \$359,990 to \$417,990 (an average of \$392,905) for some 1,979 to 3,113 sq.ft. of living area (an average of 2,706 sq.ft.), for a value ratio (price/living area) of \$145, on the average.

- * Santa Rosa is expected to have 98 single-family homes (19.5%) that are priced from \$376,990 to \$459,990 (an average of \$421,459) for some 2,266 to 3,487 sq.ft. of living area (an average of 2,967 sq.ft.), for a value ratio (price/living area) of \$142, on the average.

- * Caraway is expected to have 78 single-family homes (15.5%) that are priced from \$414,990 to \$494,990 (an average of \$464,580) for some 2,648 to 3,258 sq.ft. of living area (an average of 2,955 sq.ft.), for a value ratio (price/living area) of \$157, on the average.

- * Augusta is expected to have 114 single-family homes (22.7%) that are priced from \$494,990 to \$553,990 (an average of \$531,244) for some 3,242 to 4,063 sq.ft. of living area (an average of 3,675 sq.ft.), for a value ratio (price/living area) of \$145, on the average.

Therefore, CFD No. 2004-3 IA No. 2 with its four projects for single-family detached homes has a broad price range, from \$359,990 to \$553,990 (an average of \$440,936) for some 1,979 to 4,063 (an average of 3,015) sq.ft. of living area, for a value ratio of some \$146, as an overall average.

Finally, it is worthwhile to note that the number of homes which are actually built-out as well as the characteristics of the homes, are subject to modification, since the marketing strategies of Centex Homes, the developer/builder, may change as a result of economic and real estate conditions.

**EXPECTED PRODUCT MIX CHARACTERISTICS
CFD NO. 2004-3 IMPROVEMENT AREA NO. 2
(ROSETTA CANYON)**

August 10, 2006; Subject to Revision

Projects	Residential Product Types			
	Fox & Jacobs	Santa Rosa	Caraway	Augusta
Product Types	Single-Family	Single-Family	Single-Family	Single-Family
Lot Size, Average	6,600	8,300	7,300	7,800
Housing Unit Mix - Estimated				
Plan # 1	23	24	23	33
Plan # 2	23	17	28	38
Plan # 3	32	30	27	43
Plan # 4	43	27		
Plan # 5	45			
Plan # 6	47			
Totals	213	98	78	114
Share	42.3%	19.5%	15.5%	22.7%
Housing Prices - Base				
Plan # 1	\$359,990	\$376,990	\$414,990	\$494,990
Plan # 2	\$379,990	\$407,990	\$475,990	\$536,990
Plan # 3	\$386,990	\$429,990	\$494,990	\$553,990
Plan # 4	\$386,990	\$459,990		
Plan # 5	\$399,990			
Plan # 6	\$417,990			
Overall Average	\$392,905	\$421,459	\$464,580	\$531,244
Living Area				
Plan # 1	1,979	2,266	2,648	3,242
Plan # 2	2,400	2,710	2,916	3,613
Plan # 3	2,613	3,206	3,258	4,063
Plan # 4	2,710	3,487		
Plan # 5	2,873			
Plan # 6	3,113			
Overall Average	2,706	2,967	2,955	3,675
Value Ratio	\$145	\$142	\$157	\$145

ROLE OF THE MARKET STUDY IN THE BOND FINANCING CFD NO. 2004-3 IA NO. 2 (ROSETTA CANYON)

The Market Absorption Study for CFD No. 2004-3 IA No. 2 (Rosetta Canyon) has a multiplicity of roles with regards to the Bond Financing; accordingly, these are now discussed.

Marketing Prospects for the
Projects

Official Statement

Prospective Bond Purchasers

Aggregate Levels of
Special Tax Revenues

Maximum Special Taxes
for the Residential Projects
Conforming to the Issuer's Policies

Share of Payments:
Developer/Builder vs. Final-Users
Determined by the Absorption Schedule

Appraisal of Property
Discounted Cash Flow – Present Value
Absorption Schedules

The Issuing Agency for the Bond Issue, CFD No. 2004-3 IA No. 2 of the City of Lake Elsinore, along with the Finance Team, can utilize the Market Absorption Study, Appraisal, and Special Tax Revenue to structure the Bond Issue.

METHODOLOGY UNDERLYING THE MARKET STUDY FOR CFD NO. 2004-3 IA NO. 2 (ROSETTA CANYON)

To perform a comprehensive analysis of the macroeconomic and microeconomic factors that are expected to influence the absorption of the residential single-family detached projects in CFD No. 2004-3 IA No. 2, Empire's Market Absorption Study conducts a systematic analysis of the following factors:

MACROECONOMIC FACTORS FOR CFD NO. 2004-3 IA NO. 2 MARKET AREA

- * Market Supply
Planning Projections
- * Market Demand
Economic Conditions
- * Reconciliation
- * Growth Potential for the
Market Area

MICROECONOMIC FACTORS FOR CFD NO. 2004-3 IA NO. 2

- Regional Development Patterns
- Socioeconomic: School and Crime
- Housing Price Trends and Patterns
- Competitive Market Analysis – Product Types
- Residential Projects
 - *Location
 - *Product Type
 - *Prices
- *Special Taxes/Assessments
- *Features/Amenities

ESTIMATED ABSORPTION SCHEDULES

Each of the Projects

- *Residential
Single-Family Detached Homes
- Four Projects
- *Market Entry to Build-Out

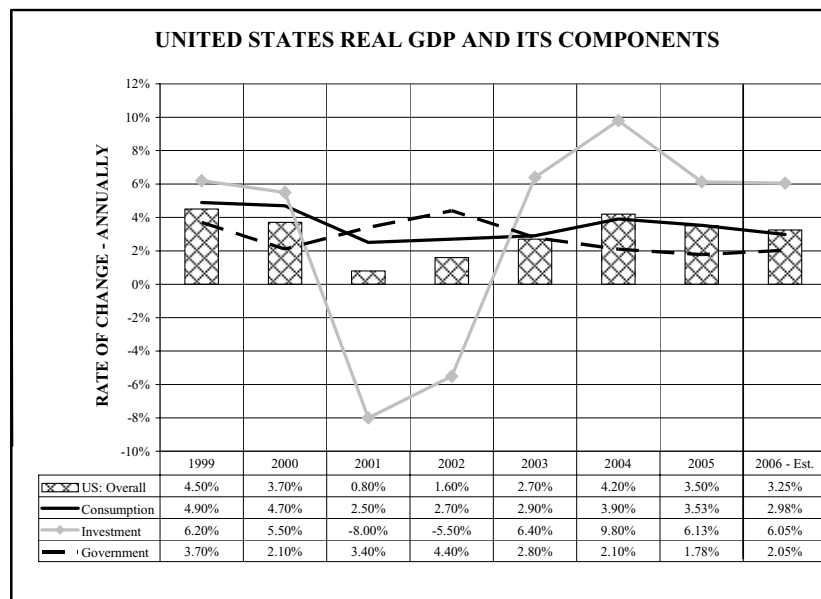
Therefore, the Market Absorption Study systematically proceeds from the macroeconomic analysis of the Market Region's future housing, industrial and commercial growth to the microeconomic analysis of the estimated absorption schedules for the residential single-family detached projects in CFD No. 2004-3 IA No. 2.

RECENT/EXPECTED ECONOMIC TRENDS/PATTERNS

The purpose of this section is to discuss the recent/expected economic trends/patterns for the United States (US), California (CA), and Riverside County (RC), including Gross Domestic Product, mortgage rates, gas prices, employment trends and housing patterns.

1. National/State Economic Trends/Patterns

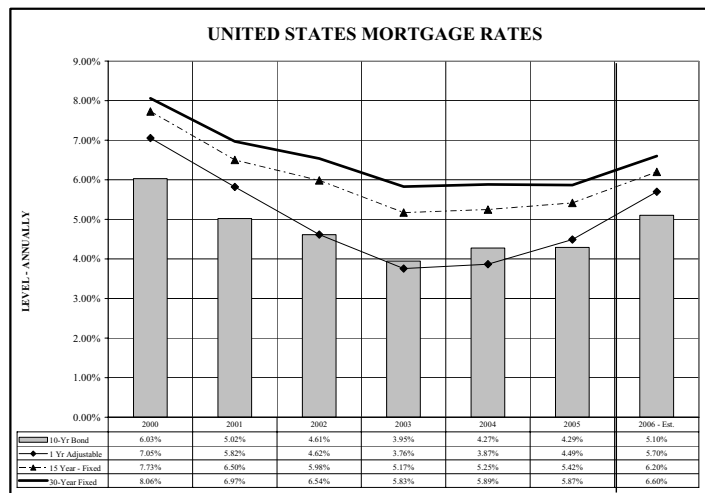
- *Gross Domestic Product (GDP)
- *Mortgage Rates
- *California Gas Prices
- *Homebuilder Stocks



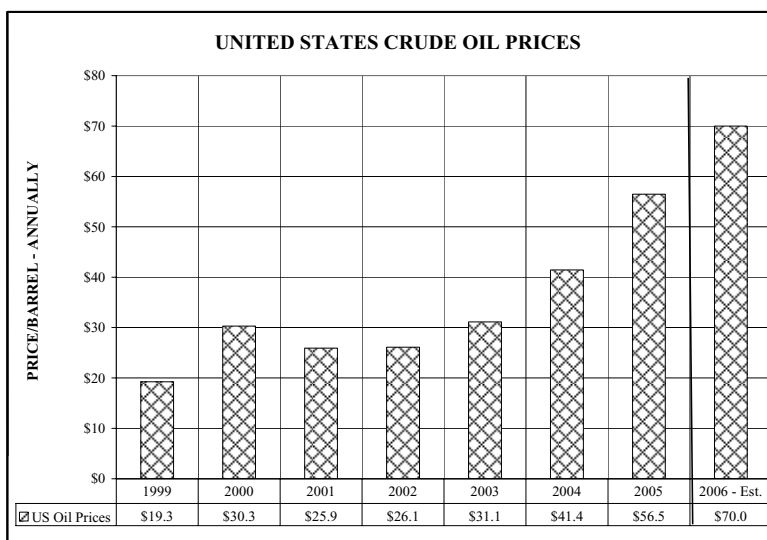
- **Overall U.S. Real GDP:** Growth moderated somewhat from a rate of 4.20% (year/year) in 2004 to a rate of 3.50% in 2005, and it is expected to moderate further in 2006, to a rate of some 3.25%.
 - **Consumption:** A growth rate of some 3.53% in 2005, but is expected to moderate somewhat to a growth rate of some 2.98% in 2006.
 - **Business Investment:** A growth rate of some 6.13% in 2005 but is expected to moderate slightly to a growth rate of some 6.05% in 2006.
 - **Government Purchases:** A growth rate of some 1.78% in 2005 and is expected to rise slightly, to a growth rate of 2.05% in 2006.

The overall rate of growth for GDP is expected to moderate somewhat; additionally, with regards to its composition, the rates of growth for consumption and investment are expected to moderate while the rate of growth for government spending is expected to increase slightly.

The relatively low levels of CPI changes during 2002 through 2005 have resulted in recent historic lows for both the 10-year bond, which is the primary driving force behind fixed rate mortgages, and also the federal fund rates, which is the primary driving force behind short-term rates, that also enhances the financial feasibility of creative financing mortgage structures.

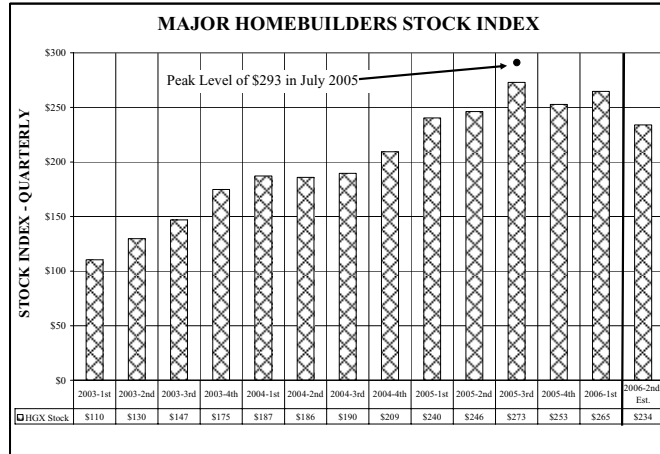


- **2000 to 2003:** The rates on the 10-year Treasury Bond, the 15 year fixed mortgage, 30 year fixed mortgage, and the 1 year adjustable mortgage all declined.
- **2004 to 2005:** The rates started to rise during 2004 and 2005 as compared to 2003: the 10-year Treasury Bond rose to 4.29% by +0.34%, the 15 year fixed mortgage increased to 5.42% by +0.25%, the 30 year fixed rate rose to 5.87% by +0.04%, and the 1 year adjustable mortgage rose to 4.49% by +0.73%.
- **2006:** As compared to 2005, the financial rates are expected to rise further, the 10-year Treasury Bond is expected to climb to 5.10% by +0.81%, the 15 year mortgage to increase to 6.20% by +0.78%, the 30 year fixed rate to 6.60% by 0.73%, and the 1 year adjustable mortgage to rise to 5.70% by +1.21%.



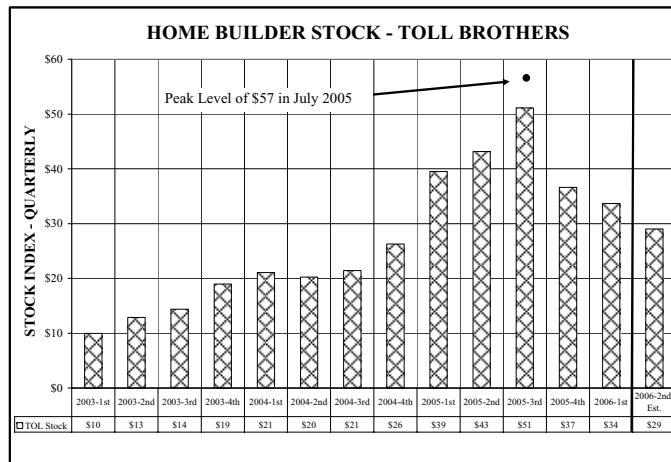
- **1999-2003:** Crude oil prices rose from \$19 a barrel in 1999 to \$31 a barrel in 2003.
- **2004-2005:** Prices rose significantly, to some \$56 a barrel.
- **2006:** Prices are expected to rise further, to some \$70 a barrel.

The recent trends in homebuilder stocks MAY provide a leading indicator of future housing market conditions, since the stock market factors reflect anticipated changes in the profitability of a firm.



The recent trends for the homebuilder stock price index, consisting of 19 major builders, referred to as HGX, have been as follows:

- **1st-2003 to 3rd-2005:** The homebuilder stock index rose dramatically from \$110 to \$273, an increase of some 154% (more than double); the peak level of \$293 occurred in July 2005.
- **3rd-2005 to 2nd-2006:** The index is expected to decline to \$234, some -20% below the prior peak level, as a result of higher mortgage rates and lower demand for housing, thereby reducing the profit margins of homebuilders.



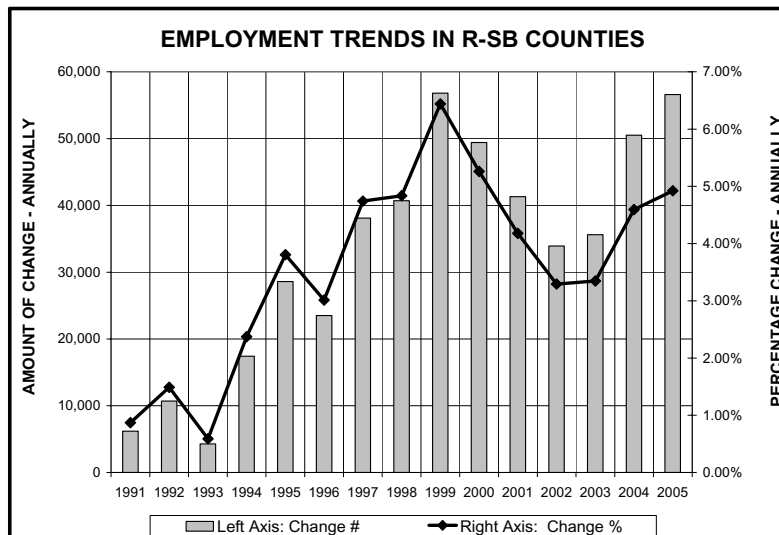
The recent stock value trends for Toll Brothers, a homebuilder primarily of luxury homes, have been as follows:

- **1st-2003 to the 3rd-2005:** The stock rose significantly from \$10 to \$51, an increase of some 400%+.
- **3rd-2005 to the 2nd-2006:** The index is expected to decline to \$29, a decrease of some -49% from the prior peak level, as a result of higher mortgage rates and slower sales reducing the profit margins for the move-up and luxury segments, as compared to the residential market as a whole.

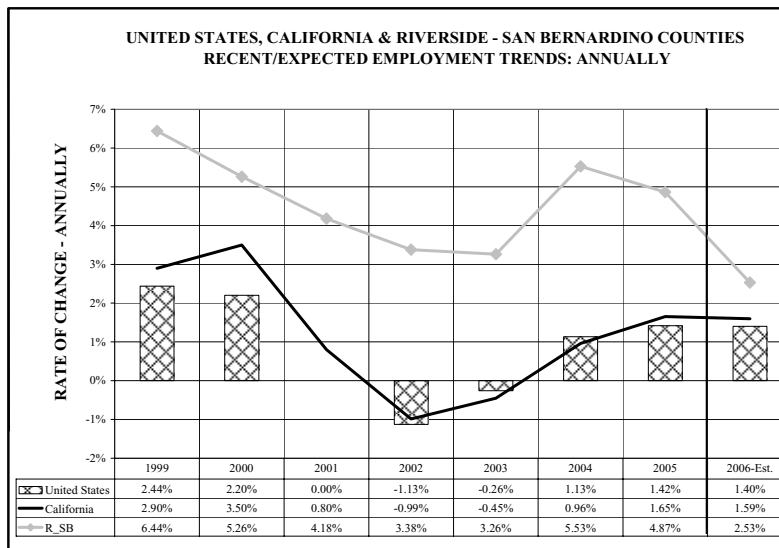
So, based upon the recent declines in homebuilder stocks, Wall Street is anticipating a slowdown in the housing market.

2. Employment Trends/Patterns

The purpose of this section is to discuss the recent/expected trends/patterns of employment activity for the United States (US), California (CA) and Riverside–San Bernardino (R-SB) counties.



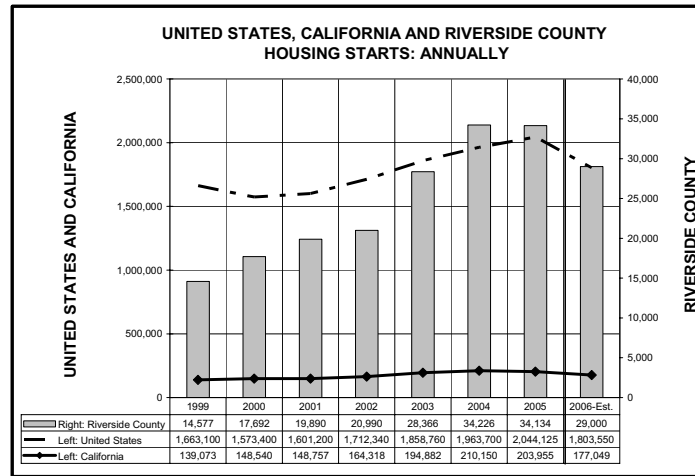
- **1991-1996:** Economic recovery, with growth rates of 15,117 or 2.02%/yr.
- **1997-2001:** Strong expansion, with growth rates of 45,260 or 5.09%/yr.
- **2002-2003:** Some moderation, growth rates of 34,750 or 3.32%/yr.
- **2004-2005:** Stronger growth rates of 53,546 or 4.76%/yr.



- **1999-2001:** The US, CA, and R-SB economies experienced moderate rates of growth during 1999 to 2000 but in 2001 their rates of growth diminished.
- **2002:** Their rates of employment growth all decreased from 2001, US experienced a decline of -1.13%, California declined by -0.99% and R-SB moderated to 3.38%.
- **2003 to 2005:** Their rates of employment growth all rose, the US to 1.42%, CA to 1.65% and R-SB to 4.87%.
- **2006:** Their rates of growth are expected to moderate, the US to 1.40%, CA to 1.59% and R-SB to 2.53%.

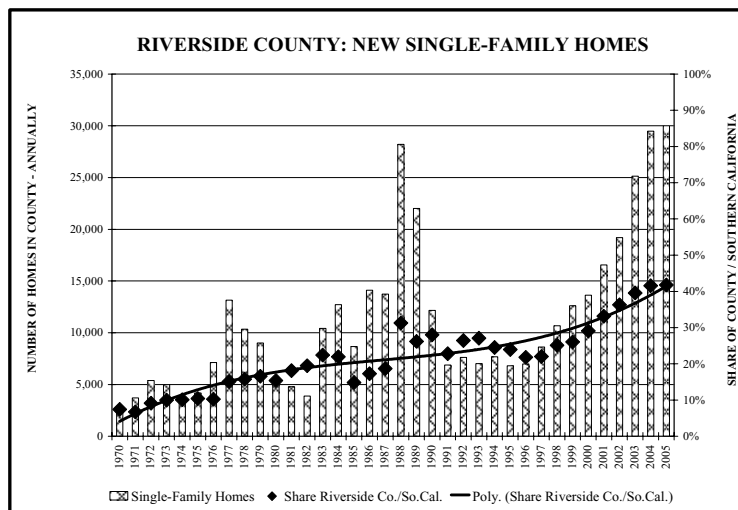
3. Housing Starts Trends/Patterns

The purpose of this section is to discuss the recent/expected trends/patterns for the levels of housing activity for the United States (US), California (CA) and Riverside County (RC).



- **1999-2001:** The US residential market experienced relatively stable levels of activity while CA and RC markets experienced a trend of higher levels of activity.
- **2002-2004:** The US, CA and RC markets experienced significant increases in their levels of activity.
- **2005:** The US market experienced a somewhat higher level of activity while for CA and RC the level of activity declined somewhat.
- **2006:** The levels of residential activity for US, CA and RC are all expected to decline somewhat, due to higher mortgage rates as well as higher gas prices.

Recent Residential Construction Activity in Riverside County



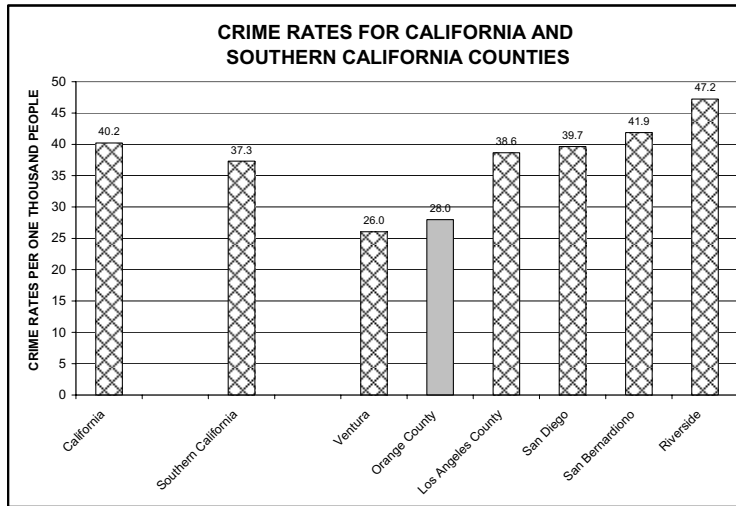
- **Major Cycles:** During the 1970-2005 time period, the number of new single-family homes in RC exhibited three major cycles, with peak levels of activity occurring in 1977, 1988 and 2005.
- **Capture Rates:** With regards to the capture rate for RC, relative to Southern California, it has demonstrated an increasing trend, from some 7% in the early 1970's to some 42% in 2005.

SOCIOECONOMICS CHARACTERISTICS: CRIME LEVELS AND THE QUALITY OF SCHOOLS

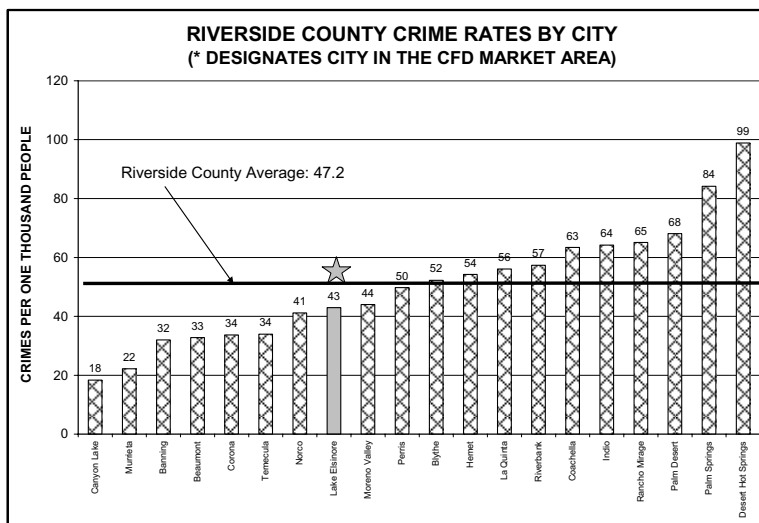
When households consider the purchase of a home, the primary factors are the location relative to their place of employment and also the price that they can afford; furthermore, secondary socioeconomic factors that are significant include the safety of the neighborhood as well as the quality of the schools.

Crime Levels and Neighborhood Safety

To gauge the safety of Riverside County and the CFD No. 2005-1 Neighborhood Area, information on crime levels was obtained utilizing the most recent data available from the Federal Bureau of Investigation (FBI) Index.



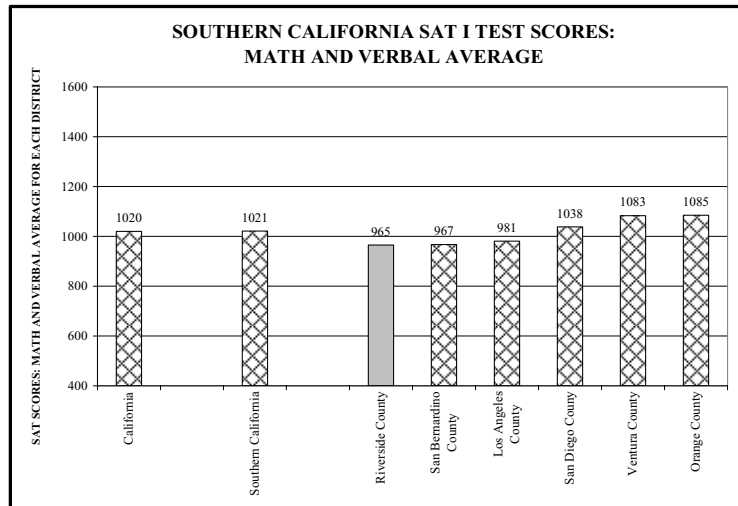
- **California:** The overall crime rate is approximately 40.2 per 1,000 people per year.
- **Southern California:** The crime rate is 37.3, slightly lower than the state.
- **Riverside County:** The crime rate is 47.2, a higher crime rate than either California or Southern California.



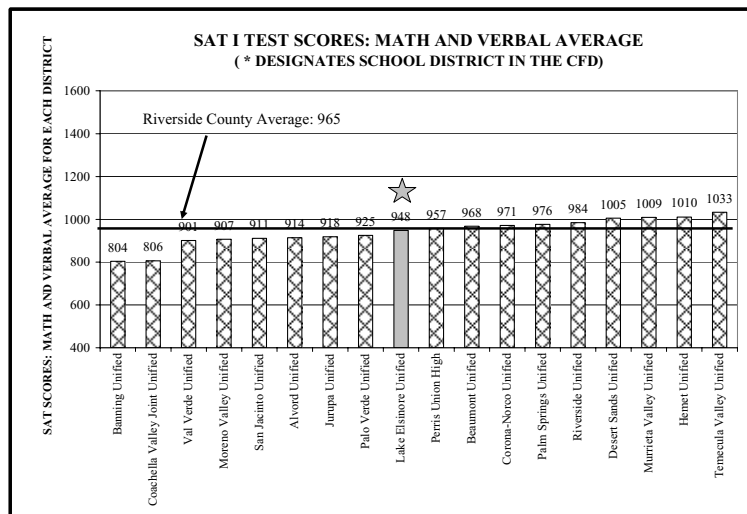
- **CFD Neighborhood Area:** This consists primarily of the City of Lake Elsinore, and this has a somewhat lower crime rate, some 43.

Quality of Schools and Education

To gauge the quality of schools in Riverside County and the CFD No. 2005-1 Neighborhood Area, information was compiled on educational achievement, specifically SAT I scores.



- **California:** The SAT I scores (with 1600 being the highest possible) amount to some 1020.
- **Southern California:** The SAT I scores amount to some 1021, similar to the state.
- **Riverside County:** The SAT I scores amount to 965, somewhat lower than for California and also Southern California.



- **CFD Neighborhood Area:** The Lake Elsinore Unified School District has a SAT I score of 948, and this is somewhat lower than for Riverside County as a whole.

Conclusions

From a socioeconomic perspective, Riverside County has a somewhat higher crime rate and a somewhat lower educational achievement level than California and also Southern California.

By comparison, the CFD Neighborhood has a somewhat lower crime rate and the school district has lower educational achievement level than Riverside County, as a whole.

COMPETITIVE MARKET ANALYSIS OF THE PROJECTS IN CFD NO. 2004-3 IA NO. 2

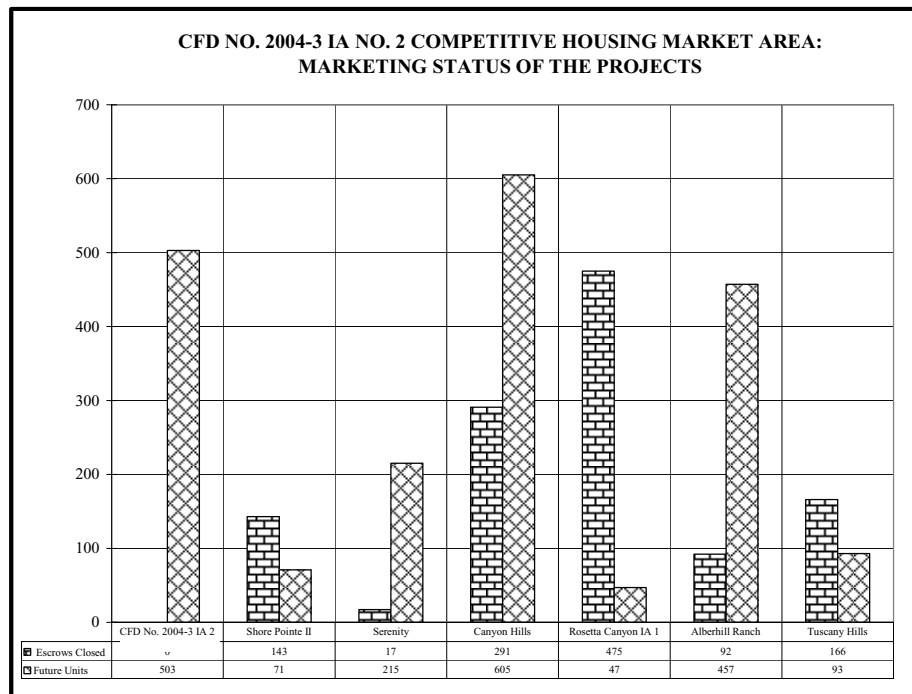
(The market surveys were updated for Rosetta Canyon as well as for Canyon Hills.)

The purpose of this section is to provide an overview of the currently active Planned Communities and their projects in the CFD No. 2004-3 IA No. 2 Competitive Housing Market Area, and then to compare these to the expected characteristics of the residential single-family detached projects in CFD No. 2004-3 IA No. 2.

The CFD No. 2004-3 IA No. 2 Housing Competitive Market Area currently has six Major Planned Communities (PCs) that are located in the City of Lake Elsinore: Shore Pointe II, Serenity, Canyon Hills, Rosetta Canyon Improvement Area (IA) I, Alberhill Ranch and Tuscany Hills.

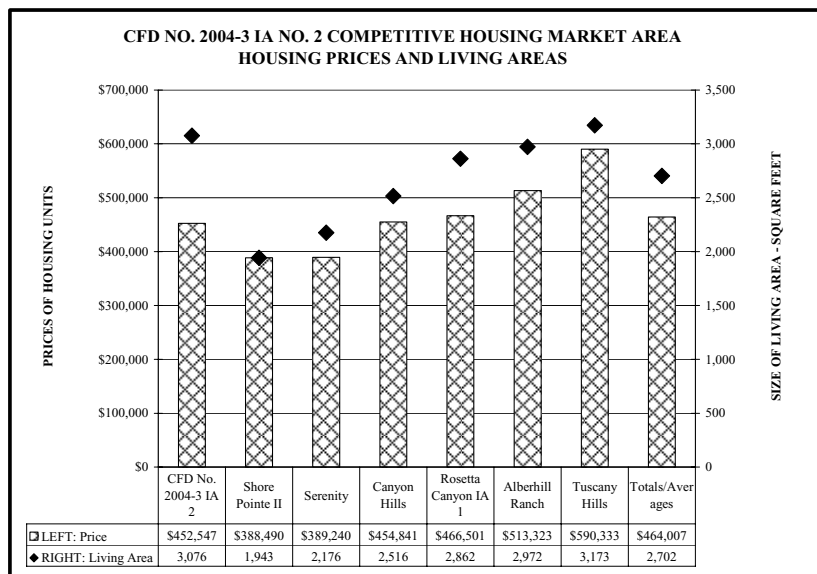
These PCs, with their twenty active projects, along with the projects in CFD No. 2004-3 IA No. 2, have a total of 3,175 housing units: 2,672 homes in the currently active projects in the PCs and another 503 homes in the projects in CFD No. 2004-3 IA No. 2; additionally, 1,184 of these homes have closed escrow.

- CFD No. 2004-3 IA No. 2: 4 projects with 503 homes.
- Shore Pointe II: 2 projects with 214 homes of which 143 have closed escrow.
- Serenity: 2 projects with 232 homes of which 17 have closed escrow.
- Canyon Hills: 7 projects with 896 homes of which 291 have closed escrow.
- Rosetta Canyon IA 1: 4 projects with 522 homes of which 475 have closed escrow.
- Alberhill Ranch: 3 projects with 549 homes of which 92 have closed escrow.
- Tuscany Hills: 2 projects with 259 homes of which 166 have closed escrow.



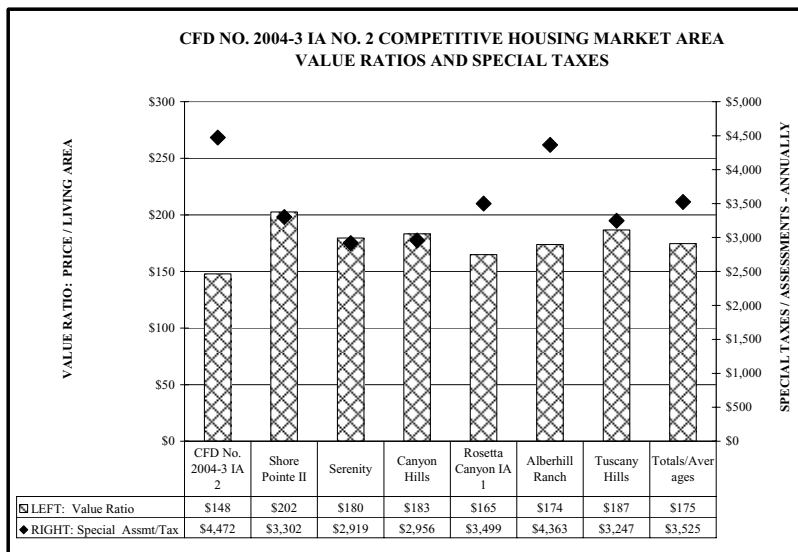
The prices of homes in these projects, including the currently active comparable projects and also the projects in the CFD, are some \$464,007 for some 2,702 sq.ft., on the average, and the prices for the projects in the various categories are as follows:

- CFD No. 2004-3 IA No. 2: \$452,547 for some 3,076 sq.ft. of living area.
- Shore Pointe II: \$388,490 for some 1,943 sq.ft. of living area.
- Serenity: \$389,240 for some 2,176 sq.ft. of living area.
- Canyon Hills: \$454,841 for some 2,516 sq.ft. of living area.
- Rosetta Canyon IA No.1: \$466,501 for some 2,862 sq.ft. of living area.
- Alberhill Ranch: \$513,323 for some 2,972 sq.ft. of living area.
- Tuscany Hills: \$590,333 for some 3,173 sq.ft. of living area.



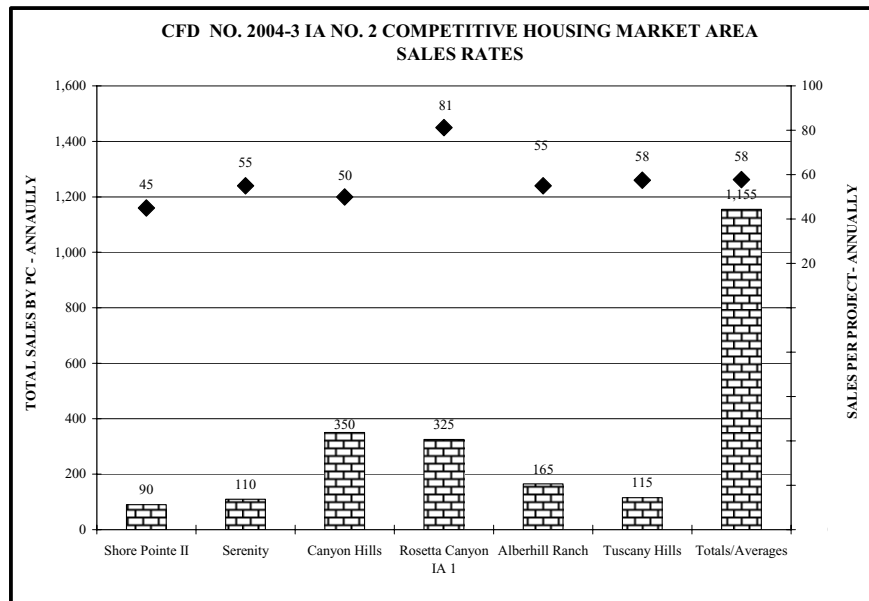
To compare the prices of the homes in these projects, their value ratios are utilized, the price per sq. ft. of living area, since this effectively makes adjustments for differences in their sizes of living areas. Accordingly, the value ratios for all of the projects amount to \$175 per sq. ft. of living area and their Special Taxes/Assessments amounts to some \$3,525/yr. (0.77% as a ratio to the housing prices); accordingly, the value ratios and Special Tax/Assessment characteristics for the product types in CFD No. 2004-3 IA No. 2 and the currently active comparable projects are as follows:

- CFD No. 2004-3 IA No. 2: expected value ratio of \$148 and the Special Taxes/Assessments amount to \$4,472/yr. (0.99%).
- Shore Pointe II: expected value ratio of \$202 and the Special Taxes/Assessments amount to \$3,302/yr. (0.85%).
- Serenity: expected value ratio of \$180 and the Special Taxes/Assessments amount to \$2,919/yr. (0.75%).
- Canyon Hills: expected value ratio of \$183 and the Special Taxes/Assessments amount to \$2,956/yr. (0.65%).
- Rosetta Canyon IA No. 1: expected value ratio of \$165 and the Special Taxes/Assessments amount to \$3,499/yr. (0.75%).
- Alberhill Ranch: expected value ratio of \$174 and the Special Taxes/Assessments amount to \$4,363/yr. (0.85%).
- Tuscany Hills: expected value ratio of \$187 and the Special Taxes/Assessments amount to \$3,247/yr. (0.55%).



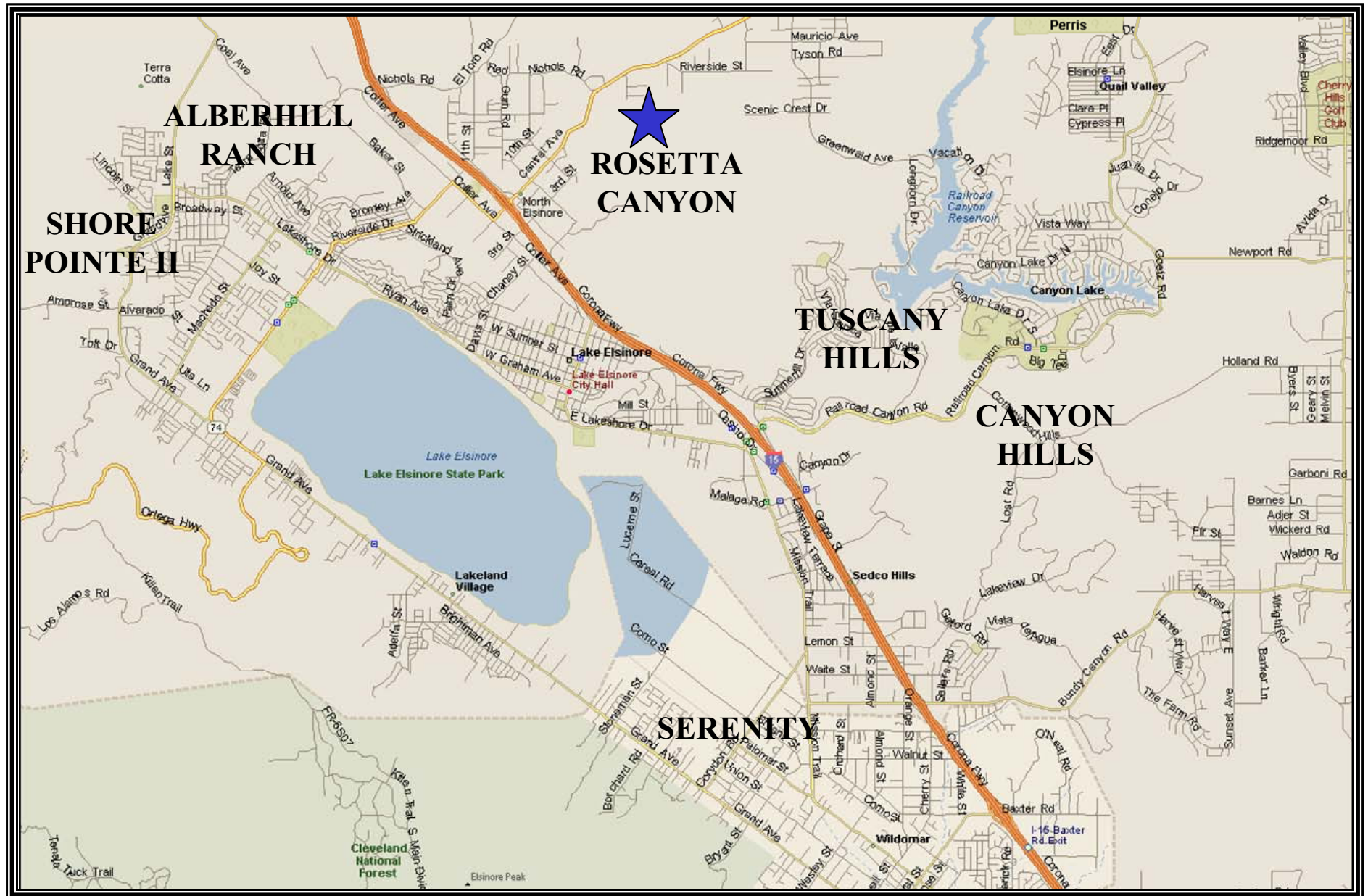
The currently active residential projects have experienced a sales rate/escrow closings at a rate of some 1,155 homes per year, for an average of some 58 units per project per year; the distribution of these sales among the various PCs is as follows:

- Shore Pointe II: an overall sales rate of 90 homes annually, some 45 per project/average.
- Serenity: an overall sales rate of 110 homes annually, some 55 per project/average.
- Canyon Hills: an overall sales rate of 350 homes annually, some 50 per project/average.
- Rosetta Canyon IA No. 1 sales rate of 325 homes annually, some 81 per project/average.
- Alberhill Ranch: an overall sales rate of 165 homes annually, some 55 per project/average.
- Tuscany Hills: an overall sales rate of 115 homes annually, some 58 per project/average.



Project Locations	Project	Builder	Product Type / Lot Sizes	Project Size and Sales				Housing Prices			Size of Living Area			Value Ratio	Special Assessments/Taxes	
				Total	Escrows Closed	Future	Sales Rate/Yr.	Lower	Average	Upper	Lower	Average	Upper		Amount/Year	Ratio/Price
CFD No. 2004-3 IA 2	Fox & Jacobs	Fox & Jacobs	6,600	213	0	213	N/A	\$359,990	\$392,905	\$417,990	1,979	2,706	3,113	\$145	\$4,055	1.03%
CFD No. 2004-3 IA 2	Santa Rosa	Fox & Jacobs	8,300	98	0	98	N/A	\$376,990	\$421,459	\$459,990	2,266	2,967	3,487	\$142	\$4,451	1.06%
CFD No. 2004-3 IA 2	Caraway	Centex Homes	7,300	78	0	78	N/A	\$414,990	\$464,580	\$494,990	2,648	2,955	3,258	\$157	\$4,452	0.96%
CFD No. 2004-3 IA 2	Augusta	Centex Homes	7,800	114	0	114	N/A	\$494,990	\$531,244	\$553,990	3,242	3,675	4,063	\$145	\$4,930	0.93%
Shore Pointe II	Emerald Collection	Forecast Homes	7,200	98	36	62	45	\$343,990	\$368,490	\$392,990	1,342	1,671	2,000	\$221	\$3,132	0.85%
Shore Pointe II	Diamond Collection	Forecast Homes	7,500	116	107	9	45	\$390,990	\$408,490	\$425,990	1,871	2,215	2,558	\$184	\$3,472	0.85%
Serenity	Fairfield	KB Home	6,500	119	0	119	60	\$351,990	\$372,990	\$393,990	1,740	1,984	2,228	\$188	\$2,797	0.75%
Serenity	Madison	KB Home	6,500	113	17	96	50	\$382,990	\$405,490	\$427,990	1,975	2,369	2,762	\$171	\$3,041	0.75%
Canyon Hills	Edgewater	Pardee Homes	4,000	108	70	38	80	\$358,000	\$376,500	\$395,000	1,683	1,894	2,105	\$199	\$2,447	0.65%
Canyon Hills	Cross Creek	Pardee	6,638	147	57	90	55	\$379,500	\$407,250	\$435,000	1,671	2,055	2,439	\$198	\$2,647	0.65%
Canyon Hills	Cedar Point	KB Home	5,500	111	91	20	45	\$417,990	\$439,990	\$461,990	2,103	2,488	2,873	\$177	\$2,860	0.65%
Canyon Hills	Weatherly	Pulte	6,525	131	21	110	50	\$430,000	\$444,500	\$459,000	1,949	2,204	2,458	\$202	\$2,889	0.65%
Canyon Hills	Briarcliff	Pardee	5,896	109	47	62	45	\$443,400	\$463,650	\$483,900	2,485	2,785	3,085	\$166	\$3,014	0.65%
Canyon Hills	Alderbrook	Pulte	6,888	143	5	138	40	\$495,000	\$504,000	\$513,000	2,607	2,855	3,103	\$177	\$3,276	0.65%
Canyon Hills	Bridgegate	Pardee	8,275	147	0	147	35	\$511,975	\$548,000	\$584,025	2,960	3,330	3,699	\$165	\$3,562	0.65%
Rosetta Canyon IA 1	Fox & Jacobs	Centex Homes	6,000	254	237	17	130	\$372,990	\$406,495	\$440,000	1,640	2,377	3,113	\$171	\$3,049	0.75%
Rosetta Canyon IA 1	Solana	Centex Homes	6,000	97	85	12	60	\$416,990	\$440,990	\$464,990	2,180	2,465	2,750	\$179	\$3,307	0.75%
Rosetta Canyon IA 1	Caraway	Centex Homes	6,000	83	80	3	70	\$458,300	\$477,489	\$498,200	2,648	2,953	3,258	\$162	\$3,581	0.75%
Rosetta Canyon IA 1	Augusta	Centex Homes	6,500	88	73	15	65	\$500,990	\$541,028	\$568,800	3,242	3,653	4,063	\$148	\$4,058	0.75%
Alberhill Ranch	Satillo	Castle & Cooke	7,000	153	67	86	80	\$423,990	\$482,490	\$540,990	2,010	2,565	3,120	\$188	\$4,101	0.85%
Alberhill Ranch	Ashburry	Castle & Cooke	7,000	206	0	206	40	\$484,990	\$521,990	\$558,990	2,764	3,166	3,568	\$165	\$4,437	0.85%
Alberhill Ranch	Capella	Castle & Cooke	7,000	190	25	165	45	\$474,990	\$535,490	\$595,990	2,531	3,185	3,838	\$168	\$4,552	0.85%
Tuscany Hills	Stone's Throw	Pulte Homes	6,000	126	100	26	60	\$535,000	\$576,165	\$617,330	2,388	2,942	3,495	\$196	\$3,169	0.55%
Tuscany Hills	Watermark	Pulte Homes	8,000	133	66	67	55	\$560,000	\$604,500	\$649,000	2,965	3,404	3,842	\$178	\$3,325	0.55%
Statistical Summary																
		Sales / Year	Projects													
CFD No. 2004-3 IA 2		N/A	4	503	0	503	N/A	\$411,740	\$452,547	\$481,740	2,534	3,076	3,480	\$147	\$4,472	0.99%
Shore Pointe II		45	2	214	143	71	90	\$367,490	\$388,490	\$409,490	1,607	1,943	2,279	\$202	\$3,302	0.85%
Serenity		55	2	232	17	215	110	\$367,490	\$389,240	\$410,990	1,858	2,176	2,495	\$180	\$2,919	0.75%
Canyon Hills		50	7	896	291	605	350	\$433,695	\$454,841	\$475,988	2,208	2,516	2,823	\$183	\$2,956	0.65%
Rosetta Canyon IA 1		81	4	522	475	47	325	\$437,318	\$466,501	\$492,998	2,428	2,862	3,296	\$165	\$3,499	0.75%
Alberhill Ranch		55	3	549	92	457	165	\$461,323	\$513,323	\$565,323	2,435	2,972	3,509	\$174	\$4,363	0.85%
Tuscany Hills		58	2	259	166	93	115	\$547,500	\$590,333	\$633,165	2,677	3,173	3,669	\$187	\$3,247	0.55%
Totals/Averages		58	24	3,175	1,184	1,991	1,155	\$432,543	\$464,007	\$493,089	2,287	2,702	3,095	\$175	\$3,525	0.77%

HOUSING MARKET AREA FOR CFD NO. 2004-3 IA NO. 2
APPROXIMATE LOCATIONS OF PLANNED COMMUNITIES



ESTIMATED ABSORPTION SCHEDULES FOR THE PROJECTS IN CFD NO. 2004-3 IA NO. 2 (ROSETTA CANYON)

The purpose of this section is to estimate the absorption schedules for the residential projects in CFD No. 2004-3 IA No. 2 (Rosetta Canyon); accordingly, this is based upon a consideration of the following:

First, the potential demand schedules for the residential projects for CFD No. 2004-3 IA No. 2 were derived, based upon a consideration of the following:

- The growth prospects for the Southern California Market Region, in general, and Riverside County, in particular.
- How much of this growth the CFD No. 2004-3 IA No. 2 Market Area is expected to capture, in particular.
- The proportion of the Market Area demand that is expected to be captured by the projects in CFD No. 2004-3 IA No. 2, based upon an evaluation of their competitiveness in the marketplace.
- For currently active projects in the Competitive Housing Market Area, their recent sales rates.
- Expected changes in the current sales rate due to anticipated higher levels of mortgage rates and gas prices during the foreseeable future when the projects in CFD No. 2004-3 IA No. 2 are on the marketplace.

Thus, the result of this analysis is the POTENTIAL demand for the residential projects in CFD No. 2004-3 IA No. 2.

Next, the ability of the residential projects in CFD No. 2004-3 IA No. 2 to respond to this demand is estimated. Accordingly, the infrastructure development schedule for the residential projects was obtained from the developer/builder. Specifically, this represents, from a time perspective, when the projects will have the infrastructure in place that is required to support their development. So, the result of this analysis is the INFRASTRUCTURE DEVELOPMENT of the projects in CFD No. 2004-3 IA No. 2, and this reflects their ability to respond to the demand in the marketplace.

Then, based upon a consideration of the POTENTIAL demand and the INFRASTRUCTURE DEVELOPMENT, the absorption rate for the residential projects are calculated, from the year in which the projects are expected to enter the marketplace, and continuing thereafter on an annualized basis, until all of the units are occupied.

The application of this algorithm results in the absorption schedules for the projects in CFD No. 2004-3 IA No. 2; absorption represents the structures being constructed as well as being occupied by households. Accordingly, the estimated absorption schedules for the 503 homes in the CFD No. 2004-3 IA No. 2 projects for Rosetta Canyon are as follows:

- * Fox & Jacob is expected to have 213 single-family homes (42.3%) that are priced from \$359,990 to \$417,990 (an average of \$392,905) for some 1,979 to 3,113 sq.ft. of living area (an average of 2,706 sq.ft.), for a value ratio (price/living area) of \$145, on the average.

These homes are expected to commenced escrow closings/move-ins during 4th-quarter of 2006, and are expected to be absorbed at a rate of 35 homes in 2006, 80 homes per year in 2007 and also 2008, and then the remaining 18 homes in 2009.

- * Santa Rosa is expected to have 98 single-family homes (19.5%) that are priced from \$376,990 to \$459,990 (an average of \$421,459) for some 2,266 to 3,487 sq.ft. of living area (an average of 2,967 sq.ft.), for a value ratio (price/living area) of \$142, on the average.

These homes are expected to commenced escrow closings/move-ins during the 4th-quarter of 2006, and are expected to be absorbed at a rate of 20 homes in 2006, 40 homes in 2007, and then the remaining 38 homes in 2008.

- * Caraway is expected to have 78 single-family homes (15.5%) that are priced from \$414,990 to \$494,990 (an average of \$464,580) for some 2,648 to 3,258 sq.ft. of living area (an average of 2,955 sq.ft.), for a value ratio (price/living area) of \$157, on the average.

These homes are expected to commenced escrow closings/move-ins during the 1st-quarter of 2007, and are expected to be absorbed at a rate of 40 homes per year in 2007 and then the remaining 38 homes in 2008.

- * Augusta is expected to have 114 single-family homes (22.7%) that are priced from \$494,990 to \$553,990 (an average of \$531,244) for some 3,242 to 4,063 sq.ft. of living area (an average of 3,675 sq.ft.), for a value ratio (price/living area) of \$145, on the average.

These homes are expected to commenced escrow closings/move-ins during the 1st-quarter of 2007, and are expected to be absorbed at a rate of 50 homes in 2007, another 50 homes in 2008, and then the remaining 14 homes in 2009.

The 503 single-family detached homes in CFD No. 2004-3 IA No. 2 are expected to be absorbed during the late 2006 through 2009 time period; the rate of absorption is estimated to be as follows:

In 2006, as two projects commence escrow closings, some 55 homes.

In 2007, as the other two projects commence escrow closings, 210 homes.

In 2008, as all of the projects are on the marketplace, 206 homes, with two projects closing out.

Finally, in 2009, the remaining 32 homes, with the remaining two projects closing-out.

The expected absorption schedules for the projects in CFD No. 2004-3 IA No. 2 can also be expressed as a capture rate of the expected market demand for the CFD No. 2004-3 IA No. 2 MA, the southwestern portion of Riverside County. Specifically, the capture rate reflects the percentage of the MA's demand that is fulfilled by the absorption of the homes in CFD No. 2004-3 IA No. 2.

With respect to the capture rates of the demand in the Market Area, they are as follows: In 2006, as the projects commence escrow closings, the CFD No. 2004-3 IA No. 2's capture rate on the MA's demand is some 1.5%. Then, in 2007 and 2008, when all of the projects have escrow closings, the capture rates are some 5.6% and 5.2%, respectively. Finally, in 2009, as the remaining homes in the projects are closed-out, the capture rate declines to some 0.8%. For the 2006-2009 time period, as a whole, the overall capture rate amounts to some 3.3% of the demand in the Market Area, on the average.

The estimated absorption schedules for the residential projects in CFD No. 2004-3 IA No. 2 are subject to change due to potential shifts in economic/real estate market conditions and/or the development strategy by the developer/builder, Centex Homes.

For additional information on the estimated absorption schedules for the residential products in CFD No. 2004-3 IA No. 2 (Rosetta Canyon), please refer to the following table and graphs.

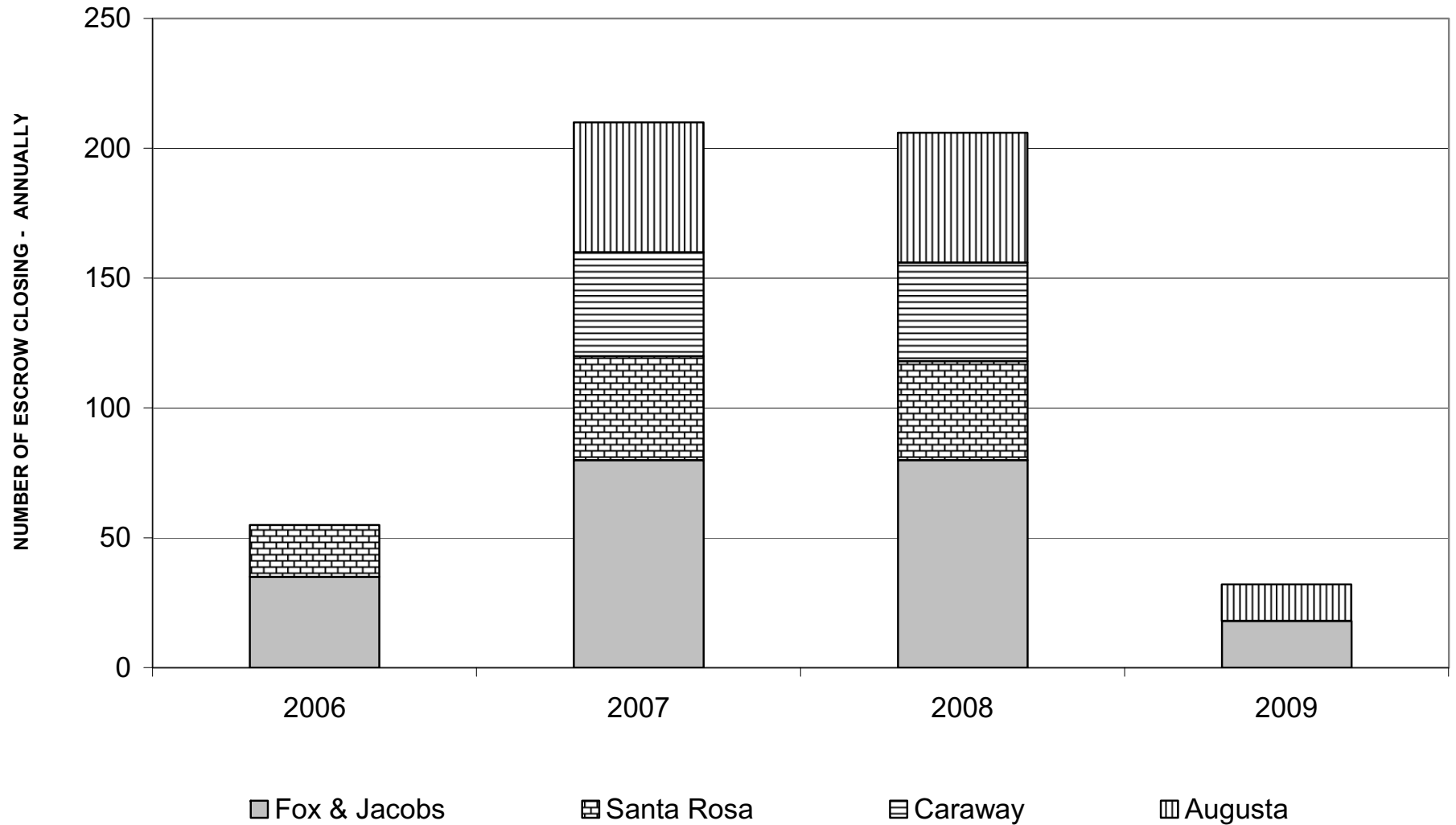
Please refer to the section following the table and graphs of the estimated absorption schedules for the residential products in CFD No. 2004-3 IA No. 2 for a discussion of the "Potential Financial Risk Factors Underlying Land Secured Financings in Southern California".

**ESTIMATED ABSORPTION SCHEDULES
CFD NO. 2004-3 IMPROVEMENT AREA NO. 2
(ROSETTA CANYON)**

August 10, 2006; Subject to Revision

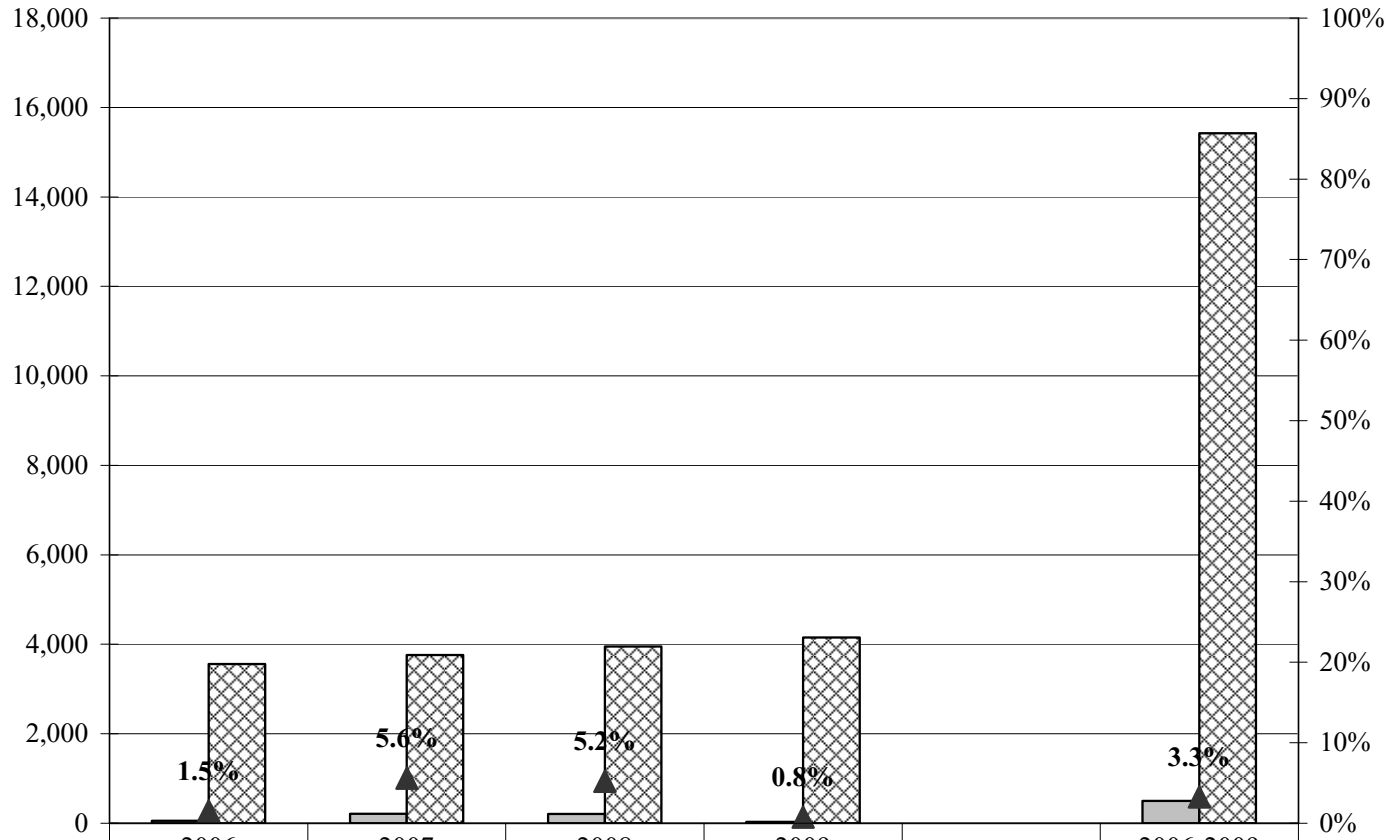
Projects	Residential Product Types				Totals - Residential	
	Fox & Jacobs	Santa Rosa	Caraway	Augusta	Annually	Cumul.
Product Types	Single-Family	Single-Family	Single-Family	Single-Family		
Lot Size, Average	6,600	8,300	7,300	7,800		
Housing Unit Mix - Estimated						
Plan # 1	23	24	23	33		
Plan # 2	23	17	28	38		
Plan # 3	32	30	27	43		
Plan # 4	43	27				
Plan # 5	45					
Plan # 6	47					
Totals	213	98	78	114	503	100.0%
Share	42.3%	19.5%	15.5%	22.7%	100.0%	
Housing Prices - Base						
Plan # 1	\$359,990	\$376,990	\$414,990	\$494,990		
Plan # 2	\$379,990	\$407,990	\$475,990	\$536,990		
Plan # 3	\$386,990	\$429,990	\$494,990	\$553,990		
Plan # 4	\$386,990	\$459,990				
Plan # 5	\$399,990					
Plan # 6	\$417,990					
Overall Average	\$392,905	\$421,459	\$464,580	\$531,244	\$440,936	
Living Area						
Plan # 1	1,979	2,266	2,648	3,242		
Plan # 2	2,400	2,710	2,916	3,613		
Plan # 3	2,613	3,206	3,258	4,063		
Plan # 4	2,710	3,487				
Plan # 5	2,873					
Plan # 6	3,113					
Overall Average	2,706	2,967	2,955	3,675	3,015	
Value Ratio	\$145	\$142	\$157	\$145	\$146	
Commence Escrow Closings	4th-2006	4th-2006	1st-2007	1st-2007		
Absorption: (Escrow Closings)						
2006	35	20	0	0	55	55
2007	80	40	40	50	210	265
2008	80	38	38	50	206	471
2009	18	0	0	14	32	503
Totals	213	98	78	114	503	

**CITY OF LAKE ELSINORE CFD NO. 2004-3 IA NO. 2 (ROSETTA CANYON)
ESTIMATED RESIDENTIAL ABSORPTION SCHEDULES**



**CFD NO. 2004-3 IA NO. 2 (ROSETTA CANYON)
ABSORPTION SCHEDULE AS WELL AS THE CAPTURE RATE**

MARKET AREA DEMAND AND CFD ABSORPTION



CAPTURE RATE OF CFD TO MARKET AREA

■ CFD No.2004-3 IA No. 2	55	210	206	32	503
▨ Market Area	3,560	3,758	3,955	4,153	15,426
▲ Capture Rate	1.5%	5.6%	5.2%	0.8%	3.3%

POTENTIAL “FINANCIAL” RISK FACTORS UNDERLYING THE CREDIT QUALITY AND BOND SIZING FOR LAND SECURED FINANCINGS IN SOUTHERN CALIFORNIA

There has been a fundamental shift in the driving force underlying the recent rates of housing price appreciation, from the historical role of employment growth as the driving force to the recent role of adjustable rate and creative financing techniques as the driving force. Since January 2002, these financial factors have been the primary driving force underling the extraordinary rate of housing price appreciation in Southern California, more than 70%. However, the economic feasibility of creative financing has recently diminished, as both short-term and long-terms rates have risen. Consequently the current levels of housing prices and land values are subject to potentially substantial downward adjustments, due to mortgage rate resets (as mortgages are adjusted from teaser rates to market rates) as well as higher short-term rates (due to rate hikes by the Federal Reserve Board). These adjustments, in turn, may cause a softening in housing prices and land values that could adversely impact the credit quality underlying land-secured financings.

Financial Risk Factors: CFDs vs. Overall Market

CFDs with newly developing residential projects have characteristics that make them more vulnerable to a housing market bubble than national or regional markets. Specifically, CFDs represent the marketing of new homes to purchasers at current prices that utilize creative financing structures and they are also concentrated in particular geographical locations.

CHARACTERISTICS	OVERALL MARKET	COMMUNITY FACILITIES DISTRICT
Geographical Location	Broad	CFD - Focused Area
Time of Purchase	Long Time Span: 10- 20 Years	Recently
Type of Financing Structure	Mostly > Fixed Rates > Amortization of Principal	Predominantly > Adjustable & Creative > Higher Loan Balances
Amount of Equity	Significant; Accumulated Over Time	Minimal > Recent Purchase > Negative Amortization
Timing of Loan Resets	Minimal & Spread Over Time	Most & Similar Time

Definition of Creative Financing

Creative financing, as utilized herein, refers to the use of loan structures other than fixed-rate or one-year adjustable loan structures that provide for amortization of principal; some examples of creative structures are as follows:

- Interest only payments.
- Payment option loans (with minimum payment options).
- Loans with initial teaser rates (below market rates that are offered only for a limited time period).

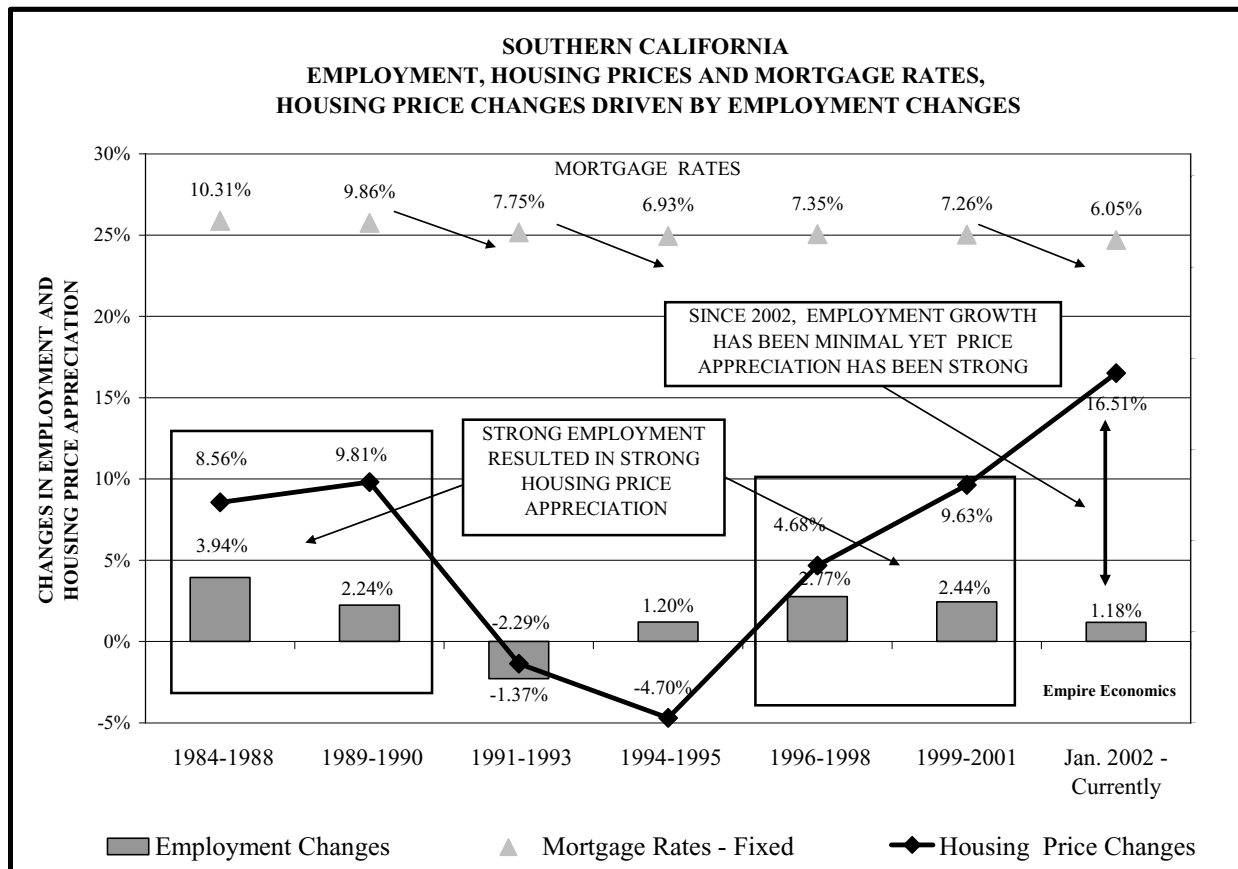
Additional factors related to creative loan structures include:

- Less stringent lending standards such as low/no documentation.
- Higher mortgage payment to income ratios.

1. Structural Shift in the Primary Factors Underlying Housing Price Appreciation: From Employment Growth to Creative Financing

The primary factors underlying housing price appreciation in Southern California since January 2002, declining mortgage rates as well as the extensive use of adjustable and creative financing, represent a fundamental shift from the traditional factor, employment growth.

- During 1984-2001 housing price appreciation was driven by employment growth, along with accommodating financial factors, such as stable or somewhat declining mortgage rates. During this time period financial factors played only a secondary role: for instance, over 1991-1993 when employment decreased, housing prices declined, even though mortgage rates fell by more than two percentage points from their 1989-1990 levels.
- However, since January 2002, as housing prices escalated at strong rates, the primary fundamental factor, employment growth, has experienced only minimal growth, some 1.18% per year, on the average. Instead, housing price appreciation has been driven primarily by financial factors, particularly the use of adjustable rate mortgages and creative financing techniques.



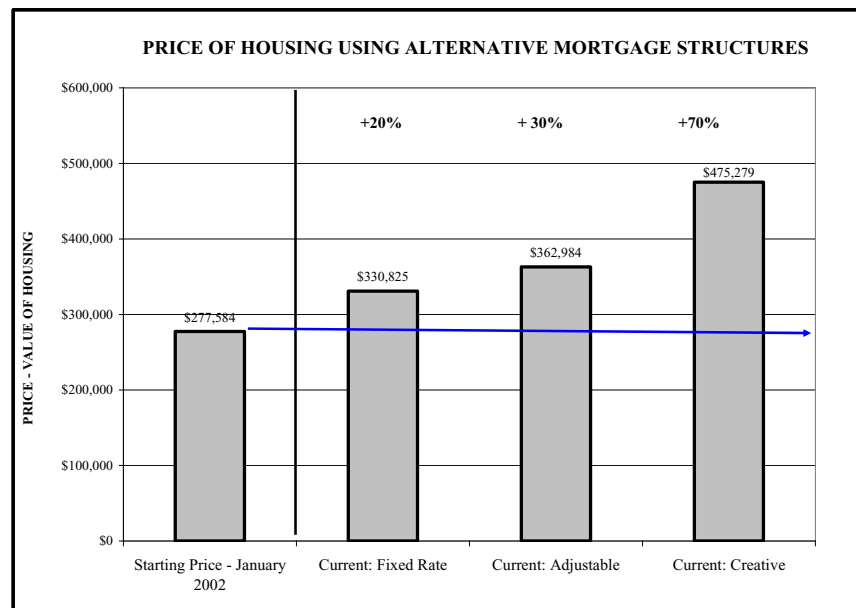
Sources: Empire Economics, Employment Development Department, Freddie Mac & Office of Federal Housing

2. Role of Financial Factors Underlying Recent Rates of Housing Price Appreciation

Since January 2002, the primary driving forces underlying housing price appreciation have been as follows:

- Households initially taking advantage of recent historically low fixed rates, through June 2003.
- A shift to adjustable rate mortgages, through March 2004.
- Since April 2004, the use of creative financing structures.

The impacts of creative mortgage financing structures on the price of housing can be gauged by estimating the prices that households could afford to pay utilizing the various structures; the starting price for housing, as of January 2002, was some \$278,000, and prices have recently increased to some \$475,000, a change of more than 70%.



- **Fixed Rates:** Based upon the recent historic low for fixed rates, which occurred in June 2003, the price amounted to some \$350,000, an increase of \$72,000; however, using current fixed rates, the most recent price amounts to some \$331,000, some -\$144,000 below current price levels.
- **Adjustable Rates:** Based upon the recent historic low for adjustable rates, which occurred in March 2004, the price amounted to some \$444,000, an increase of \$164,000; however, using current adjustable rates, the most recent price amounts to some \$363,000, some -\$112,300 below current price levels.
- **Creative Financing:** Based upon the rates for creative financing, the price currently amounts to some \$475,000, an increase of \$197,000 above the price for housing as of January 2002 of some \$278,000.

3. Potential Risk Factors for Purchasers Utilizing Creative Financing Structures

The purchasers of homes that utilize creative financing structures are able to “afford” homes at current market prices; however, their rates are subject to resets that will cause their payments to rise substantially, and so they face the risk of potentially becoming delinquent on their mortgage and tax payments.

3-A. Purchasers Using Creative Financing and Mortgage Loan Resets

Purchasers of homes that utilize creative financing are subject to resets, as their initial teaser rates are re-aligned to the market rates, and so their mortgage payments are likely to increase significantly.

The potential for mortgage reset is illustrated below, using a home with a price of \$500,000 that is fully financed, with no down payment, something that buyers often do using first and second mortgages:

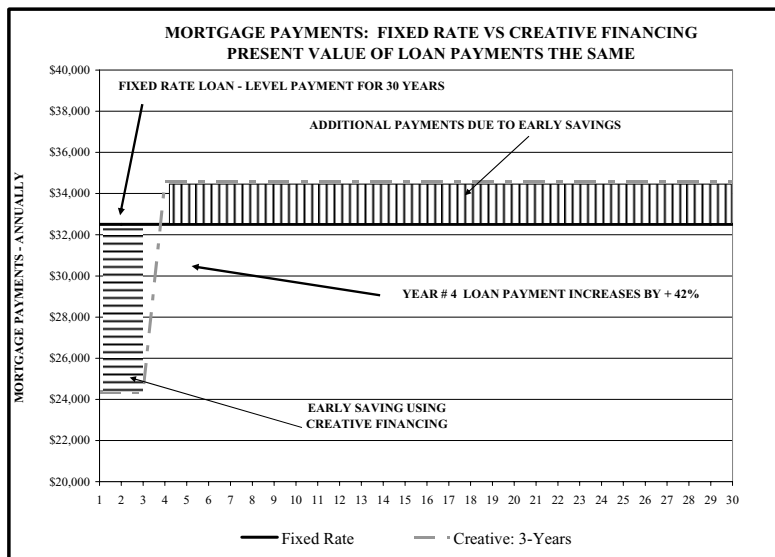
Fixed Rate Loan Structure:

- Mortgage payment of some \$32,500 per year.

Creative Loan Structure:

- First three years, \$24,375 per year, using a teaser rate interest only payment.
- Starting in the fourth year, when the loan payment is adjusted to the market rate and fully amortized to pay principal as well, the payment rises to some \$34,600 per year.

Therefore, the mortgage payment for the fourth year and thereafter is some 42% higher than for the first three years, an increase of some \$10,225 per year.



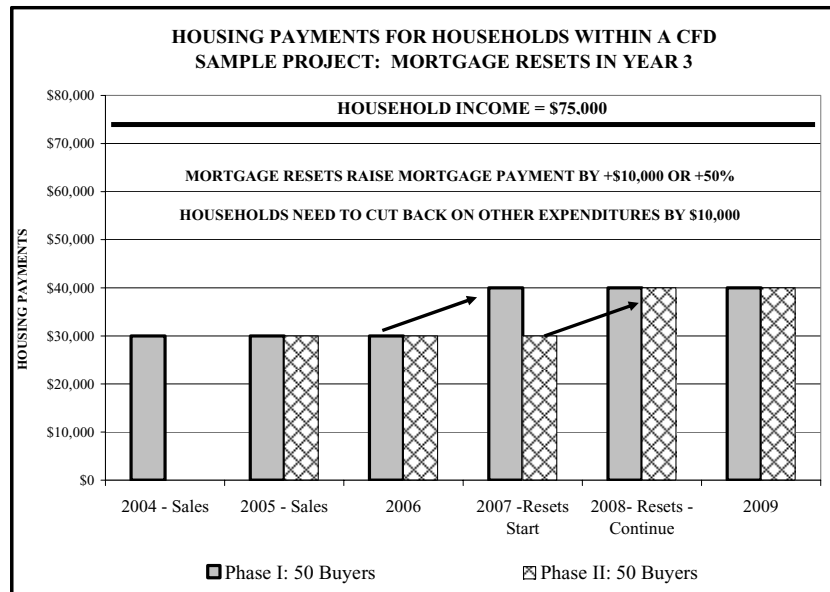
With regard to the amount of mortgages that are subject to such resets, based upon data for the United States mortgage market as a whole, these are expected to rise dramatically, from some \$0.83 billion in 2005 to more that \$1.0 trillion in 2007.

Furthermore, it is worthwhile to note that with regards to CFDs in particular, mortgage resets are expected to be significant, since most of the recent purchasers have utilized creative financing.

3 - B. Example of Purchasers of Homes in a Residential Project with Mortgage Resets

The following example provides a simulation of the potential impacts of mortgage resets for the recent purchasers of homes in a newly developing residential project:

- **Price of Homes:** \$500,000
- **Household Income:** \$75,000
- **Fully Mortgaged:** 100% First of 80% and second of 20%
- **Creative Structure:**
 - Interest only for first three years: \$20,000 per year
 - Interest and amortization: next 27 years: \$30,000 per year
- **Property and Special Taxes:** 2.0%, \$10,000 per year.



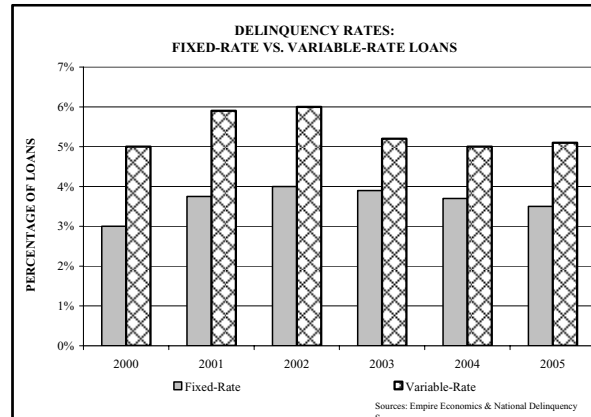
Accordingly, the application of these assumptions results in the following scenario:

- **Phase I:** 50 buyers in 2004 have payments of \$30,000 per year until 2007 when the reset cause the payment to escalate to \$40,000 per year. (mortgage payment rises by \$10,000)
- **Phase II:** 50 buyers in 2005 follows a similar pattern, with a year's delay.
- **2006:** The buyers in both phases have stable payments, and so the delinquency rate is expected to be normal.
- **2007:** The first 50 buyers have their payment rise by some \$10,000.
- **2008:** The buyers in Phase II which have their payments also rise.

The delinquency rates resulting from these mortgage payment increases will be determined by a multiplicity of factors, including the financial reserves of the households, their ability to reduce other expenditures, and so forth. Nevertheless, an increase in the mortgage payment by some \$10,000 may prove to be beyond the financial capabilities of some of the households. Furthermore, their motivation to re-allocate funds to the mortgage payment may be diminished by their low levels of equity (100% financing and negative amortization).

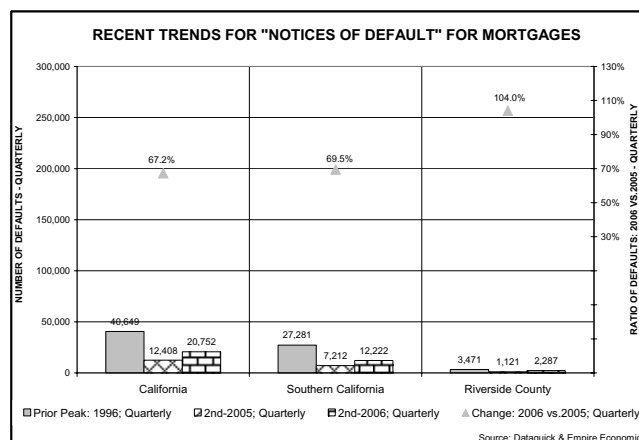
3 – C Delinquency Rates and Types of Loans

From an historical perspective, the mortgage delinquency levels for homeowners with adjustable mortgages have traditionally been significantly higher than for homeowners with fixed rate loans. During the 2000-2005 time period, the 5.4% delinquency rate for adjustable rate loans has been above the 3.6% delinquency rate for fixed rate loans by some 50% (5.4% vs. 3.6%). This is typically attributed to homeowners with adjustable rate loans having difficulty with higher mortgage payments as rates rise as well as such households having “low” equity levels (due to higher loan to price ratios as well as negative amortization), and hence less of an incentive to “hold-on” to the home.



However, the potential delinquency rates for households with creative financing does not have an historical track record, since such loan structures have just become available recently, and so they have not yet been tested under adverse real estate and economic conditions. Considering that creative loans are subject to substantial increase in mortgage payments when they are reset, as compared to traditional adjustable loans which vary only due to interest rates fluctuations, their delinquency rates are likely to be substantially higher.

A “leading” indicator of higher Special Tax delinquency rates may be “notices of default” that are recorded against homes that are not making their mortgage payments on a timely basis.



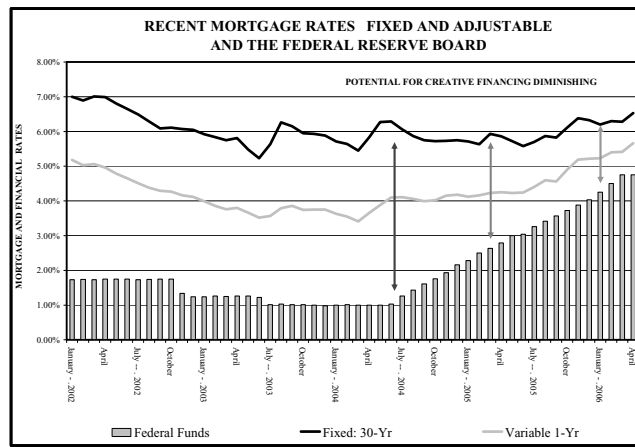
Therefore, although a project may initially have low delinquency levels, when the resets start to occur several years after the original purchase, then the delinquency rates may rise dramatically, since most of the buyers in the project have similar financing structures. Furthermore, these delinquency rate increases may occur despite the higher value of the homes (but minimal equity) and favorable economic growth (not a recession).

4. Potential Challenges for Purchasers Utilizing Traditional Financing Structures

The purchasers of homes that are now utilizing traditional financing structures are NOT able to “afford” homes at current market prices, and so this may cause the rate of sales to slowdown unless builders offer them substantial concessions.

4–A. Diminishing Potential of Creative Financing

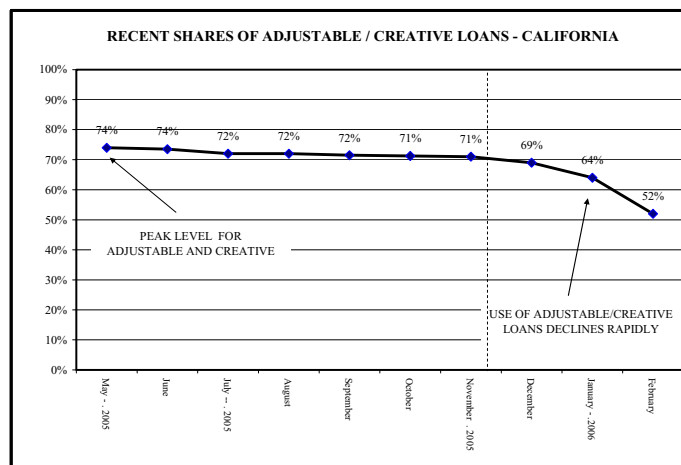
The potential for creative financing as a means of enhancing the purchasing power of prospective homebuyers has diminished recently, due primarily to the Federal Reserve Board raising the Federal Funds Rate. Specifically, the “spread” between conventional financing and teaser rates has been compressed as a result of the flattening of the yield curve (the vertical arrows diminish in size).



4–B. Recent Shift Towards Traditional Financing Structures

The purchasers of new homes now face higher mortgage rates, since the availability of creative financing has recently diminished, due to the flattening of the yield curve; additionally, the yields on the ten year bond which influences the 15-year and 30-year fixed rate mortgages have also increased as well.

In recent months, the proportion of buyers using creative financing has recently declined from some 71% in November 2005 to 64% in January 2006 and then further to 52% as of February 2006.



As the purchasers of new homes move back towards the more traditional financing structures, their purchasing power may not be able to support the recent prices which were bolstered by the use of creative structures which currently support a price of some \$475,000, an increase of \$197,000 above the January 2002 levels.

- **Fixed Rates:** Based upon current fixed rates, the supportable price amounts to some \$331,000, some -\$144,000 below the actual current price levels.
- **Adjustable Rates:** Based upon current adjustable rates, the supportable price amounts to some \$363,000, some -\$112,300 below the actual current price levels.

Therefore, the purchasers of new homes that use the traditional financing structures will encounter challenges in paying the current prices, since their purchasing power with traditional loan structures is significantly below their purchasing power with creative structures. So, the real estate market is expected to encounter some significant adjustments, through a combination of lower prices, enhanced builder incentives, and slower sales rates.

5. Conclusions

The housing market is expected to experience some significant adjustments during the foreseeable future, as the current price structure, which is based upon the extensive use of creative financing, is re-aligned with a sustainable price structure, which is based upon the use of more traditional financing structures:

- The purchasers of homes that are utilizing creative financing structures are able to “afford” homes at current market prices; however, such structures are subject to resets that will cause their payments to rise substantially, and so they face the risk of becoming delinquent on their mortgage and tax payments.
- The purchasers of homes that are utilizing traditional financing structures are NOT able to “afford” homes at current market prices, and so their inability to do so may cause the rate of sales to slowdown, unless builders offer them substantial concessions, and eventually lower prices.

These market adjustments are expected to have a much more significant impact on newly developing residential CFDs than the broader market, as a whole, since CFDs represent the marketing of new homes to purchasers at current prices and they are also concentrated in particular geographical locations.

ASSUMPTIONS AND LIMITING CONDITIONS

The Market Absorption Study for CFD No. 2004-3 IA No. 2 is based upon various assumptions and limiting conditions; accordingly, these are as follows:

Title to Property

No opinion as to title is rendered. Data related to ownership and legal description, obtained from governmental records related to the formation of the District that forms the basis for identifying the boundaries of CFD No. 2004-3 IA No. 2 are considered reliable. Title is assumed to be marketable and free and clear of all liens, encumbrances, easements and restrictions except those specifically discussed in the report. The property is evaluated assuming to be under responsible ownership and competent management and available for development to highest and best use.

Property Boundaries

No survey or engineering analysis of CFD No. 2004-3 IA No. 2 property has been made by the market analyst; the District Engineer's report utilized for the Bond is deemed to be reliable. The market analyst assumes the existing boundaries to be correct, that no encroachments exist and assumes no responsibility for any condition not readily observable from customary investigation and inspection of the premises, which might affect the valuation, excepting those items which were specifically mentioned in the report.

Accuracy of Information from Others

In preparing this report, the market analyst was required to rely on information furnished by other individuals or found in previously existing records and/or documents. Unless otherwise indicated, such information is presumed to be reliable. However, no warranty, either expressed or implied, is given by the market analyst for the accuracy of such information and the market analyst assumes no responsibility for information relied upon and later found to have been inaccurate. The market analyst reserves the right to make such adjustments to the analyses, opinions and conclusions set forth in this report as may be required by consideration of additional data or more reliable data that may become available.

Date of Study

The date to which the conclusions and opinions expressed in this report apply as set forth in the study. Furthermore, the dollar amount of any price/value opinion rendered was based upon the purchasing power of the American dollar existing on that date.

Hidden or Unapparent Conditions

The market analyst assumes no responsibility for hidden or unapparent conditions of the property, subsoil, groundwater or structures that render the subject property more or less valuable. No responsibility is assumed for arranging for engineering, geologic or environmental studies that may be required to discover such hidden or unapparent conditions.

Opinions of a Legal/Specialized Nature

No opinion is intended to be expressed for matters which require legal expertise or specialized investigation or knowledge beyond that customarily employed by the market analyst.

Right of Publication of Report

Possession of this report, or a copy of it, does not carry with it the right of publication except for the party to whom it is addressed. Without the written consent of the market analyst, this report may not be used for any purpose by any person other than the party to whom it is addressed. In any event, this report may be used only with properly written qualification and only in its entirety for its stated purpose.

Soil and Geological Studies

No detailed soil studies or geological studies or reports were made available to the market analyst. Assumptions employed in this report regarding soils and geologic qualities of the subject property have been provided to the client. However, such assumptions are not conclusive and the market analyst assumes no responsibility for soils or geologic conditions discovered to be different from the conditions assumed unless otherwise stated in this report.

Earthquakes and Seismic Hazards

The property which is the subject of this market analysis is within a geographic area prone to earthquakes and seismic disturbances. Except as specifically indicated in the report, no seismic or geologic studies have been provided to the market analyst concerning the geologic and/or seismic condition of the subject property. The market analyst assumes no responsibility for the possible effect on the subject property of seismic activity and/or earthquakes.

Testimony or Court Attendance

Testimony or attendance in court or at any other hearing is not required by reason of rendering this market analysis, unless such arrangements are made a reasonable time in advance of said hearing. Separate arrangements would need to be made concerning compensation for the market analyst's time to prepare for and attend any such hearing.

Maps and Exhibits

Maps, plat and exhibits included in this report are for illustration only as an aid in visualizing matters discussed within the report. They should not be considered as surveys, or relied upon for any other purpose, nor should they be removed from, reproduced, or used apart from the report.

Environmental and Other Regulations

The property is evaluated assuming it to be in full compliance with all applicable federal, state and local environmental regulations and laws, unless otherwise stated.

Required Permits and Other Governmental Authority

Unless otherwise stated, the property evaluated is assumed to have all required licenses, permits, certificates, consents or other legislative and/or administrative authority from any local, state or national government or private entity or organization that have been or can be obtained or renewed for any use on which the evaluation analysis contained in this report is based upon.

Liability of Market Analyst

The liability of Empire Economics, the market analyst responsible for this report, is limited to the client only and to the fee actually received by the market analyst. Further, there is no accountability, obligation or liability to any third party. If this report is placed in the hands of anyone other than the client, the client shall make such party aware of all limiting conditions and assumptions of the assignment and related discussion. The market analyst is in no way to be responsible for any costs incurred to discover or correct any deficiencies or any type present in the property--physical, financial, and/or legal.

Presence and Impact of Hazardous Material

Unless otherwise stated in the report, the market analyst did not become aware of the presence of any hazardous material or substance during the market analyst's general inspection of the subject property. However, the market analyst is not qualified to investigate or test for the presence of such materials or substances. The presence of such materials or substances may adversely affect the evaluation of the subject property. The evaluation in this report is predicated on the assumption that no such material or substance is present on or in the subject property or in such proximity thereto that it would cause a change in the evaluation analysis. The market analyst assumes no responsibility for the presence of any such substance or material on or in the subject property, nor for any expertise or engineering knowledge required to discover the presence of such substance or material. Unless otherwise stated, this report assumes that subject property is in compliance with all federal, state and local environmental laws, regulations and rules.

Structural Deficiencies of Improvements

The market analyst has not performed a thorough inspection of the subject property, and except as noted in this report has not found obvious evidence of structural deficiencies in any improvements located on the subject property. Consequently, the market analyst assumes no responsibility for hidden defects or nonconformity with specific governmental requirements, such as fire, building and safety, earthquake or occupancy codes, unless inspections by qualified independent professions or governmental agencies were provided to the market analyst. Further, the market analyst is not a licensed engineer or architect and assumes no responsibility for structural deficiencies not apparent to the market analyst at the time of their inspection.

Presence of Asbestos

The market analyst is not aware of the existence of asbestos in any existing improvements on the subject property. However, the market analyst is not trained to discover the presence of asbestos and assumes no responsibility should asbestos be found in or at the subject property. For the purposes of this report, the market analyst assumes the subject property is free of asbestos and the subject property meets all federal, state and local laws regarding asbestos abatement.

Acreage of Property

The acreage has been abstracted from the documents relating to the District which is assumed to be accurate. If the Assessor's map or legal description is subsequently found to be in error, we reserve the right to amend the market analysis.

Designated Economic Scenario

The Market Absorption Study focuses upon the expected absorption schedules for the products in CFD No. 2004-3 IA No. 2 according to the designated economic scenario. Specifically, this scenario represents the economic and real estate conditions for the Market Region and also the Market Area during the foreseeable future according to the most probable conditions, and this is regarded as being appropriate for the Bond Financing. However, the economic and market conditions which actually materialize on a year by year basis may differ from those presented according to the designated economic scenario, as a result of exogenous factors which are difficult to forecast/quantify. Accordingly, the designated scenario should be utilized as an economic framework for evaluating the marketing prospects of the properties within CFD No. 2004-3 IA No. 2 rather than a "literal" representation of what is expected to occur on a year/year basis during the foreseeable future.

Provision of the Infrastructure; Role of Coordinator

The Market Absorption Study assumes that the governmental agencies that supply public facilities and services, including water, provide these in a timely manner so that the proposed projects in CFD No. 2004-3 IA No. 2 can respond to the expected market demand for their products. Otherwise, if the required infrastructure is not available in a timely manner, then the absorption of the projects could be adversely impacted.

Developer/Builder Responsiveness to Market Conditions

The Market Absorption Study assumes that the developer/builder in CFD No. 2004-3 IA No. 2 responds to the market conditions with products that are competitively priced and have the features/amenities that are desired by the purchasers. Specifically, most of the homes have not yet entered the marketplace, and so the specific characteristics of their product types cannot be identified until they actually offer products on the marketplace. Consequently, to the extent that future products/projects have prices/features that differ from the competitive market standards, then their absorption schedules would need to be modified from those presented according to the designated economic scenario.

Financial Strength of the Project Developer/Builder

The Market Absorption Study assumes that Project developer/builder in CFD No. 2004-3 IA No. 2 (and also their lenders) have sufficient financial strength to adequately fund including paying their Special Taxes/Assessments, and that they have sufficient financial reserves which could be utilized to supplement their cash flow positions, in the event that adverse economic or market conditions occur.

Market Absorption Study Timeliness of Results

The Market Absorption Study performs a comprehensive analysis of the relevant land-use, economic and residential market conditions that are expected to influence the marketing success of the properties/projects in CFD No. 2004-3 IA No. 2. Nevertheless, the Study should be updated on a six-month basis, or even sooner, should these land-use and/or economic market conditions change significantly.

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APPENDIX D
APPRAISAL REPORT

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APPRAISAL REPORT
CITY OF LAKE ELSINORE
COMMUNITY FACILITIES DISTRICT NO. 2004-3
IMPROVEMENT AREA 2
ROSETTA CANYON

Prepared for:

CITY OF LAKE ELSINORE
130 S. Main Street
Lake Elsinore, CA 92530

James B. Harris, MAI
Berri J. Cannon Harris
Harris Realty Appraisal
5100 Birch Street, Suite 200
Newport Beach, CA 92660

August 2006

Harris Realty Appraisal

5100 Birch Street, Suite 200
Newport Beach, California 92660
949-851-1227 FAX 949-851-2055
www.harris-appraisal.com

August 10, 2006

Mr. Matt N. Pressey
Director of Administrative Services
CITY OF LAKE ELSINORE
130 S. Main Street
Lake Elsinore, CA 92530

Re: **CFD No. 2004-3**
Improvement Area 2
Rosetta Canyon

Dear Mr. Pressey:

In response to your authorization, we have prepared a self-contained appraisal report that addresses all of the taxable property within the boundaries of Improvement Area 2 of Community Facilities District No. 2004-3 (CFD No. 2004-3). This appraisal includes an estimate of Market Value of the land and site improvements and dwelling units subject to special tax. This land is under the ownership of one developer/merchant builder, Centex Homes. The land ranges from blue-top lots to near finished lots with site improvements currently under construction. In addition, 62 production homes are in various stages of unit construction. There are 384 near finished lots and 57 lots in a blue-top condition or blue-top with some addition site work. There are a total of 503 lots in Improvement Area 2.

According to the specific guidelines of the California Debt and Investment Advisory Commission (CDIAC), each ownership is valued in bulk, representing a discounted value to that ownership as of the date of value.

Based on the investigation and analyses undertaken, our experience as real estate appraisers and subject to all the premises, assumptions and limiting conditions set forth in this report, the following opinion of Market Value is formed as of August 5, 2006.

SEVENTY-EIGHT MILLION FIVE HUNDRED THOUSAND DOLLARS

\$78,500,000

The estimated value assumes bond proceeds of about \$19,300,000 for eligible facilities and/or fees, as described in the Community Facilities Report, are available at the time of sale.

Mr. Matt N. Pressey
August 10, 2006
Page Two

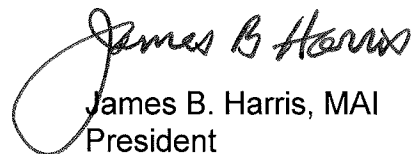
The self-contained report that follows sets forth the results of the data and analyses upon which our opinion of value is, in part, predicated. This report has been prepared for the City of Lake Elsinore for use in the issuance of Community Facilities District No. 2004-3, Improvement Area 2 bonds. The intended users of this report are the City of Lake Elsinore, its underwriter, legal counsel, consultants, and potential bond investors. This appraisal has been prepared in accordance with and is subject to the requirements of the Appraisal Standards for land secured financing as published by the California Debt and Investment Advisory Commission; the *Uniform Standards of Professional Appraisal Practice* (USPAP) of the Appraisal Foundation; and the *Code of Professional Ethics* and the *Standards of Professional Appraisal Practice* of the Appraisal Institute.

We meet the requirements of the Competency Provision of the *Uniform Standards of Professional Appraisal Practice*. A statement of our qualifications appears in the Addenda.

Respectfully submitted,



Berri J. Cannon Harris
Vice President
AG009147



James B. Harris, MAI
President
AG001846

City of Lake Elsinore
Community Facilities District No 2004-3
Improvement Area 2

Rosetta Canyon

Interstate 15 Frwy

HWY 78

Wasson Canyon Rd

Boundaries Approximate

9901_080506



SUMMARY OF FACTS AND CONCLUSIONS

EFFECTIVE DATE OF APPRAISAL	August 5, 2006
DATE OF REPORT	August 10, 2006
INTEREST APPRAISED	Fee Simple Estate, subject to special tax liens
LEGAL DESCRIPTION	Lots 1 through 213, Tract No. 25477 Lots 1 through 290, Tract No. 25476
OWNERSHIP	Centex Homes
SITE CONDITION	<p>Tract No. 25477 has 213 lots in one subdivision. There are 62 production homes in various stages of construction from framing to wrapped. There are 151 near finished lots, some with foundations under construction. Dry utilities and interior street paving of the near finished lots should be completed by the end of August 2006.</p> <p>Tract No. 25476 has 290 lots in three subdivisions. There are 233 lots in a near finished condition. There are 57 lots in a blue-top plus wet utilities condition. Dry utilities and interior street paving should be completed by September 2006.</p>
HIGHEST AND BEST USE	Continued residential development within the Rosetta Canyon Master Planned Community. Development of four subdivisions with floor plans ranging from 1,979 square feet to 4,063 square feet on 5,000 square foot minimum lots.
VALUATION CONCLUSION	<p>\$78,500,000 MARKET VALUE</p> <p><i>The estimated value assumes bond proceeds of about \$19,300,000 for eligible facilities and/or fees, as described in the Community Facilities Report, are available at the time of sale.</i></p>

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INTRODUCTION

Purpose of the Report

The purpose of this appraisal is to estimate the Market Value for the *fee simple estate, subject to special tax liens* for all the taxable property within Improvement Area 2 of Community Facilities District No. 2004-3, located in the City of Lake Elsinore. The purpose of this appraisal is to estimate the "As Is" Market Value of the land and improvements under the ownership of the developer/merchant builder.

The opinions set forth are subject to the assumptions and limiting conditions set forth in this appraisal, and the appraisal guidelines as set forth by the City of Lake Elsinore.

Function of the Report and Intended Use

It is our understanding that this appraisal report is to be used for Community Facilities District bond purposes only. The subject properties are described more particularly within this report. The bonds are issued pursuant to the Mello-Roos Community Facilities District Act of 1982, as amended. The maximum authorized bond indebtedness for the CFD is \$28,000,000.

Client and Intended Users of the Report

This report was prepared for our client, the City of Lake Elsinore. The intended users of the report include the City, its legal counsel, underwriter, consultants, and potential bond purchasers.

Scope of the Assignment

According to the CDIAAC guidelines, the total value conclusion includes the "As Is" estimate of Market Value for the property under the ownership of the developer/merchant builder within the boundaries of Improvement Area 2 of CFD No. 2004-3. This is a fully documented self-contained appraisal report. Any lands designated for park, open space or civic uses within these tracts not subject to special tax are not included in this assignment.

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The residential land is valued in its "As Is" condition as of the date of value. Site development for the subject property ranges from blue-top lots with some additional site work to near finished lot condition with three model homes under construction and 62 production homes in various stages of unit construction. The production homes under construction are in Tract No. 25477. The following exhibit illustrates the condition and construction in each of the four subdivisions within the subject property.

CFD NO. 2004-3 Improvement Area 2 Current Condition August 5, 2006					
Construction Stages	Fox & Jacobs @ Rosetta Canyon Tr 25477	Fox & Jacobs Santa Rosa Tr 25476	Centex Homes Caraway II Tr 25476	Centex Homes Augusta II Tr 25476	Total
Model Units ⁽¹⁾					
Completed	--	--	--	--	0
Under Construction	--	0	--	--	0
Production Units					
Completed	0	0	0	0	0
Under Construction	62	0	0	0	62
Finished lots ⁽²⁾	151	98	66	69	384
Blue Top Lots	--	--	12	45	57
Total	213	98	78	114	503
⁽¹⁾ Models for Fox & Jacobs @ Rosetta Canyon, Caraway II and Augusta II are located in Improvement Area 1					
⁽²⁾ Includes finished lots, lots in a near finished condition and lots with foundations under construction.					

We have analyzed the subject property based upon the proposed uses and our opinion of its highest and best use. We have searched for sales of residential land to estimate the value of the property.

The following paragraphs summarize the process of collecting, confirming and reporting of data used in the analysis.

1. Gathered and analyzed demographic data from sources including the California Department of Finance (population data), Employment Development Department of the State of California (employment data), City of Lake Elsinore (zoning information, building permit

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trends), Lake Elsinore Chamber of Commerce (local demographic trends), Hanley Wood Market Intelligence (housing sales, inventory levels, and absorption), and sales personnel of comparable projects (market trends of individual home sales). Subject information was gathered from the developer/builder and their consultants.

2. Inspected the subject's neighborhood and reviewed proposed product and similar products for consideration of Highest and Best Use of the proposed lots.
3. Gathered and analyzed comparable merchant builder land sales within the Lake Elsinore market areas, and residential detached unit sales, within the subject's primary and secondary market areas. Data was gathered from sources including, Comps.com, brokers, appraisers, builders active in the area and developers within the Southern California area. Where feasible, data were confirmed with both the buyer and seller. The data gathered are presented on summary data sheets within this report.

Date of Value and Report

The opinion of Market Value expressed in this report is stated as of August 5, 2006. The date of the appraisal report is August 10, 2005.

Date of Inspection

The subject property was inspected on several occasions, with the most recent on August 5, 2006.

Property Rights Appraised

The property rights appraised are those of the *fee simple estate subject to special tax liens* of the real estate described herein.

Property Identification

The subject property consists of land under site and unit construction in the City of Lake Elsinore. According to the City's Special Tax Consultant, Improvement Area 2 of CFD No. 2004-3 is identified as Lots 1 through 290 of Tract No. 25476. Tract No, 25476 consists of APN's 349-430-006, 349-430-014, 349-430-016, 349-420-001, 349-420-022, and 349-430-019. Lots 1 through 213 of Tract No. 25477 consist of APN's 349-400-020, 349-400-021, 349-410-001, 349-410-002, 349-410-003, 349-410-004, and

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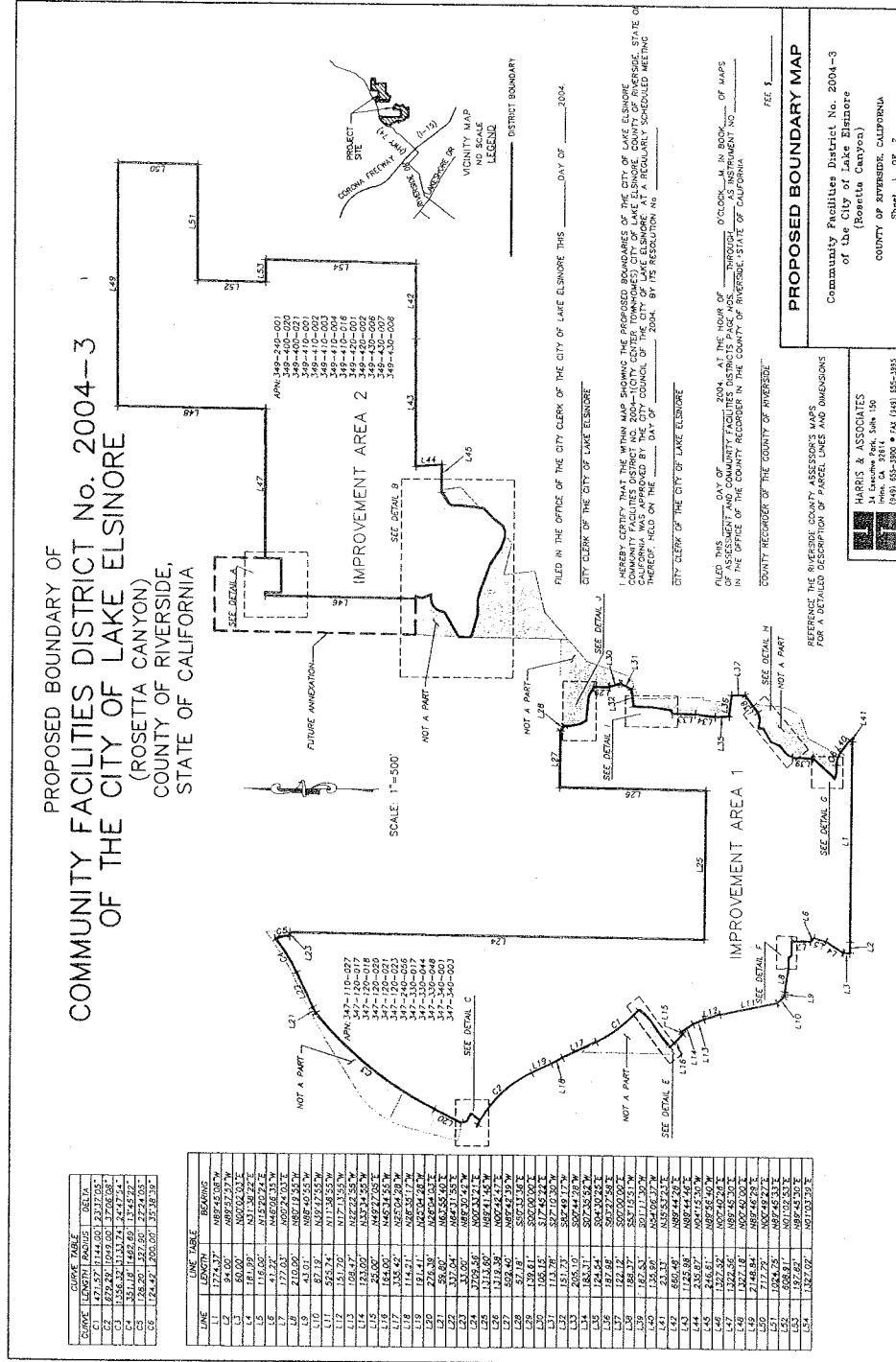
349-400-016. The subject property is a part of the Ramsgate Specific Plan. The Specific Plan in its entirety consists of 1,239 gross acres. CFD No. 2004-3, Improvement Area 2 contains 84.15 taxable acres proposed for 503 dwelling units. Improvement Area 2 has 4 subdivisions which are currently in development, ranging from blue-top lot condition to near finished lot condition with production homes under construction.

Legal Description and Ownership

The table below identifies lot and tract, and ownership, APNs and assessor's parcel size for the subject property. Tract Map No. 25476 contains 101.76 gross acres and Tract Map No. 25477 contains 51.55 gross acres. According to the recorded tract maps, Improvement Area 2 of CFD No. 2004-3 contains 153.31 gross acres.

CFD NO. 2004-3 Improvement Area 2 Ownership and Legal Description				
Ownership	Legal Description	APN	TRA	Lot Size (Acres)
Centex Homes	Lots 1 through 290	349-430-006-3	5025	8.94
	Tract No. 25476	349-430-014-0	5008	16.60
		349-430-016-2	5008	1.74
		349-420-001-7	5008	6.83
		349-420-022-8	5008	11.19
		349-430-019-5	5008	55.58
		Subtotal Tract 25476		
Centex Homes	Lots 1 through 213	349-400-020-2	5025	14.69
	Tract No. 25477	349-400-021-3	5025	5.00
		349-410-001-6	5025	3.43
		349-410-002-7	5025	4.51
		349-410-003-8	5025	2.36
		349-410-004-9	5025	2.06
		349-410-016-0	5025	16.47
Subtotal Tract 25477			48.52	
Total CFD No. 2004-3, Improvement Area 2				149.40

CFD No. 2004-3 – Improvement Area 2



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Property History

Centex Homes purchased the entire District, Improvement Area 1 and Improvement Area 2 on November 5, 2003 (Document No. 2003-878254) for \$30,000,000. Centex Homes purchased the raw land from White Rock Acquisition Co. L.P. A review of the public records indicated two sequential transactions on January 28, 1998. The first sale was from Ramsgate, L. P to Santa Barbara Properties, Inc. for \$3,358,182, according to the documentary transfer stamps on the deed. The subsequent sale was from Santa Barbara Properties, Inc. to White Rock Acquisition Co. L.P. The terms of the sale were not disclosed.

Definitions

Market Value¹

The most probable price in terms of money which a property should bring in a competitive and open market under all conditions requisite to a fair sale, the buyer and seller, each acting prudently, knowledgeably and assuming the price is not affected by undue stimulus. Implicit in this definition is the consummation of a sale as of a specified date and the passing of title from seller to buyer under conditions whereby:

- (a) Buyer and seller are typically motivated.
- (b) Both parties are well informed or well advised, and each acting in what he considers his own best interest.
- (c) A reasonable time is allowed for exposure in the open market.
- (d) Payment is made in terms of cash in U.S. dollars or in terms of financial arrangements comparable thereto.
- (e) The price represents the normal consideration for the property sold unaffected by special or creative financing or sales concessions granted by anyone associated with the sale.

Fee Simple Estate²

Absolute ownership unencumbered by any other interest or estate subject only to the four powers of government.

¹ Part 563, subsection 563.17-1a(b)(2), Subchapter D, Chapter V, Title 12, Code of Federal Regulations.

² *The Dictionary of Real Estate Appraisal*, Third Edition, published by The Appraisal Institute, 1993, Page 140

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Fee Simple Estate Subject to Special Tax and Special Assessment Liens Empirical evidence (and common sense) suggests that the selling prices of properties encumbered by such liens are discounted compared to properties free and clear of such liens. In new development projects, annual special tax and/or special assessment payments can be substantial, and prospective buyers take this added tax burden into account when formulating their bid prices. Taxes, including special taxes, are legally distinct from assessments.

The Market Value included herein, reflects the value potential buyers would consider given the special tax lien of Community Facilities District No. 2004-3, Improvement Area 2.

Retail Value

Retail value should be estimated for all fully improved and sold properties. Retail value is an estimate of what an end user would pay for a finished property under the conditions requisite to a fair sale.

Blue-Top Graded Parcel

Blue-top graded parcel includes streets cut and padded lots with utilities stubbed to the parcel and perimeter streets in.

Finished Site³

Land that is improved so that it is ready to be used for a specific purpose. (Improvements include padded lot, streets and utilities to the lot, and all fees required to issue a building permit paid.)

Mass-Graded Parcels

Mass-graded parcel with utilities stubbed to the site and perimeter streets in.

Assumptions and Limiting Conditions

The analyses and opinions set forth in this report are subject to the following assumptions and limiting conditions:

Standards Rule ("S.R.") 2-1(c) of the "Standards of Professional Appraisal Practice" of the Appraisal Institute requires the appraisers to "clearly and accurately disclose any extraordinary assumption or limiting condition that directly affects an appraisal analysis, opinion, or conclusion." In compliance with S.R. 2-1(c) and to assist

³ Ibid, Page 334

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the reader in interpreting the report, the following contingencies, assumptions and limiting conditions are set forth as follows:

Contingencies of the Appraisal

The appraisal is contingent upon the successful issuance and funding of bonds for Community Facilities District No. 2004-3, Improvement Area 2, through the City of Lake Elsinore. The special tax formula was prepared on behalf of the City of Lake Elsinore by Harris & Associates, Special Tax Consultant.

The Market Value estimate reported in this report reflects a portion of the funding for the infrastructure improvements and fees from the proceeds of Community Facilities District No. 2004-3, Improvement Area 2. The public improvements and fees subject to reimbursement include fire station, street improvements, water & sewer facilities and fees and City development impact fees. The total construction funds and fees with contingency subject to possible reimbursement are about \$19,300,000. If the CFD is not funded and/or the amount or timing of the reimbursements should change, the value opinion stated herein could change. Please refer to the Valuation section for further detail of the reimbursements and timeline for reimbursement.

The appraisers have been provided with overall site costs and costs to complete from Centex Homes. It is assumed that all conditions for site development as indicated in the Conditions of Approval are included in the infrastructure costs. *A specific assumption of this appraisal report is that the costs are accurate.*

The individual parcel sizes have been calculated by Hunsaker and Associates Irvine, Inc. Our value estimate is, in part, based on the accuracy of this information.

Assumptions and Limiting Conditions

No responsibility is assumed by your appraisers for matters that are legal in nature. No opinion of title is rendered, and the property is appraised as though free of all encumbrances and the title marketable. No survey of the boundaries of the property was undertaken by your appraisers. All areas and dimensions furnished to your appraisers are presumed to be correct.

The date of value for which the opinions of Market Value are expressed in this report is August 5, 2005. The dollar amount of this value opinion is based on the purchasing power of the United States dollar on that date.

Maps, plats, and exhibits included herein are for illustration only, as an aid for the reader in visualizing matters discussed within the report. They should not be considered as surveys or relied upon for any other purpose,

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nor should they be removed from, reproduced, or used apart from this report.

Oil, gas, mineral rights and subsurface rights were not considered in making this appraisal unless otherwise stated and are not a part of the appraisal, if any exist.

A Preliminary Geotechnical report and Rough Grading Plan Review were provided for the appraiser's review. The appraisers have reviewed portions of the "Rough Grading Plan Review, Tracts 25477 and 25476, Rosetta Canyon," dated October 20, 2004. The report was prepared by Albus-Keefe & Associates Inc. The reports conclude in Section 5.1, page 9, under *Feasibility of Proposed Development*, "From a geotechnical point of view, the proposed site development is considered feasible provided the recommendations presented in this report are incorporated into the design and construction of the project." The report specifies issues identified by the study or previous studies as possibly affecting site development. Recommendations to mitigate these issues are presented in the text of the report. It is recommended that the client and any potential bond purchaser review all soils and geotechnical reports. Surrounding land has been improved with numerous dwellings. For purposes of this appraisal, the soil is assumed to be of adequate load-bearing capacity to support all uses considered under our conclusion of Highest and Best Use.

The appraisers have been provided with two preliminary title reports for Tract No. 25476 and Tract No. 25477. The preliminary reports are from Commerce Title Company, dated June 13, 2006. For purposes of this appraisal, we are not aware of any easements, encroachments or restrictions that would adversely impact the value of the subject properties.

Information contained in this report has been gathered from sources which are believed to be reliable, and, where feasible, has been verified. No responsibility is assumed for the accuracy of information supplied by others.

Since earthquakes are common in the area, no responsibility is assumed for their possible affect on individual properties, unless detailed geologic reports are made available.

The appraisers have inspected as far as possible by observation, the land; however, it was impossible to personally inspect conditions beneath the soil. Therefore, no representations are made as to these matters unless specifically considered in the report.

The appraisers assume no responsibility for economic or physical factors that may occur after the date of this appraisal. The appraisers, in rendering these opinions, assume no responsibility for subsequent changes in

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management, tax laws, environmental regulations, economic, or physical factors that may or may not affect said conclusions or opinions.

No engineering survey, legal, or engineering analysis has been made by us of this property. It is assumed that the legal description and area computations furnished are reasonably accurate. However, it is recommended that an analysis be made for exact verification through appropriate professionals before demising, hypothecating, purchasing or lending occurs.

Unless otherwise stated in this report, the existence of hazardous substances, including without limitation asbestos, polychlorinated biphenyls, petroleum leakage, or agricultural chemicals, which may or may not be present on the property, or other environmental conditions, were not called to the attention of nor did the appraisers become aware of such during the appraisers' inspection. The appraisers have no knowledge of the existence of such materials on or in the property unless otherwise stated. The appraisers, however, are not qualified to test for such substances or conditions.

The presence of such substances such as asbestos, urea formaldehyde, foam insulation, or other hazardous substances or environmental conditions may affect the value of the property. The value estimated herein is predicated on the assumption that there is no such condition on or in the property or in such proximity thereto that it would cause a loss in value. No responsibility is assumed for any such conditions, or for any expertise or engineering knowledge required to discover them. The client is urged to retain an expert in the field of environmental impacts upon real estate if so desired.

The cost and availability of financing help determine the demand for and supply of real estate and therefore affect real estate values and prices. The transaction price of one property may differ from that of an identical property because financing arrangements vary.

The distribution, if any, of the total valuation in this report between land and improvements applies only under the stated program of utilization. The separate allocations for land and improvements must not be used in conjunction with any other appraisal and are invalid if so used.

The forecasts of future events that influence the valuation process are predicated on the continuation of historic and current trends in the market.

The property appraised is assumed to be in full compliance with all applicable federal, state, and local environmental regulations and laws, and the property is in conformance with all applicable zoning and use ordinances/restrictions, unless otherwise stated.

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The *Americans with Disabilities Act* ("ADA") became effective January 26, 1992. We have not made a specific compliance survey and analysis of this property to determine whether or not it is in conformity with the various detailed requirements of the ADA. It is possible that a compliance survey of the property, together with a detailed analysis of the requirements of the ADA, could reveal that the property is not in compliance with one or more of the requirements of the Act. If so, this fact could have a negative effect on the value of the property. Since we have no direct evidence relating to this issue, we did not consider possible non-compliance with the requirements of the ADA in estimating the value of the property.

We shall not be required, by reason of this appraisal, to give testimony or to be in attendance in court or any governmental or other hearing with reference to the property without prior arrangements having first been made with the appraisers relative to such additional employment.

In the event the appraisers are subpoenaed for a deposition, judicial, or administrative proceeding, and are ordered to produce their appraisal report and files, the appraisers will immediately notify the client.

The appraisers will appear at the deposition, judicial, or administrative hearing with their appraisal report and files and will answer all questions unless the client provides the appraisers with legal counsel who then instructs them not to appear, instructs them not to produce certain documents, or instructs them not to answer certain questions. These instructions will be overridden by a court order which the appraisers will follow if legally required to do so. It shall be the responsibility of the client to obtain a protective order.

The appraisers have personally inspected the subject property; however, no opinion as to structural soundness of existing improvements or conformity to any applicable building code is made. The appraisers assume no responsibility for undisclosed structural deficiencies/conditions. No consideration has been given in this appraisal to personal property located on the premises; only the real estate has been considered unless otherwise specified.

James B. Harris is a Member, and Berri J. Cannon Harris is an Associate Member, of the Appraisal Institute. The Bylaws and Regulations of the Institute require each Member and Associates to control the uses and distribution of each appraisal report signed by such Member or Associates. Except as hereinafter provided, possession of this report, or a copy of it, does not carry with it the right of publication. It may not be used for any purpose by any person other than the party to whom it is addressed without the written consent of the appraisers and in any event only with properly written qualification and only in its entirety. **The City of Lake Elsinore, its underwriter and legal counsel may publish this report in the Official Statement for this Community Facilities District.**

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Neither all nor any part of the contents of this report (especially any conclusions as to value, the identity of the appraisers or the firm with which they are connected, or any reference to the Appraisal Institute or the MAI designation) shall be disseminated to the public through advertising media, public relations, news media or any other public means of communication without the prior consent and approval of the undersigned.

The acceptance of and/or use of this appraisal report by the client or any third party constitutes acceptance of the following conditions:

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AREA DESCRIPTION

The following section of this report will summarize the major demographic and economic characteristics such as population, employment, income and other pertinent characteristics for the Southern California region, Riverside County, City of Lake Elsinore and the subject market areas.

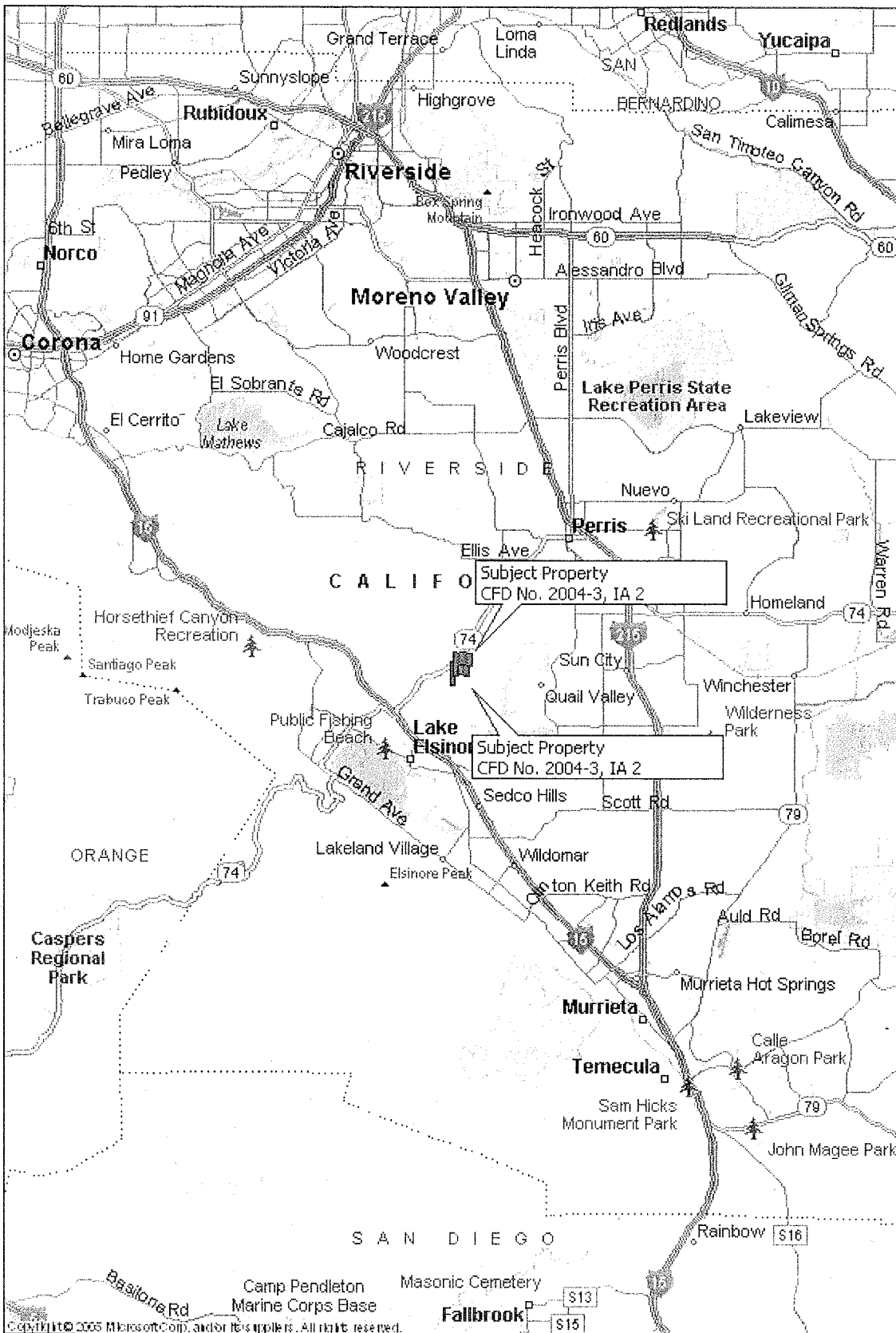
Southern California Regional Overview

The Southern California region, as defined in this report, encompasses six individual counties including Los Angeles, Orange, Riverside, San Bernardino, San Diego, and Ventura Counties. The Southern California region extends from the California-Mexico border on the south to the Tehachapi mountain range on the north and from the Pacific Ocean on the west to the California-Arizona border on the east. The region covers an estimated 38,242 square miles and embodies a diverse spectrum of climates, topography, and level of urban development. Please refer to the following page for a location map.

Population

The Southern California region has added about 7.7 million new residents since 1980 as indicated in the table shown on page 15. According to the California Department of Finance, the most recent data available indicate that as of January 2006, the regional population stood at over 21.1 million. If the region were an individual state, it would rank as one of the most populous in the nation.

Since 1981, annual population gains from natural increase and immigration have ranged from a low of 87,300 persons in 1995 up to 568,645 persons in 1989. These figures represent annual gains of 0.5% to 3.5%. During the past five years, the population of the six-county Southern California region grew by 1.2% to 2.0% per annum.



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As of January 2006 the population of the six-county area stood at 21,147,233 persons. Looking toward the future it is estimated that the region's population will continue to climb as new residents seek out the southern California area. During the economic downturn from 1992 through 1996, and continuing through 2006, the population growth rate declined compared to the growth experienced in the late 1980s.

Population Trends 1980-2006

Year	Population	Average Annual Change Number	Percent
1980	13,359,673	--	--
1981	13,571,785	212,112	1.6%
1982	13,868,390	296,605	2.2%
1983	14,179,920	311,530	2.2%
1984	14,483,010	303,090	2.1%
1985	14,795,200	312,190	2.2%
1986	15,189,600	394,400	2.7%
1987	15,613,100	423,500	2.8%
1988	16,027,400	414,300	2.7%
1989	16,460,900	433,500	2.7%
1990	17,029,545	568,645	3.5%
1991	17,232,000	202,455	1.2%
1992	17,539,200	307,200	1.8%
1993	17,746,100	206,900	1.2%
1994	17,862,000	115,900	0.7%
1995	17,949,300	87,300	0.5%
1996	18,041,500	92,200	0.5%
1997	18,223,500	182,000	1.0%
1998	18,467,800	244,300	1.3%
1999	18,750,300	282,500	1.5%
2000	19,187,478	437,178	2.3%
2001	19,522,459	334,981	1.7%
2002	19,919,857	397,398	2.0%
2003	20,299,133	379,276	1.9%
2004	20,629,260	330,127	1.6%
2005	20,902,628	273,368	1.3%
2006	21,147,233	244,605	1.2%

April 1, 1980, 1990, and 2000; all other years January 1
Source: California Department of Finance. 5/06

The future rate of growth will depend on a number of factors that may dramatically affect the region. Some of the major factors include availability of developable land, availability of water, national economic climate, and public policy toward growth and the assimilation of a large number of new foreign immigrants. The continued growth of the

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population within the region, even during periods of economic slow down provides a positive indicator as to the desirability of the Southern California region.

Employment

In conjunction with the population growth, a key indicator of the region's economic vitality is the trend in employment. The most common measure of employment growth is the change in non-agricultural wage and salary employment. The table below illustrates the non-agricultural wage and salary employment trends in Southern California.

Southern California Region Employment Trends 1983-2005

Year	Population	Average Annual Change	
		Number	Percent
1983	5,691,000	-	-
1984	5,960,100	269,100	4.7%
1985	6,198,400	238,300	4.0%
1986	6,384,500	186,100	3.0%
1987	6,664,000	279,500	4.4%
1988	6,903,800	239,800	3.6%
1989	7,096,000	192,200	2.8%
1990	7,288,100	192,100	2.7%
1991	7,104,000	-184,100	-2.5%
1992	6,900,700	-203,300	-2.9%
1993	6,798,100	-102,600	-1.5%
1994	6,833,900	35,800	0.5%
1995	6,957,800	123,900	1.8%
1996	7,084,100	126,300	1.8%
1997	7,300,900	216,800	3.1%
1998	7,546,800	245,900	3.4%
1999	7,767,800	221,000	2.9%
2000	7,985,900	218,100	2.8%
2001	8,082,300	96,400	1.2%
2002	8,073,100	-9,200	-0.1%
2003	8,102,100	29,000	0.4%
2004	8,224,600	122,500	1.5%
2005	8,362,000	137,400	1.7%

2005 Benchmark

Source: Employment Development Department 5/06

In the Southern California region, average annual non-agricultural employment has grown from 5,691,000 jobs in 1983, to a peak employment of 8,362,000 in 2005. Employment declined to 8,073,100 in 2002. This decline was mostly caused by a

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significant job decrease in Los Angeles County. In 2005, employment climbed to a new record level, 8,362,000. This was in spite of Los Angeles County only adding an additional 20,000+ jobs. This represents an increase of approximately 280,000 new jobs over the past five years.

As the economy entered into an economic recession during the latter part of 1990, employment growth began to slow. The average annual gain in 1990 was approximately 192,100 jobs or 2.7%. In 1992 when the full weight of the recession was felt, area employment suffered the highest annual decline in jobs registered in the last decade, losing nearly 204,000 jobs or a percentage decrease of 2.9%. This was followed by further employment declines of 102,600 jobs in 1993. It appears that by the middle of 1994, the economic recovery finally began to take hold in the Southern California region. In 1997, total non-agricultural employment stood at 7.3 million, finally exceeding the prior high in 1990. As of year-end 2002, employment was over 8.0 million. Forecasts prior to September 11, 2001, indicate that job growth would continue to be positive in 2001 and increase moderately over the next one to two years. However, with the terrorist attack on the United States and the conflict with Iraq, most economists are saying we were in a flat to slightly declining economy, during 2002 and first half of 2003, but that we began recovery during the second half of 2003. 2003 showed a small increase over the previous high mark in 2001. Employment gains have recovered in 2005 with an additional 137,400 new jobs or a 1.7% increase.

Employment among the individual industry categories reflects some fundamental regional changes in the economy during the past decade. The level of mining activity in Southern California continues to steadily decline as reflected in the consistent decrease in mining employment. Construction employment, as of 1989, was at a high level in response to the level of construction activity that had occurred in the region during the past five years. During the period from 1991 through 1994, construction employment declined in response to decreased residential and commercial construction activity. From 1994 through 2005, as the economy rebounded, residential construction increased bringing back more than the construction jobs lost during the recession.

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Total manufacturing employment in the region has exhibited little gain from the levels recorded in 1980. Due to the high labor, land, and capital costs in most of the Southern California region, some manufacturing firms have expanded or relocated their manufacturing operations outside of the area.

The Southern California economy, which historically depended heavily on aerospace and defense related employment, has been dealt a double blow. First the reduction of the space program and reduced defense spending affected manufacturers and suppliers. Secondly, the closure of several military bases had a ripple effect throughout the local economy. Areas heavily dependent on military spending will be impacted as the units are deployed abroad.

The finance, insurance, and real estate ("FIRE") employment category grew rapidly as the economy recovered from the 1981-1982 national recession. As the economy entered a new recessionary cycle, the FIRE employment sector exhibited little growth from 1991 through 1995. Some of the manufacturing and aerospace jobs permanently displaced from the economy were slowly being replaced with administrative, marketing and research employment. It is reasonable to assume that similar stagnant growth in this area will be experienced during the current economy.

The employment group that has contributed most to the employment growth in the region is the service sector. Since 1980, the majority of all new jobs have been created in the service category. The service sector was the leader in new job growth during the years that followed the economic recovery from the 1990 recession.

Government employment tends to mirror the growth of the population that it services. It is expected that government employment will grow at a rate similar to the area population. The future employment growth in the Southern California region is expected to continue but at a level moderately lower than recent years. Factors that will affect employment growth include the direction of the national economy, wage levels, housing prices, and population trends. Given the national disaster of September 11, 2001, government should not experience layoffs; on the contrary, growth particularly in the

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defense sector should occur. However, the California deficit has negatively impacted both state and local government employment.

Riverside County

Riverside County consists of 24 individual cities and numerous unincorporated communities. Riverside County is typically grouped with adjacent San Bernardino County to form the Riverside-San Bernardino Metropolitan Statistical Area ("MSA"). This area is commonly called the Inland Empire. Riverside County is bounded by Orange County to the west, San Bernardino to the north, the state of Arizona to the east, and San Diego County to the south.

The major urbanized areas are located in the western portion of the County. The major incorporated cities include the cities of Riverside, Corona, and Moreno Valley. These areas were the most active areas for new growth during the mid 1980's until the recession took hold during 1990. The area which encompasses Lake Elsinore, Murrieta, Menifee Valley and Temecula has also experienced rapid growth since the mid 1980's. The areas that have experienced the most active growth during the 1980s also suffered the most during the lengthy recession. However, since 1996, residential activity has increased due to downsizing of product with more affordable pricing, and the general improvement in the regional economy.

Population

Riverside County has almost tripled its population, adding approximately 1,290,000 new residents since 1980 as illustrated in the following table. As of the 2000 Census, the countywide population stood at 1,545,387 residents. The 2006 estimate by the State of California indicates that the County had 1,953,330 residents on January 1, 2006. Annual population gains, from natural increase and immigration, have ranged from 44,799 persons in 2001 up to 81,303 persons in 2004. From 1991 to 1996, the rate of growth in population declined moderately each year. Recent gains of 44,799 to 81,303 persons represent annual changes of 2.9% to 4.7%.

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The future rate of growth within the County will depend on a number of factors. Some of the major factors include availability of developable land, availability of water, national and regional economic climate and public policy toward growth.

The areas within the County that will continue to experience the largest share of the new population growth will be the Corona-Riverside area and the area between Lake Elsinore, Sun City and Temecula, which includes the Menifee Valley.

Riverside County Population Trends 1980-2006

Year	Population	Average Annual Change Number	Percent
1980	663,199	--	--
1985	815,100	30,380	4.6%
1990	1,170,413	71,063	8.7%
1991	1,221,300	50,887	4.3%
1992	1,275,500	54,200	4.4%
1993	1,312,300	36,800	2.9%
1994	1,340,200	27,900	2.1%
1995	1,365,500	25,300	1.9%
1996	1,391,800	26,300	1.9%
1997	1,420,600	28,800	2.1%
1998	1,451,400	30,800	2.2%
1999	1,490,500	39,100	2.7%
2000	1,545,387	54,887	3.7%
2001	1,590,186	44,799	2.9%
2002	1,653,847	63,661	4.0%
2003	1,726,321	72,474	4.4%
2004	1,807,624	81,303	4.7%
2005	1,888,311	80,687	4.5%
2006	1,953,330	65,019	3.4%

April 1, 1980, 1990, and 2000, all other years January 1
Source: California Department of Finance. 5/06

Employment

Employment data for Riverside County are compiled for the entire MSA, which includes San Bernardino and Riverside Counties. These counties have a diverse economy, with manufacturing, construction and tourism being the major industry groups. In conjunction with the rapid population growth experienced in the past two decades, the employment base has continued to grow and diversify. The Inland Empire's

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unemployment rate is moderately above the Southern California average and similar to the State. The higher unemployment rate is due to the seasonal nature of agricultural employment in the area. The following exhibit illustrates the area's unemployment compared to California as of May 2006. Unemployment rates have declined 64% from the recession high of 12.2% in 1993.

	<u>Labor Force</u>	<u>Unemployment</u>
California	17,716,300	4.6%
Inland Empire	1,713,000	4.3%

The most common measure of employment growth is the increase in nonagricultural employment. Nonagricultural employment is outlined in the following exhibit. During the 1980's the Inland Empire's employment base expanded rapidly as the area moved away from its military and government oriented employment base to a more fully diversified economy.

Nonagricultural employment has grown from an annual average of 443,100 jobs in 1983 to 1,235,400 jobs in 2005. This represents an increase of over 792,000 new jobs created in San Bernardino and Riverside Counties during the past 22 years. Job gains peaked in 1990 with 71,000± new jobs. Since 2000, job increases have ranged from 34,100 new jobs to a record increase of 59,300± new jobs in 2004. The percentage increases have ranged from 3.2% to 5.3%. The table on the following page illustrates the annual employment trends from 1983 through 2005. In May 2006, the non-agricultural employment had increased to 1,246,200, a 2.1% increase from May 2005.

Employment among the individual industry categories reflects changes in the Inland Empire economy during the past decade. Construction employment gains generally mirror the regional economy. In response to the high level of construction activity that occurred in the County during the period from 1984 to 1989, construction employment reached nearly three times the level recorded in 1982. From 1992 through 1995, construction employment declined in response to decreased building activity. The 2005 levels were more than double the 1993 low.

**San Bernardino-Riverside MSA
Employment Trends
1983-2005**

<u>Year</u>	<u>Population</u>	<u>Average Annual Change</u>	
		<u>Number</u>	<u>Percent</u>
1983	443,100	—	—
1984	473,600	30,500	6.9%
1985	514,100	40,500	8.6%
1986	551,400	37,300	7.3%
1987	588,700	37,300	6.8%
1988	625,100	36,400	6.2%
1989	668,200	43,100	6.9%
1990	735,200	67,000	10.0%
1991	741,600	6,400	0.9%
1992	751,500	9,900	1.3%
1993	755,800	4,300	0.6%
1994	772,800	17,000	2.2%
1995	801,700	28,900	3.7%
1996	824,800	23,100	2.9%
1997	863,200	38,400	4.7%
1998	903,800	40,600	4.7%
1999	960,300	56,500	6.3%
2000	1,010,100	49,800	5.2%
2001	1,050,700	40,600	4.0%
2002	1,084,800	34,100	3.2%
2003	1,119,400	34,600	3.2%
2004	1,178,700	59,300	5.3%
2005	1,235,400	56,700	4.8%

2005 Benchmark

Source: Employment Development Department 5/06

The number of manufacturing jobs in the Inland Empire has increased over 45% from the levels recorded in 1991. However, manufacturing jobs declined 5.5% from the 2000 high of 120,000 jobs to 113,400 jobs by 2003, but increased back up to 120,200 in 2005. Due to the high labor and capital costs in Los Angeles and Orange Counties, manufacturing firms have expanded or relocated some of their manufacturing operations to Riverside and San Bernardino counties to take advantage of the labor force and lower land costs.

Transportation and public utilities employment tend to mirror population growth. In the Inland Empire the finance, insurance and real estate ("FIRE") category is still a small segment of the employment picture.

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A significant number of the new jobs created in the last 15 years have been created in the service sector. The service sector will continue to play a major role in employment growth during the next few years. Government employment is a major employment sector in the Inland Empire due to the rapid growth.

The future employment growth in the Inland Empire is expected to continue as more firms relocate to the area to take advantage of lower land prices and the abundant labor pool. Factors that will affect employment growth include the direction of the state and national economy, and consumer confidence. Due to the terrorist attack on September 11, 2001 and the Iraq conflict, consumer confidence was negatively impacted. Most economists report that we were in a flat economy in 2002 and the first half of 2003, but that we began recovery during the second half of 2003. The recovery continued into 2006.

Income

The average household income in Riverside County is estimated to be \$64,601. The median household income stands at \$49,128. These figures are moderately below the Southern California region average. The lower income level is due to the lower wages in agriculture, manufacturing, service and government employment. The household income distribution for Riverside County is illustrated in the following table.

County of Riverside Household Income Distribution 2006

<u>Income Range</u>	<u>Households</u>	<u>Percent 1/</u>
Less than \$15,000	79,214	12.60%
\$15,000 - \$24,999	72,692	11.56%
\$25,000 - \$34,999	70,749	11.25%
\$35,000 - \$49,999	97,465	15.50%
\$50,000 - \$74,999	121,784	19.36%
\$75,000 - \$99,999	77,760	12.30%
\$100,000 - \$149,999	74,100	11.78%
\$150,000 or more	35,544	5.66%
Total	628,908	100.0%
Median Household Income		\$49,128
Average Household Income		\$64,601

1/ Percent of total distribution
Source: Claritas 6/06

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Retail Sales

Retail demand continues to be fueled by the growth in population as outlined previously. For Riverside County, taxable retail sales have increased from \$3.9 billion in 1985 to over \$7.1 billion by 1994 and to over \$18.7 billion by 2004. During the past seven years, annual changes have ranged from an increase of \$768 million in 1998 to an increase of \$2.7 billion in 2004, as shown on the next table. Data for 2005 are not available as of the date of this report.

The increases in retail sales are due to the exceptionally high County population growth rates experienced during the period from 1983 through 1990. During the period from 1991 through 1993, retail sales were stagnant due to the economic recession. From 1994, and continuing through 2004, there was a significant rebound in retail sales. Official state reports for 2005 will not be released until later this year. In the future, retail sales growth should mirror the population growth in the County.

**Riverside County
Retail Sales Trends ¹
1985-2004**

<u>Year</u>	<u>Taxable²</u>	<u>Average Annual Change</u>	
	<u>Retail Sales</u>	<u>Number</u>	<u>Percent</u>
1985	\$3,974,400	\$319,632	8.7%
1986	\$4,338,628	\$364,228	9.2%
1987	\$4,868,644	\$530,016	12.2%
1988	\$5,486,787	\$618,143	12.7%
1989	\$6,257,222	\$770,435	14.0%
1990	\$6,596,974	\$339,752	5.4%
1991	\$6,389,890	-\$207,084	-3.1%
1992	\$6,684,107	\$294,217	4.6%
1993	\$6,716,783	\$32,676	0.5%
1994	\$7,131,216	\$414,433	6.2%
1995	\$7,435,414	\$304,198	4.3%
1996	\$8,003,061	\$567,647	7.6%
1997	\$8,508,010	\$504,949	6.3%
1998	\$9,276,448	\$768,438	9.0%
1999	\$10,685,724	\$1,409,276	15.2%
2000	\$12,190,474	\$1,504,750	14.1%
2001	\$13,173,281	\$982,807	8.1%
2002	\$14,250,753	\$1,077,472	8.2%
2003	\$16,030,952	\$1,780,199	12.5%
2004	\$18,715,949	\$2,684,997	16.7%

1/ Taxable Retail Sales Total (not adjusted for inflation)

2/ 000s

Source: State Board of Equalization 5/06

Transportation

Riverside County is served by a major airport, Ontario International, located in adjoining San Bernardino County. Several major airlines have flights into Ontario, while international flights can be booked out of Los Angeles International Airport.

A network of freeways links most urbanized areas of the County. The major north-south arterials are the Corona (15) and Escondido (215) Freeways. The Pomona Freeway (60) provides east-west access to the Los Angeles area and the desert areas of Riverside County. The Riverside Freeway (91) provides access to Orange and Los Angeles Counties.

Environmental Concerns

The Endangered Species Act of 1973 precludes any activity that constitutes a taking of a federally listed endangered species except by permit. Numerous areas within

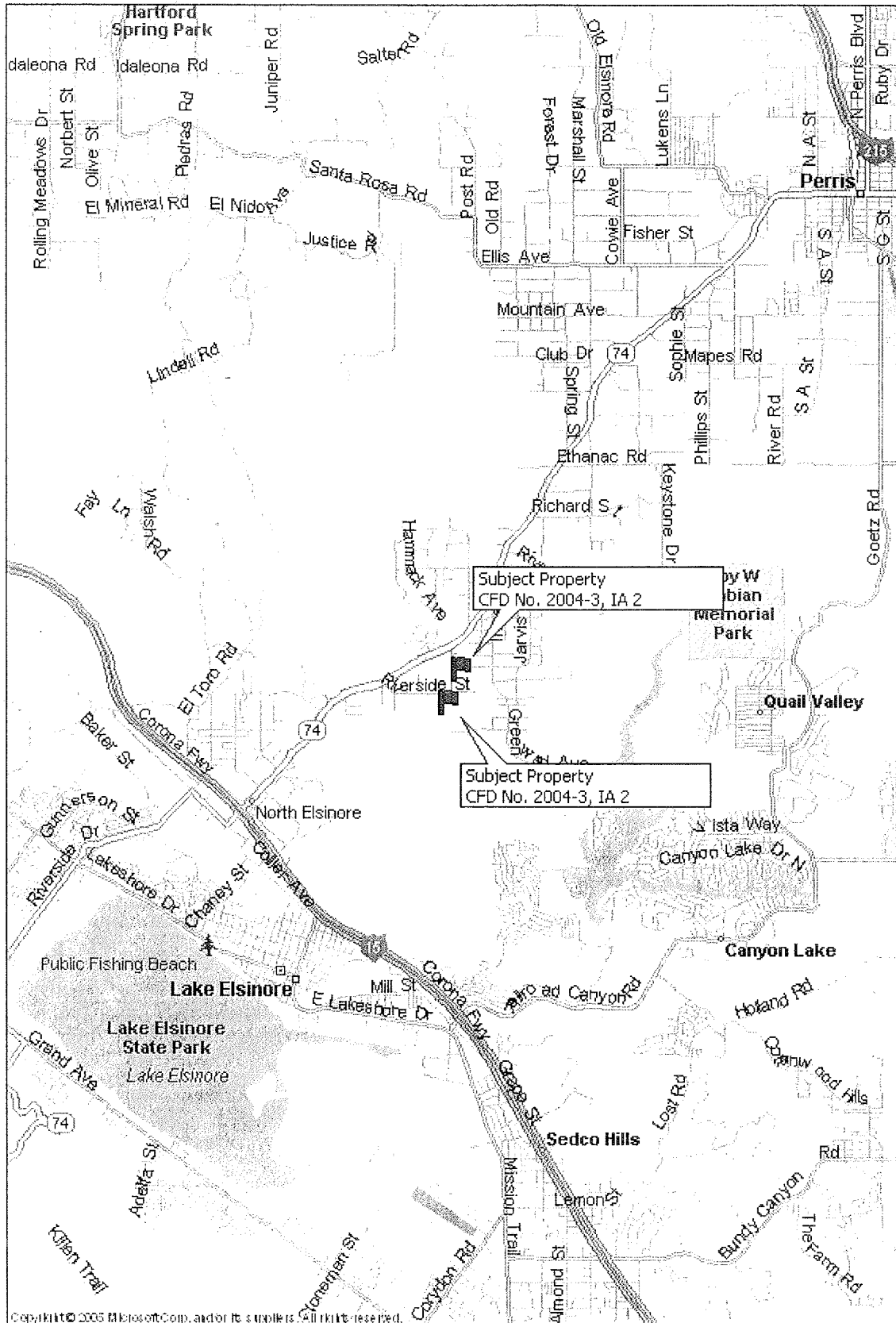
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Riverside County have been identified as containing potential habitat of the Stephen's Kangaroo Rat, a listed species. The evidence of habitation by this rat has resulted in delays or substantial revisions of proposed developments. The California Department of Fish and Game is currently reviewing the status of additional wildlife for possible inclusion on a list of endangered or threatened species. A Multiple Species Habitat Conservation Plan (MSHCP) was approved by the County Board of Supervisors on June 17, 2003. The MSHCP is a comprehensive, multi-jurisdictional effort that includes the County and 14 cities. This plan focuses on the conservation of 146 species. The MSHCP consists of a reserve system of approximately 500,000 acres of which 347,000 acres are within public ownership and approximately 153,000 acres are in private ownership. The purchase of the privately owned lands will be funded by an adopted fee. A MSHCP fee of \$1,651 per dwelling unit is imposed for housing built in the MSHCP area.

In summary, the region exhibited very strong population and employment growth during the 1980 to 1989 period. The recession of the early 1990s had significantly slowed population growth and resulted in overall job losses from 1990 to 1995. Over the past seven years, as the economy recovered, population and employment growth have been stronger than during the prior growth years of the 1980s. The long-term outlook for the region remains positive as the elements of abundant affordable land and labor still exist. Future growth will, however, continue to be affected by the trends in the overall economy. Riverside County's economic environment should follow a path similar to that of the other Southern California counties.

Lake Elsinore

The City of Lake Elsinore is located in the southwestern portion of Riverside County. The City of Lake Elsinore and the surrounding area to the southeast, most notably Murrieta and Temecula, experienced rapid development beginning in the early 1980's and late 1990's and was one of the fastest growing areas in Southern California. It has become a sprawling suburban bedroom community for Orange and Los Angeles counties. The area has attempted to retain the semi-rural, western atmosphere of the early residents. Please refer to the next page for a neighborhood map.



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During the past five to ten years, the City of Lake Elsinore has begun to add new residential and retail developments. Most of the newer retail commercial development has occurred adjacent to the Corona Freeway (I-15), which bisects the northern and eastern sections of the City of Lake Elsinore. The major community commercial retail development is concentrated near the intersection of the Corona Freeway (I-15) and Railroad Canyon Road, primarily along Mission Trails. A major retail development is under construction at the I-15 and State Highway 74.

There is older commercial development located along Riverside Drive between Lakeshore Drive and Grand Avenue.

The newest residential developments are located in the northeastern area of the City, in the vicinity of the Tuscany Hills, Rosetta Canyon and Canyon Hills developments. In addition, there is some residential development on the northwest side of Lake Elsinore, along Lake Avenue. Most of the new home construction is single-family detached product in master planned communities. The homes offered range from entry-level homes in moderate price ranges to larger move-up homes. As the market changed during the past recession, the residential sector moved to the smaller homes with affordable prices. But recent development has shown an increase in dwelling size and sales prices.

Population

Although the City of Lake Elsinore, incorporated in 1888, is old by southern California standards, it was not until the 1980's that the City experienced significant population growth. The City of Lake Elsinore has experienced moderate population increases during recent years as illustrated on the following exhibit. Since 1980, annual population gains of 400 persons to a peak of 2,700 persons have been recorded. The current population of the City of Lake Elsinore, as of January 2006, is estimated to be 40,985 persons. Over the last three years, the City has averaged a 6.9% annual growth in population.

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Although the City of Lake Elsinore is predominantly residential in nature, there are 1,200 acres zoned for industrial use. The improved industrial development is limited with most of the industrial land remaining vacant.

**City of Lake Elsinore
Population Trends
1980-2006**

Year	Population	Average Annual Change	
		Number	Percent
1980	5,982	--	--
1990	18,316	1,233	20.6%
1991	19,050	734	4.0%
1992	21,600	2,550	13.4%
1993	22,000	400	1.9%
1994	23,100	1,100	5.0%
1995	23,850	750	3.2%
1996	24,700	850	3.6%
1997	25,750	1,050	4.3%
1998	26,450	700	2.7%
1999	27,950	1,500	5.7%
2000	28,930	980	3.5%
2001	30,039	1,109	3.8%
2002	31,243	1,204	4.0%
2003	33,460	2,217	7.1%
2004	35,983	2,523	7.5%
2005	38,289	2,306	6.4%
2006	40,985	2,696	7.0%

April 1, 1980, 1990, and 2000, all other years January 1
Source: California Department of Finance. 5/06

Employment in the immediate Lake Elsinore area is limited. The major employers in the area are as follows:

<u>Manufacturing</u>	<u>Employment</u>	<u>Product</u>
Labeda Wheels	150	Racing Skates
Pacific Clay	130	Building Products
Wieland Precision, Inc.	112	Tool & Dye

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<u>Non-manufacturing</u>	<u>Employment</u>	<u>Product</u>
Lake Elsinore USD	1,681	School
Lake Elsinore Outlet Center	1,169	Outlet Mall
Wal-Mart	400	Retail
Lake Elsinore Storm	250	Baseball
Lake Elsinore Casino	200	Resort/Casino
Albertsons	150	Supermarket
Vons	145	Supermarket
Stater Bros.	131	Supermarket

Most of the residents in Lake Elsinore work in areas outside of the City. Many residents drive considerable distances to work in San Diego, Los Angeles and Orange counties.

The housing market in Lake Elsinore is typically single-family residences. New homes range from relatively entry-level homes of 2,000± square feet on 5,000 square foot lots up to larger move-up homes on 7,200 square foot lots. The majority of the homes range in size from 2,000 to 3,000 square feet and are located in larger subdivision tracts or master planned communities on typical lot sizes of 5,000 to 7,200 square feet.

In view of Lake Elsinore's growing economy and population, only shortages of public services or a prolonged national building slump are likely to keep the City from reaching full development over time.

Based on the past and expected future economic and population growth of the Lake Elsinore area, the Lake Elsinore area is considered to have average to good future growth potential.

Immediate Neighborhood

The subject property is located in the north central portion of the City of Lake Elsinore. The District is in the Ramsgate Specific Plan Community approximately 1½ miles east of the I-15 Freeway south of Highway 74. The newer homes in this area are part of the existing Rosetta Canyon master planned community. The community has

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been under construction for approximately one to two years. The homes are a mix of one and two story construction, of average quality in good condition.

The first phase of the Rosetta Canyon Planned community, CFD No. 2004-3, Improvement Area 1, is nearing build out. There are 528 residential units in the first phase. The subdivisions include Fox & Jacobs @ Rosetta Canyon with 254 homes, Caraway with 80 homes, Augusta with 114 homes and Solana with 80 homes. These subdivisions are nearing sell out. The Fox and Jacobs @ Rosetta Canyon, Caraway and Augusta residential-products are being carried over for development in Improvement Area 2.

Conclusion

Lake Elsinore and the surrounding area has been experiencing rapid population growth during the past few years. New residents are being attracted to the area because of the affordable housing in comparison to the coastal regions of Los Angeles, San Diego and Orange counties. The subject's neighborhood is experiencing new construction of single-family developments that conform to the existing neighborhoods. The demand for continued development supports the build-out of the subject property.

The economy has experienced economic growth beginning in the third quarter of 2003, due largely to increased consumer and business spending. The anticipated continued strength should bring renewed job growth. Inflation is reported to remain low, which should keep mortgage rates from rising too steeply while the economy gains strength. The Inland Empire's housing boom has shown minimal signs of slowing. Builders in Riverside County increased demand for new housing permits and pulled 34,226 residential permits during 2004 and 34,330 residential permits in 2005.

The Riverside County area saw an increase of 9.4% in the median home price from a year ago. The median home price in Riverside County was \$422,000 in June 2006. San Bernardino's median home price was \$367,000. Home prices continue to increase, although the percentage increase is declining on a monthly basis. The subject's

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market area has continued to experience moderate to average demand for detached single-family homes. However, over each of the last eight months, the number of home sales has declined from the previous year. As long as the economy continues to grow, employment opportunities improve closer to the subject area, and the cities close to the more urbanized areas become even more expensive areas to live and operate a business in, the Lake Elsinore area and the District are anticipated to continue to experience moderate growth.

SITE ANALYSIS

General

The subject property of this appraisal is identified as CFD No. 2004-3, Improvement Area 2. The subject is proposed for 503 residential units in Tract Nos. 25477 (213 homes in 1 subdivision) and 25476 (290 homes in 3 subdivisions). In Tract No. 25477 there are 62 production units in various stages of unit construction from framing to wrapped in the Fox & Jacobs subdivision. The remaining 151 lots range from blue-top with wet utilities, to finished lot condition. The western section within Tract No. 25477 is finished lots with sewer and water complete and dry utilities complete. The streets are paved. There are a number of lots with dwelling foundation work under way. The eastern section within Tract No. 25477 has nearly finished lots with sewer and water completed, and dry utilities and street paving expected to be completed in August 2006.

In Tract No. 25476, 290 lots range from finished lots with some dwelling foundation work under construction to blue-top with sewer and water completed. Dry utilities and street paving should be completed by September 2006.

It should be noted that the only model units proposed for Improvement Area 2 are the three model units for the Santa Rosa subdivision. The other three subdivisions, Fox & Jacobs (Tract No. 25477) and Caraway II and Augusta II (Tract No. 25476) are nearly identical to the products constructed in Improvement Area 1. The homes of the Fox & Jacobs and Augusta II subdivisions are being marketed from the existing model complexes in Improvement Area I. A new model complex for the Caraway II homes is currently under construction in Improvement Area I across the street from the Augusta model complex. CFD No. 2004-3 is a portion of the Ramsgate Specific Plan. Please refer to page 5 for a map of the District.

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Location

The subject property is located in the City of Lake Elsinore in the southwestern portion of the County of Riverside. The District is within the Ramsgate Specific Plan and is located approximately 1½ miles east of the Interstate 15 Freeway and south of Highway 74. The major streets bisecting Tract No. 25477 is Steele Valley Road (Wasson Canyon Road), and the southern boundary of Tract No. 25477 and northern boundary of Tract No. 25476 is Riverside Street.

Current Site Condition

Improvement Area 2 of CFD No. 2004-3 is well under way with site construction. Tract No. 25477 has 33 production homes in various stages of construction from framing to wrapped. The balance of the lots is in a near finished condition. Tract No. 25476 ranges from a blue-top plus wet utility condition to a near finished condition. Dry utilities and street paving are underway and should be completed by September 2006. In the valuation section of this report, each lot condition is identified on the valuation exhibits.

CFD NO. 2004-3 Improvement Area 2 Current Condition August 5, 2006					
Construction Stages	Fox & Jacobs @ Rosetta Canyon Tr 25477	Fox & Jacobs Santa Rosa Tr 25476	Centex Homes Caraway II Tr 25476	Centex Homes Augusta II Tr 25476	Total
Model Units ⁽¹⁾					
Completed	--	--	--	--	0
Under Construction	--	0	--	--	0
Production Units					
Completed	0	0	0	0	0
Under Construction	62	0	0	0	62
Finished lots ⁽²⁾	151	98	66	69	384
Blue Top Lots	--	--	12	45	57
Total	213	98	78	114	503
⁽¹⁾ Models for Fox & Jacobs @ Rosetta Canyon, Caraway II and Augusta II are located in Improvement Area 1 ⁽²⁾ Includes finished lots, lots in a near finished condition and lots with foundations under construction.					

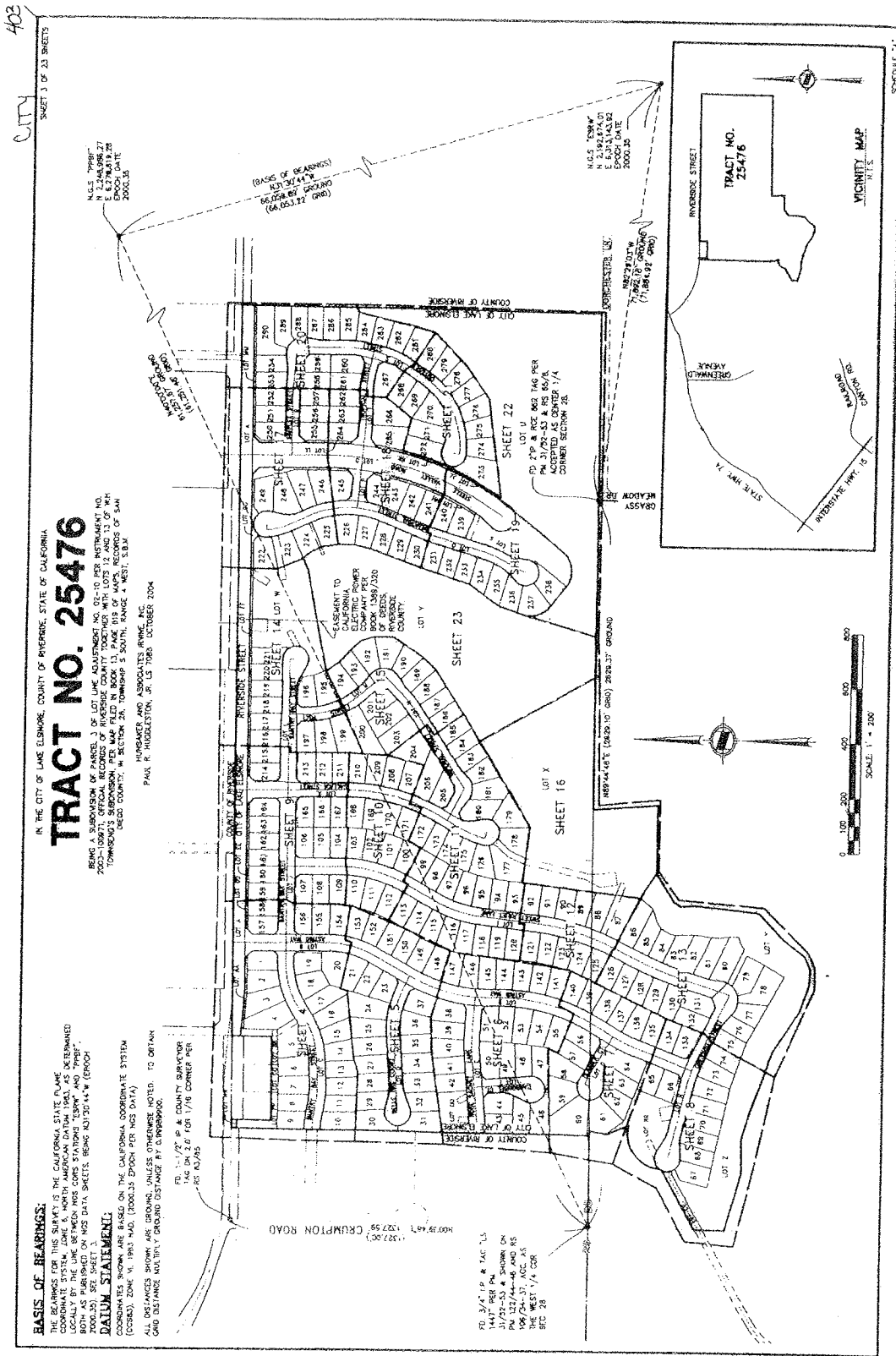
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Size and Shape

The overall shape of CFD No. 2004-3, Improvement Area 2 is irregular and contains 153.31 gross acres, according to the recorded tract maps. CFD No. 2004-3, Improvement Area 2 has been subdivided into two tract maps. Please refer to the following table, which summarizes the tracts. The following two pages show a copy of the tract maps.

CFD NO. 2004-3 Improvement Area 2				
Legal Description & Lots				
Ownership	Legal Description	Lots	Lot Size (Acres)	
Centex Homes	Lots 1 through 290 Tract No. 25476	290	101.76	
Centex Homes	Lots 1 through 213 Tract No. 25477	213	51.55	
Total CFD No. 2004-3, Improvement Area 2		503	153.31	

Final Tract No. 25476



IN THE CITY OF LAKE ELSOM, COUNTY OF RIVERSIDE, STATE OF CALIFORNIA
TRACT NO. 25476
BEING A SUBDIVISION OF PARCELS 3 OF LOT LINE NO. 10000-33
RECORDS OF SAN DIEGO COUNTY
RECORDS OF SAN DIEGO COUNTY
PAUL R. HUNTERMAN AND ASSOCIATES INC. RIVERSIDE, CALIFORNIA
OCTOBER 2004

BASIS OF BEARINGS:
THE BEARINGS AND DISTANCES ARE BASED ON THE NATIONAL GEODETIC SYSTEM (NAD 83) LOCAL TO THE AREA AND ARE REFERENCED TO THE LINE BETWEEN NEOS CORNER STATIONS 'TSPY' AND 'TPST', BOTH AS PUBLISHED ON NOS DATA SHEETS, BEING N37°30'14"W (ERROK).
DATUM STATEMENT:
COORDINATES WERE OBTAINED FROM THE NATIONAL GEODETIC SYSTEM (NAD 83), DATE: 10/13/04. EPOCH PER NOS DATA.
ALL DISTANCES WERE MEASURED ALONG THE GROUND SURFACE. DISTANCES WERE OBTAINED BY DISTANCE MEASUREMENT.
EAS. 3/4" 1/2" & COUNTY SURVEYOR PER 1/16 CORNER PER 85 AS/AS

Final Tract No. 25477

388
15
A Jy
SHEET 3 OF 12 SHEETS

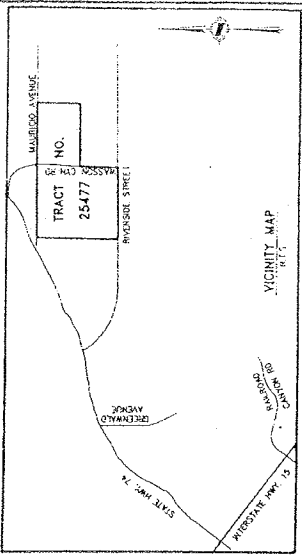
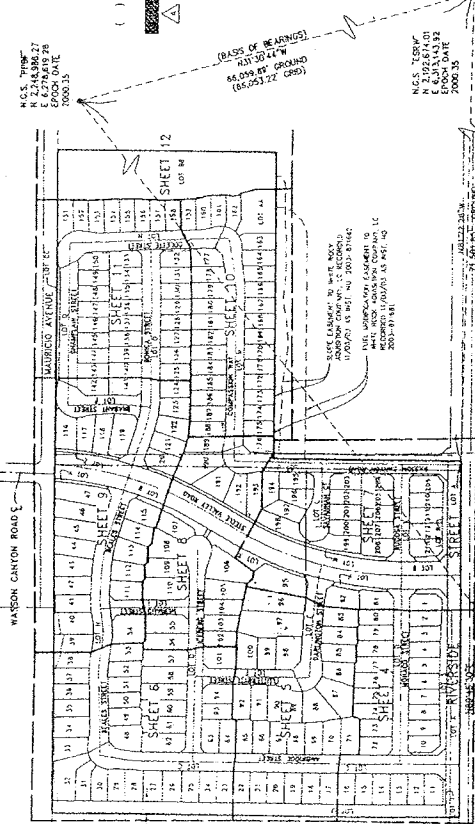
TRACT NO. 25477

IN THE CITY OF LAKE ELSWORTH, COUNTY OF RIVERSIDE, STATE OF CALIFORNIA

BEING A SUBDIVISION OF PARCELS 1 THROUGH 4, INCLUSIVE, AND LOTS A THROUGH D, INCLUSIVE, OF PARCEL MAP 12744, AS SHOWN ON PAGE 33, PAGE 35 OF PARCEL MAPS, RECORDS OF RIVERSIDE COUNTY TOGETHER WITH LOTS A AND B, PARCELS 1 AND 2, AND LOTS C AND D, PARCELS 3 AND 4, MAP NO. 11, PAGE 818 OF MAPS, RECORDS OF SAN DIEGO COUNTY, IN SECTION 28, TOWNSHIP 3 SOUTH, RANGE 4 WEST, S.B. 14.

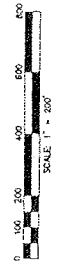
PREPARED AND ASSOCIATES, INC., AND
PAUL R. HINDLESTON, A.L.S. 7083, NOVEMBER 2000

SURVEYOR'S NOTES:
• INDICATES FOUND MONUMENT AS NOTED.
C INDICATES SET 1" UP AND TAG "S.S. 2005", FLUSH SET LEAD AND TAG "S.S. 2005", AT ALL REAR LOT CORNERS, UNLESS OTHERWISE NOTED.
SIDE LOT LINES PROJECTED AND FOR L.C.S. AND H.C.S. PROJECTED PERPENDICULAR OR RADIAL FROM CENTERLINE, UNLESS OTHERWISE NOTED.
TRACT NO. 25477 CONTAINS 54.59 ACRES, GROSS.
TRACT NO. 25477 CONTAINS 313 LOTS, LETTERED LOTS "A" THROUGH "D" AND LOTS "1" THROUGH "12" FOR STAKE AND LANDSCAPE MAINTENANCE PURPOSES, AND LETTERED LOTS "A", "B", AND "C" FOR OTHER STAKE PURPOSES.
DRAINAGE DRAINAGE SHALL BE KEPT FREE OF OBSTRUCTIONS AND OBSTRUCTIONS UNLESS OTHERWISE NOTED.
INDICATES RESTRICTED USE AREA (RIGHT DISTANCE PURPOSES).
INDICATES (RESERVED FOR LANDSCAPE MAINTENANCE PURPOSES), RESERVED AREA.
BASIS OF BEARINGS:
BEARINGS AND DISTANCES OF ALL LINES ARE BASED ON THE CALIFORNIA COORDINATE SYSTEM (CCS), ZONE 10N, NORTH AMERICAN DATUM 1983, AND TYPICALLY LOCAL BY THE LINE BETWEEN MGS STATIONS "TSK" AND "TYP".
2000-35
COORDINATES SHOWN ARE BASED ON THE CALIFORNIA COORDINATE SYSTEM (CCS), ZONE 10N, 1983 M.D. (2000.35 EPOCH PER M.S. D.14).
ALL DISTANCES SHOWN ARE GROUND, UNLESS OTHERWISE NOTED TO BE HORIZONTAL DISTANCE, MULTIPLE GROUND DISTANCE BY 0.99987500.



ENVIRONMENTAL CONSTRAINT NOTE:
ENVIRONMENTAL CONSTRAINT SHEET APPLICABLE TO THIS MAP IS BY REFERENCE TO THE CITY SURVEY, CITY OF LAKE ELSWORTH, THIS AFFECTS ALL LOTS.

SHEET INDEX MAP AND CONTROL SURVEY CONTROL DIAGRAM



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Soils and Geology

For CFD No. 2004-3 Improvement Area 2, one geotechnical report, *Rough Grading Plan Review*, was provided for review. The report was prepared by Albus-Keefe & Associates, Inc. (Geotechnical Consultants) dated October 20, 2004 for Centex Homes. The report covers Tract Nos. 25476 and 25477. The conclusion reached was that from a geotechnical point of view, the proposed site development was considered feasible provided recommendations presented in their report were incorporated into the design and construction of the project.

The appraisers assume that the soil conditions allow all of the proposed development as discussed in the Highest and Best Use section of this report and as proposed by the developer/builder.

Topography and Drainage

The topography within Improvement Area 2 is generally rolling terrain. Surface runoff is generally directed in all directions from the high points and hilltops via sheet flow to drainage swales or narrow ravines. Overall, regional drainage across the site is directed to the south and southwest towards Wasson Canyon.

Zoning

The District is zoned SP, Specific Plan, by the City of Lake Elsinore. This zone allows for a variety of compatible uses that comprise a master planned community. According to the Ramsgate Specific Plan, Third Revision, the entire planned community allows up to 3,330 dwelling units. Tract No. 25476, within Planning Area 3, is zoned for medium density residential development. Tract No. 25477, within Planning Area 4, is also zoned for medium density residential development. The minimum lot size is 5,000 square feet. Final Tract Map No. 25476 recorded on May 19, 2006 as Document No. 2006-0365293 and is proposed for 290 detached dwellings. Final Tract Map No. 25477 recorded on March 1, 2006, as Document No. 2006-0148370 and is proposed for 213 detached dwellings.

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As proposed, the subject project appears to be a legally conforming use. The subject property is in conformance with all zoning requirements, and is assumed to be in conformance with all governmental regulations. It is assumed at all the conditions of approval as outlined in *Conditions of Approval for Residential Project No. R2005-22-Centex Homes "Fox & Jacobs" @ Rosetta Canyon, Tract No. 25477*, dated February 7, 2006; *Conditions of Approval for Residential Project No. R2005-21-Centex Homes "Augusta & Caraway" @ Rosetta Canyon, Tract No. 25476*, dated March 13, 2006; and *Conditions of Approval for Residential Project No. R2006-05-Centex Homes "Santa Rosa" @ Rosetta Canyon, Tract No. 25476*, will be met by the developer.

Access and Circulation

The City of Lake Elsinore is served by Interstate 15 which links the City with the major freeway network serving the region. I-15 travels from the Mexican border north through Riverside and San Bernardino counties, Las Vegas and Salt Lake City, connecting with several east/west freeways. Full freeway interchange facilities are located approximately 1½ miles west of the subject property at State Highway 74. State Highway 74 generally serves as the main access to the planned community of Rosetta Canyon. Highway 74 is generally north of Tract No. 25477. Tract No. 25477 will be accessed via Wasson Canyon Road which becomes Steele Valley Road. Steel Valley Road bisects the Fox and Jacobs @ Rosetta Canyon II subdivision. The interior subdivision streets west of Steele Valley Road have the interior streets paved, while the eastern half should have street improvements completed in August 2006.

Tract No. 25476 is generally located south of Riverside Street and can be accessed via Wasson Canyon Road which becomes Steele Valley Road. Riverside Street has not been paved as of the date of value. The interior subdivision streets of Tract No. 25476 are unpaved. Interior street improvements should be completed in September 2006.

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Easements

The appraisers have been provided with two preliminary title reports for the two tracts in Improvement Area 2 of CFD No. 2004-3. The reports were prepared by Commerce Title Company, dated June 13, 2006 for Tract No. 25476 (order number 399641) and June 13, 2006 for Tract No. 25477 (order number 399642). Copies of the title reports are retained in the appraisers' work files.

There did not appear to be any easements, restrictions or conditions that would adversely impact the value of the subject property. It is a specific assumption of this appraisal that easements and encumbrances affecting the property are not detrimental to value.

Utilities

The subject property is served by the following companies/agencies:

Electricity	Southern California Edison
Water	Elsinore Valley Municipal Water District
Gas	Southern California Gas Company
Sewer	Elsinore Valley Municipal Water District
Telephone	Verizon

Earthquake, Flood Hazards, and Nuisances

The subject property is shown on the Riverside County National Flood Insurance Map Panel No. 060636-2054F, dated August 18, 2003. According to the flood insurance rate map for the City of Lake Elsinore, the subject property is not located in a HUD flood hazard area. The subject is within Zone X, outside the 500-year flood area.

According to the California Division of Mines and Geology, the subject property is not located in a seismic study zone; however, earthquakes impact all of Southern California. There are several faults in the vicinity of the subject. They consist of the Glen Ivy Fault, Elsinore Fault, Willard Fault and the Wildomar Fault. Other active faults are the San Jacinto (23 miles from the subject) and the San Andreas (30 miles from the subject).

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Toxic Hazards

A toxic hazard report was not provided to the appraiser. There are no toxic hazards known to the appraiser on the parcels.

Environmental Issues

The subject site is not classified as property with historical, archaeological, or scientific value and to the best of our knowledge, is not considered wetlands.

The property owner has provided a Phase 1 Environmental Site Assessment Report prepared by Environmental Advisors and Engineers, Inc. dated January 26, 1999 for the appraisers' review. The report covers the entire Ramsgate Specific Plan area which covers 1,185 acres, of which the subject is a part. The conclusion of the report revealed several environmental conditions in connection with the property. For each condition a recommendation was made to mitigate the issue. It is a specific assumption of this appraisal that all environmental concerns have been addressed and mitigated. Based on the current site condition and map status it appears that the site is suitable for development of the proposed uses.

Assessed Values, Taxes and Special Assessments

The 13 individual assessor parcels have property taxes as shown on the following table. Pursuant to Proposition 13, passed in California in 1978, current Assessed Values may or may not have any direct relationship to current Market Value. Real estate tax increases are limited according to Proposition 13 to a maximum of 2% per year plus bonds, if any. If the property is sold, real estate taxes are normally subject to modification to the then current Market Value.

Currently, there are special assessments for several agencies. In addition, there will be special taxes for CFD No. 2004-3, Improvement Area 2. The total tax rate is estimated not to exceed 2.0% of the base value of the dwelling. CFD No. 2004-3 will have special taxes ranging from \$2,460 to \$3,637 per unit depending on house size.

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The office of Harris & Associates estimates the Special Taxes on the undeveloped residential land within CFD No. 2004-3. The Special Taxes for the individual homes are also estimated. The estimated property values are based, in part, on the Special Taxes estimated for the ultimate homeowner.

CFD NO. 2004-3 Improvement Area 2 Assessed Values FY July 1, 2005 through June 30, 2006						
Ownership	Legal Description	APN	TRA	Lot Size (Acres)	Assessed Value	Property Tax (1)
Centex Homes	Lots 1 through 290, A through Z and	349-430-006-3	5025	8.94	\$ 770,100	\$ 9,136.10
	AA through SS of Tract No. 25476	349-430-014-0	5008	16.60	\$ 1,430,040	\$ 16,926.26
		349-430-016-2	5008	1.74	\$ 149,940	\$ 1,750.14
		349-420-001-7	5008	6.83	\$ 562,020	\$ 6,701.80
		349-420-022-8	5008	11.19	\$ 963,900	\$ 11,448.10
		349-430-019-5	5008	55.58	\$ 4,786,860	\$ 56,768.58
	Subtotal Tract 25476			100.88	\$ 8,662,860	\$ 102,730.98
Centex Homes	Lots 1 through 213, A through Z and	349-400-020-2	5025	14.69	\$ 1,264,800	\$ 17,085.70
	AA through CC of Tract No. 25477	349-400-021-3	5025	5.00	\$ 430,440	\$ 5,815.36
		349-410-001-6	5025	3.43	\$ 295,800	\$ 3,978.62
		349-410-002-7	5025	4.51	\$ 388,620	\$ 5,250.88
		349-410-003-8	5025	2.36	\$ 202,980	\$ 2,707.76
		349-410-004-9	5025	2.06	\$ 177,480	\$ 2,341.76
		349-410-016-0	5025	16.47	\$ 1,418,820	\$ 19,186.48
	Subtotal Tract 25477			48.52	\$ 4,178,940	\$ 56,366.56
	Total CFD No. 2004-3, Improvement Area 2			149.40	\$ 12,841,800	\$ 159,097.54
(1) Includes Property Tax and Special Assessments All Property taxes have been paid for 2005/2006						

The subject property falls within the taxing jurisdiction of the Riverside County Assessor's office. The published annual tax rate in these TRA's is 1.0052%. The overall effective tax rate for the proposed homes will be approximately 1.8% to 2.0% of our appraised base values. This tax burden is common for Riverside County where tax rates in new home communities typically range from 1.70% to 2.00%. A survey of the subject's market area revealed that special Assessment Districts or CFDs encumber most of the competing residential subdivisions. There does not appear to be a great deal of resistance to the special assessments that do not increase the overall tax rate significantly above 2.00% of Assessed Value.

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According to the County's web site, both installments of property taxes due by December 10, 2005 and April 10, 2006 for fiscal year 2005-06 are paid in full.

Site Improvements

As of the date of value, in Tract No. 25477, the western portion is improved to near finished lot condition with 62 production homes in various stages of construction. The eastern portion is in a near finished lot condition with, dry utilities and street paving currently underway and expected to be completed in August 2006. Tract No. 25476 is in a blue top lot plus wet utilities condition to near finished condition with dry utilities and street paving expected to be completed by September 2006. Three model homes are just beginning construction, but will be valued as finished lots.

The builder provided a summary site improvement budget, dated June 12, 2006 which totals \$54,018,370. The costs are reported to include the fee credits and/or reimbursements eligible from this CFD. A summary of the costs is included in the Addenda of this report. The costs are reported to bring the land from a raw condition to a physical and legal finished lot condition. According to the builder/developer's cost information and input from the developer's consultant, \$28,805,427 has been expended as of the date of value. Approximately \$25,212,943 remain in costs to bring the subject from its current "as is" condition to finished lot condition. Eligible reimbursement for infrastructure improvements and/or fee credits from Improvement Area 2 of CFD No. 2004-3 is about \$19,300,000.

It is a specific assumption of this appraisal, that the site costs provided by the developer/builder are all the site costs required to bring the land within CFD No. 2004-3, I.A. 2 from its "as is" condition to a finished lot ready to issue building permit condition for the 503 lots within Final Tract Map Nos. 25477 and 25476. This appraisal report and estimated value is based on the developer receiving reimbursements or fee credits of about \$19,300,000. If there is any change in the reimbursements, the value estimate would likely change.

IMPROVEMENT DESCRIPTION

General

The proposed residential developments known as Fox & Jacobs @ Rosetta Canyon II, Santa Rosa, Caraway II and Augusta II are located in the Rosetta Canyon portion of the City of Lake Elsinore. The subject Improvement Area of the CFD is proposed to include 503 detached residential units within 153± gross acres. The 503 units will be built on lots that generally range from a minimum size of 5,000 to 6,600 square feet. The following table summarizes the proposed floor plans within Improvement Area 2 of CFD No. 2004-3 as of the appraisal date. The base sales prices are those actually being achieved, as of the date of value. The Fox and Jacobs project is offering \$5,000 in incentives and the other three projects are in the initial stages of their marketing programs.

Rosetta Canyon Current Subdivisions, CFD 2004-3, Improvement Area 2 Subdivision Homes August 5, 2006								
<u>No. Project/Developer/Location</u>	<u>Total Units</u>	<u>Lot Size Min./Avg.</u>	<u>Model</u>	<u>Base Price</u>	<u>Size Sq. Ft.</u>	<u>\$/Sq. Ft.</u>	<u>Bdrm/ Bath</u>	<u>Stories Garage</u>
1 Fox & Jacobs @ Rosetta Canyon II Fox & Jacobs Homes Riverside St./Steel Valley Rd. (Rosetta Canyon), Lake Elsinore TBM 836 H-6	213	5,000 6,600	Plan 1	\$379,990	2,400	\$158.33	3/2.5	2/2
			Plan 2	\$386,990	2,710	\$142.80	4/2.5	2/2
			Plan 3	\$399,990	2,875	\$139.13	4+ / 2.5	2/3
			Plan 4	\$417,990	3,113	\$134.27	5/3	2/2+
			Plan 6	\$359,990	1,979	\$181.91	4/3	2/2
			Plan 7	\$386,990	2,613	\$148.10	5/3	2/2
			2 Santa Rosa @ Rosetta Canyon II Fox & Jacobs Homes Bantry Bay Street/Astird Way/Riverside St. (Rosetta Canyon), Lake Elsinore TBM 836 G&H-7	98	6,500 8,300	Plan 2266	\$376,990	2,266
Plan 2710	\$407,990	2,710				\$150.55	3/2.5	2/2
Plan 3206	\$429,990	3,206				\$134.12	5/3	2/3
Plan 3487	\$459,990	3,487				\$131.92	5+ / 3	2/3
3 Caraway II @ Rosetta Canyon Centex Gallica St./Riverside St. (Rosetta Canyon), Lake Elsinore TBM 836 G&H-7	78	6,600 7,300	Plan 1	\$414,990	2,648	\$156.72	4/2.5	2/3
			Plan 2	\$475,990	2,916	\$163.23	4+ / 3	2/3
			Plan 3	\$494,990	3,258	\$151.93	4+ / 3	2/3
4 Augusta II @ Rosetta Canyon Centex Gallica St./Riverside St./Steel Valley Rd. (Rosetta Canyon), Lake Elsinore TBM 836 G&H-7	114	6,600 7,800	Plan 3242	\$494,990	3,242	\$152.68	4+ / 3	2/3
			Plan 3613	\$536,990	3,613	\$148.63	5/4	2/3
			Plan 4063	\$553,990	4,063	\$136.35	5/4.5	2/3

Survey Date 7/7/06

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In the market area incentives in recent months have increased, with some projects offering up to \$10,000 in incentives, usually in the form of closing costs when the buyer uses the builder's preferred lender. Specifications have not been provided. We have been provided with brochures of the actively selling project and reduced floor plans for the proposed projects and they have been reviewed. The following is a list of some of the assumed general construction specifications for the detached single-family homes.

Construction

Units are of Class "D" construction; wood frame and stucco siding with several elevation choices.

Foundations

Foundations are poured concrete. Particle board over wood floor joists for the second floor.

Structural Frame

Consists of 2" x 4" and 2" x 6" wood framing.

Roofs

Roofs are of concrete tile.

Windows

White framed vinyl windows with low-e glass.

Floor Covering

Floor coverings are wall-to-wall carpet in all living areas. Entries are of ceramic tile and kitchen, bathrooms and laundry room are of vinyl.

Interior Finish

Custom trowelled ceiling and wall treatments.

Heating/HVAC

Energy efficient central air conditioning and gas forced air heating.

Kitchens

Kitchens will be equipped with maple cabinets and ceramic tile counter tops. Each kitchen will include a freestanding range and oven, 30" microwave, and dishwasher.

Bathrooms

Master bathrooms will have double sinks with cultured marble countertops and maple cabinets, separate fiberglass shower/tub. Secondary bathrooms will have cultured marble countertops, fiberglass combination tub/shower, and maple cabinets.

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Doors

Solid core 8 foot entry door. Garage doors are sectional steel roll-up.

Site Improvements

The production homes include concrete driveways and walkways to the front entry. Side and rear yard fencing are included. Front landscaping and irrigation system are included.

Options

Numerous options and upgrades will be available including flooring, cabinet, and countertop upgrades. Most options and upgrades, provided at competing similar quality developments, will be offered.

Conclusion of the Improvements

Based on the review of the product information and physical inspection of current models and similar products, we are of the opinion that the quality of the projects are average and will generally meet buyer expectations for the subject's marketplace.

Functional Utility

It is an assumption of this appraisal that all of the floor plans are functional, and competitive with current design standards.

Remaining Economic Life

The total/remaining economic life, according to the Marshall Valuation Service, is considered to be 50 years from date of completion.

Homeowners Association

The currently selling project, Fox & Jacobs at Rosetta Canyon has a Homeowner's Association. The monthly association dues are reported to be approximately \$130.00 per month at the beginning and will decrease to \$99.00 per month at build out. The appraisers have not been provided with information on the other three projects. For purposes of this appraisal it is assumed that the developments of Santa Rosa, Caraway II and Augusta II, will have similar Homeowners Associations and monthly dues.

HIGHEST AND BEST USE

The term *highest and best use* is an appraisal concept that has been defined as follows:

The reasonably probable and legal use of vacant land or an improved property, which is physically possible, appropriately supported, financially feasible, and that results in the highest value. The four criteria the highest and best use must meet are legal permissibility, physical possibility, financial feasibility, and maximum productivity.⁴

The determination of highest and best use, therefore, requires a separate analysis for the land as legally permitted, as if vacant. Next, the highest and best use of the property with its improvements must be analyzed to consider any deviation of the existing improvements from the ideal. "The highest and best use of both land as though vacant and property as improved must meet four criteria. The highest and best use must be: legally permissible, physically possible, financially feasible, and maximally productive. These criteria are often considered sequentially."⁵ The four criteria interact and, therefore, may also be considered in concert. A use may be financially feasible, but it is irrelevant if it is physically impossible or legally prohibited.

Legally Permissible Use

The legal factors affecting the site and its potential uses are often the most restrictive. These would typically be government regulations such as zoning and building codes.

CFD No. 2004-3 is located in the City of Lake Elsinore. The subject is zoned for residential development within the Specific Plan. This zone designation allows for detached single-family residential use with a minimum 5,000 square foot lot size. CFD No. 2004-3, Improvement Area 2 has two recorded final tract maps proposed for 213 and 290 dwelling units. All proposed developments are considered legal and conforming uses.

⁴ *The Dictionary of Real Estate Appraisal*, 4th Edition, Pub. by the Appraisal Institute, Chicago, IL., p. 135.

⁵ *The Appraisal of Real Estate*, 10th Edition, Pub. by the Appraisal Institute, Chicago, IL., p. 280.

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Physically Possible Use

Improvement Area 2 of CFD No. 2004-3 is irregular in shape and contains approximately 153± gross acres according to their tract maps. The sites have a sloping topography. The four residential developments are a natural extension of existing nearby residential developments, within the Ramsgate Planned Community.

Within Tract No. 25477 a portion of the land is improved to near finished lot condition. The western section of Tract No. 25477 is improved with paving, sewer, water, storm drains and dry utilities. The eastern section of Tract No. 25477 is improved with sewer, water and storm drains, with dry utilities and street paving to be completed in August 2006. In Tract No. 25476 three model homes are in the initial stages of construction. Tract No. 25476 is graded to blue-top lots with sewer and water installed to the majority of lots. Dry utilities and the balance of the wet utilities, plus street paving should be completed by September 2006. All normal utilities are available to serve the subject sites.

The property is generally bounded by residential development and undeveloped land. Access is considered to be good via Wassan Canyon off the 74 Highway, and the I-15 Freeway. This appraisal considers the benefits and/or improvements that are to be funded by CFD No. 2004-3, Improvement Area 2.

Based on the physical analysis, the subject property appears to be viable for numerous types of development based on its size and topography. However, the site's location and current site improvements would suggest the lands have a primary use of residential development.

Financial Feasibility and Market Conditions

The financial feasibility of the development of the subject property is based on its ability to generate sufficient income and value in excess of the costs to develop the property to its highest and best use. Please refer to the Valuation section of this report, which gives support to the financial feasibility of CFD No. 2004-3, Improvement Area 2.

General Market Conditions – Riverside County

The Inland Empire housing market has continued to increase in demand and price over the past several years. As in the past, the increased housing prices in Orange, San Diego and Los Angeles counties have encouraged buyers to look at alternative locations for homes. The Riverside County housing prices as of March 2006 were up 4.0% over the same month last year. The median detached new home price in the County was \$448,823 in March 2006, according to a survey by the Hanley Wood Market Intelligence. Although up 4.0% from the end of the first quarter 2005, the median price is up only 0.75% from the fourth quarter 2005 level. San Bernardino County had a median price of \$371,836, up 7.7% in one year, but down 15.0% from September 2005. New home sales volume for the quarter, is down 27.0% from the first quarter of 2005. No new home submarkets had sales increases. All submarkets had declines. The subject property is located in the Central submarket, which had a 10.2% decline in sales from one year ago. For all of 2005, all submarkets declined in their sales per project, with a decline of 13.6% for all of Riverside County, compared to 2004. During the first quarter of 2006, all sub-markets continued their decline, with a decline of 30.9% from the sales rate per project in the first quarter of 2005.

The current projection for the housing market is that we are seeing a return to a more balanced and normal market. The past several years of record high sales volume and record high appreciation appears to have stabilized, causing property values to plateau or even decline in some areas. The Inland Empire is expected to stay stronger than surrounding counties, because homes are more affordable than on the coast. The Inland Empire is expected to continue to draw homebuyers from Orange, Los Angeles and San Diego counties where home prices are significantly higher.

Up to the fourth quarter of 2005, these three counties saw a decline in home sales from a year earlier, while the Inland Empire experienced its strongest or second strongest monthly sales rates. Most markets throughout Southern California plateaued during the last quarter of 2004 and the first two months of 2005. However, between

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March and November 2005, sales prices and sales rates improved. Sales in the Inland Empire have slowed over the last six months.

While overall inventory is up, the impact is to a more normal market especially when it comes to supply and demand. Job creation was moderate over the past 24 to 30 months of recovery from the previous recession and the economy is still growing at a reasonable pace overall. Given the supply of new residential product in the Riverside County market, the subject tract, if still selling, would sell at a moderate rate, but without the increases in price that have been experienced over the past several years. More and more news articles are suggesting that home prices are reaching a maximum level, and might even decline in this year or 2007.

Builders within Riverside County sold 4,616 new single-family detached homes and 1,097 condominiums during the first quarter of 2006. Both are significant declines from the third quarter of 2005, and from the first quarter of 2005. This represents a decrease of 27.0% for detached product and 61.9% for attached product over the first quarter of 2005. The bulk of the detached homes sold in Riverside County during the first quarter of 2006 is priced over \$450,000 and comprises 72%± of the total sales. Sales of homes priced between \$350,000 to more than \$550,000 continue to see the most activity, comprising 95%± of the detached market. The number of active detached projects in Riverside County increased by 1 project during the first quarter of 2006. The submarket with the greatest number of projects is the South submarket.

Standing (completed, but unsold) detached inventory increased almost 400% in the first quarter of 2006 compared to the first quarter of 2005 to 333 units in Riverside County. This is up almost 140% from 140 units at the end of the third quarter of 2005. At the current sales rate, that is about a one-week supply of detached homes. Detached total (built, under construction, planned) unsold inventory consisted of 22,570 units at the end of the first quarter of 2006, which is down from 25,733 units last year. At the current sales rates, this level of inventory equates to an 11.9 month supply, which is down from 14.1 months last year.

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Home prices generally continued to increase during all of 2005 and the first quarter of 2006, albeit at a much lower rate than prior years. While year over year prices are slightly above that of the previous 12 months, month to month increases have slowed significantly. We are aware that most projects are offering incentives or concessions to their buyers. However, the exact amount is often difficult to quantify. Often the incentives vary based on the status of the home construction. That is, if the home is standing inventory the incentives and concessions are much higher than if the home has two to three months before being ready for occupancy. Some projects in Riverside County began price reductions during the first quarter of 2006.

According to an interest rate survey published weekly in The Los Angeles Times, the typical 30-year, fixed rate conforming loan was between 6.25% and 6.75% as of the date of this report. Mortgage rates have been in the 5.50% to 6.00% range over the past year, following more than a year of rates in the 6.00% range. While a slight increase in rates may impact demand, we do not anticipate a significant drop in demand as long as rates remain near or below the 8.00% level.

Riverside - South Submarket

The subject is situated in the South submarket region, which accounted for 1,136 detached sales during the first quarter of 2006, or about a 24.6% market share of the Riverside County market. This sales rate is down 16.0% from the first quarter 2005 sales rate, but down 20%± from the third quarter of 2005. Another indication of the slowing market is that for all of 2005, the South submarket had average monthly sales per project of 4.8 units. However, in the first quarter, the average sales rate was only 3.8 units per project per month, a 20% decline. The median base price in the South submarket was stagnant over the past year at \$471,240, a -0.1% decrease. Although it is a mid-priced submarket in Riverside County with a price per square foot of \$185.00, the price per square foot in the subject's submarket increased by 12.8%, and the average size of a detached home decreased by 11.4%.

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During the first quarter of 2006, the subject's submarket sold no detached homes priced between \$300,000 and \$349,999; 198 detached homes priced between \$350,000 and \$399,999 were sold; and 235 detached homes priced between \$400,000 and \$449,999 were sold. Additionally, 703 homes over \$450,000 were sold. There were 291 attached units that sold in the subject's submarket, mostly under \$350,000.

Within the South submarket there are 111 active projects, which is 3 more than last year at this time. The subject's market area reports 37 unsold standing (built, but unsold) inventory units and 521 unsold units under construction. This is a five-week absorption time for the completed dwellings and for the units under construction. This absorption time is slightly less than the overall rate for the entire county. This inventory level is 7% greater than the inventory level at the end of the first quarter of 2005. Total inventory which includes units built, under construction and future construction totals 4,608 units which equates to a 10.2 month supply at the current sales rate. One year ago total inventory was at 4,498 units, and the absorption time based on last year's sales rate was 11.6 months.

Feasibility

It is not in the scope of this appraisal assignment for the appraisers to conduct an extensive independent market study/absorption analysis, but it is the appraisers' responsibility to address the reasonableness of the conclusions of any market study which has been prepared by outside firms for the subject property. Unforeseen national and regional economic and/or social changes will affect the time-frame of real estate development.

In an attempt to arrive at reasonable and supportable absorption schedules for the various uses within Improvement Area 2 of CFD No. 2004-3, the appraisers reviewed an independently prepared absorption analysis that relates to the CFD. This independent study is titled Market Absorption Study, CFD No. 2004-3 Improvement Area No. 2, (Rosetta Canyon), prepared by Empire Economics, Inc, dated May 25, 2006, for the City of Lake Elsinore. A copy of a portion of the absorption analysis summary is included in the Addenda of this report.

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The study reports that the subject property will have a 3± year absorption time frame. The 213 homes at Fox & Jacobs are estimated to absorb at 25 units in 2006, 80 units in 2007 and 2008 and the balance of 28 homes in 2009. The 98 proposed homes at Santa Rosa are estimated to absorb at 20 homes in 2006, 40 homes in 2007, and the remaining 38 homes in 2008. The number of homes in the product mix allocated to the Caraway II and Augusta II product has changed since the Market Study but the absorption rate is assumed to stay the same. The overall monthly absorption is 6 to 7 units per month for the Fox & Jacobs project and generally between 3 and 4 units per month for the Santa Rosa, Caraway II and Augusta II projects. It should be noted that this appraisal values merchant builder land, while the market absorption report refers to homebuyers purchasing completed homes.

It is our opinion, after surveying the competitive projects and analyzing the pricing, design, location differences and other pertinent factors, that the subject property should experience average to good absorption, similar to that reported by Empire Economics.

The table on the following page reports the prices and absorption of ten detached residential developments including the four subject projects at Rosetta Canyon. Detached absorption has ranged from 3.9 units per month to 8.8 units per month for projects that have been in an active sales program for 12 to 18 months. The subject's tract, Fox & Jacobs, opened for sales on February 25, 2006. The sales representative reports 43± homes sold as of the survey date, July 7, 2006. The homes are under construction for delivery in the 4th quarter of 2006. This represents a monthly absorption of 8± units per month. The Santa Rosa, Caraway II and Augusta II projects opened for sales in mid-June 2006 and as of the survey date, August 5, 2006, Santa Rosa has sold 6 homes, Caraway II 4 homes and Augusta II 2 homes.

**Rosetta Canyon Market Area
Comparable Residential Project Summary
Detached Single Family Homes
August 5, 2006**

No.	Project/Developer/Location	Total Lot Size		Model	Base Price	Size		No. Sold Start Dt.	Overall Mo. Abs.
		Units	Min./Avg.			Sq. Ft.	\$/Sq. Ft.		
1	Fox & Jacobs @ Rosetta Canyon II Fox & Jacobs Homes Riverside St./Steel Valley Rd. (Rosetta Canyon), Lake Elsinore TBM 836 H-6	213	5,000	Plan 1	\$379,990	2,400	\$158.33	43 ⁽¹⁾ Feb-06	8.1
			6,600	Plan 2	\$386,990	2,710	\$142.80		
				Plan 3	\$399,990	2,875	\$139.13		
				Plan 4	\$417,990	3,113	\$134.27		
				Plan 6	\$359,990	1,979	\$181.91		
				Plan 7	\$386,990	2,613	\$148.10		
2	Santa Rosa @ Rosetta Canyon II Fox & Jacobs Homes Bantry Bay Street/Astird Way/Riverside St. (Rosetta Canyon), Lake Elsinore TBM 836 G&H-7	98	6,500	Plan 2266	\$376,990	2,266	\$166.37	6 ⁽¹⁾ Jun-06	3.3
			8,300	Plan 2710	\$407,990	2,710	\$150.55		
				Plan 3206	\$429,990	3,206	\$134.12		
				Plan 3487	\$459,990	3,487	\$131.92		
3	Caraway II @ Rosetta Canyon Centex Gallica St./Riverside St. (Rosetta Canyon), Lake Elsinore TBM 836 G&H-7	78	6,600	Plan 1	\$414,990	2,648	\$156.72	4 ⁽¹⁾ Jun-06	2.5
			7,300	Plan 2	\$475,990	2,916	\$163.23		
				Plan 3	\$494,990	3,258	\$151.93		
4	Augusta II @ Rosetta Canyon Centex Gallica St./Riverside St./Steel Valley Rd. (Rosetta Canyon), Lake Elsinore TBM 836 G&H-7	114	6,600	Plan 3242	\$494,990	3,242	\$152.68	2 ⁽¹⁾ Jun-06	1.3
			7,800	Plan 3613	\$536,990	3,613	\$148.63		
				Plan 4063	\$553,990	4,063	\$136.35		
5	Solana @ Rosetta Canyon Centex Homes Rosetta Canyon Dr. @ Diana Lane (Rosetta Canyon), Lake Elsinore TBM 836 F-6	80	6,500	Plan 1	\$411,990	2,180	\$188.99	70 Jun-05	5.2
				Plan 2	\$412,990	2,324	\$177.71		
				Plan 3	\$436,990	2,579	\$169.44		
				Plan 4	\$443,990	2,750	\$161.45		
6	Alderbrook at Canyon Hills Pulte Homes Canyon Hills Road @ Fallsbrook Lane (Canyon Hills Community), Lake Elsinore TBM 867 E-6	143	5,000	Plan 1	\$497,680	2,607	\$190.90	22 ⁽¹⁾ Feb-06	3.9
				Plan 2	\$516,100	2,888	\$178.70		
				Plan 3	\$522,200	3,103	\$168.29		
7	Weatherly at Canyon Hills Pulte Homes Angles Falls @ Chaparossa (Canyon Hills Community), Lake Elsinore TBM 867 E-6	131	4,100	Plan 1	\$430,670	1,949	\$220.97	27 Jan-06	4.2
				Plan 2	\$441,030	2,110	\$209.02		
				Plan 3	\$459,100	2,458	\$186.78		
8	Briarcliff Pardee Homes Hillside Drive @ Trailside Drive (Canyon Hills Community), Lake Elsinore TBM 867 E-6	109	6,000	Plan 1	\$470,600	2,485	\$189.38	67 Jul-05	5.4
				Plan 2	\$483,375	2,679	\$180.43		
				Plan 3	\$473,864	2,820	\$168.04		
				Plan 4	\$485,175	3,035	\$159.86		
9	Bridgagate Pardee Homes Hillside Drive Lake Elsinore, TBM 867 E-6	147	6,000	Plan 1	\$510,325	2,962	\$172.29	12 ⁽¹⁾ May-06	3.8
				Plan 2	\$524,000	3,059	\$171.30		
				Plan 3	\$548,000	3,315	\$165.31		
				Plan 4	\$570,000	3,699	\$154.10		
10	Cross Creek Pardee Homes Sweet Acacia Ct. (Canyon Hills Community), Lake Elsinore TBM 867 E-6	127	6,000	Plan 1	\$392,550	1,671	\$234.92	109 Jul-05	8.8
				Plan 1X	\$411,050	1,918	\$214.31		
				Plan 2	\$443,600	2,113	\$209.94		
				Plan 3	\$448,300	2,439	\$183.80		

Survey Date 8/5/06
(1) Reservations

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Maximally Productive

In considering what uses would be maximally productive for the subject property, we must consider the previously stated legal considerations. We are assuming the land uses allowed under the Specific Plan zone regulation with the City of Lake Elsinore are the most productive uses that will be allowed at the present time. Current zoning and approved uses indicate that other alternative uses are not feasible at this time. Given the steady, but moderating demand for residential product in Riverside County and the subject market area, it is our opinion that the development as proposed provides the highest land value and is, therefore, maximally productive.

Conclusion

Legal, physical, and market considerations have been analyzed to evaluate the highest and best use of the property. This analysis is presented to evaluate the type of uses that will generate the greatest level of future benefits possible from the land.

After reviewing the alternatives available and considering this and other information, it is the opinion of the appraisers that the highest and best use for the subject property, as vacant and as proposed, is for residential development similar to that proposed for the subject tracts. The projects appear to have the location, features, and pricing structure to obtain an average to good sales rate under normal financing and market conditions.

As Vacant and As Improved

After reviewing the alternatives available and considering this and other information, it is these appraisers' opinion that ultimate development of single-family detached and attached for-sale homes similar to the current proposed products are considered the highest and best use of the property.

VALUATION METHODOLOGY

Basis of Valuation

Valuation is based upon general and specific background experience, opinions of qualified informed persons, consideration of all data gathered during the investigative phase of the appraisal and analysis of all market data available to the appraiser.

Valuation Approaches

Three basic approaches to value are available to the appraiser:

Cost Approach

This approach entails the preparation of a replacement or reproduction cost estimate of the subject property improvements new (maintaining comparable quality and utility) and then deducting for losses in value sustained through age, wear and tear, functionally obsolescent features, and economic factors affecting the property. This is then added to the estimated land value to provide a value estimate.

Income Approach

This approach is based upon the theory that the value of the property tends to be set by the expected net income therefrom to the owner. It is, in effect, the capitalization of expected future income into present worth. This approach requires an estimate of net income, an analysis of all expense items, the selection of a capitalization rate, and the processing of the net income stream into a value estimate.

Direct Comparison Approach

This approach is based upon the principle that the value of a property tends to be set by the price at which comparable properties have recently been sold or for which they can be acquired. This approach requires a detailed comparison of sales of comparable properties with the subject property. One of the main requisites, therefore, is that sufficient transactions of comparable properties be available to provide an accurate indicator of value and that accurate information regarding price, terms, property description, and proposed use be obtained through interview and observation.

Static Residual Analysis is used to estimate the merchant builder land value when the proposed product is known. From the estimated base retail home price, all costs associated with the home construction including direct

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construction costs, indirect construction costs, financing and profit are deducted. Following the deduction of costs, the residual figure is an estimate of the merchant builder land value.

The residential land is valued by the Direct Comparison Approach and the Static Residual Analysis. The Income Approach is typically used when appraising income producing properties. This approach is not applicable in the valuation of land as land is not typically held to generate monthly income, but rather purchased to construct an end product which may or may not generate income. The Cost Approach is not an appropriate tool in the valuation of the land.

The subject property is in various stages of development. Rosetta Canyon includes production homes under construction by the builder/developer. Most of the lots in CFD No. 2004-3, I.A. 2 are in a blue-top plus wet utilities to a near finished condition. The products being built are considered the highest and best use of the property and are in demand by the Riverside County homebuyer. Therefore, the partially completed improvements are considered to add value. The units under construction are valued based on a conservative estimate of their stage of completion. This percentage is applied to the estimated base sales price of the home for an indication of value. Lots that do not have at least partial framing under construction are valued as near finished lots.

VALUATION OF CFD NO. 2004-3, IMPROVEMENT AREA 2

General Information

The subject property is being built by the developer Centex Homes and Fox & Jacobs, which is a subsidiary of Centex Homes. The actual sales price of a particular parcel is always considered the best indication of value, assuming the transaction is arm's length, current and meets the definition of Market Value. The first section of the valuation portion of the report will value the lots that do not have unit construction. The value estimates for the lots at blue-top lot and finished lot condition is provided based on the lot condition as of the date of value. In the case of the subject lots, its Market Value will be best indicated by the merchant builder residential land sales that have occurred in the City of Lake Elsinore, Menifee Valley and Wildomar. A discussion of the market data will precede the parcel valuation. A residual analysis will also be completed as a cross-check to the value indicated by the land sales. The next section of the report will value the production units that are in various stages of construction.

Direct Comparison Approach – Finished Lots

The Direct Comparison Approach is based upon the premise that, when a property is replaceable in the market, its value tends to be set by the purchase price necessary to acquire an equally desirable substitute property, assuming no costly delay is encountered in making the decision and the market is reasonably informed. In appraisal practice, this is known as the Principle of Substitution.

This approach is a method of analyzing the subject property by comparison of actual sales of similar properties, when available. These sales are evaluated by weighing both overall comparability and the relative importance of such variables as time, terms of sale, location of sale property, and lot characteristics. The actual sales price of a particular parcel is always considered the best indication of value, assuming the transaction is arm's length, current and meets the definition of Market Value. The Market Value will be best indicated by the merchant builder residential land sales that have occurred in the Lake Elsinore, Wildomar and Menifee areas. A discussion of the

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market data will precede the parcel valuation. For the purpose of this report, the unit of comparison utilized is the price per unit for the residential land. Please refer to the following page that summarizes the sales considered similar to the subject parcel.

We have surveyed residential sales in the Lake Elsinore, Menifee and Wildomar market areas. The eight sales used in the analysis are the comparables considered most helpful in valuing the subject property. We have reviewed and inspected all of the data items. The previous table includes the raw land cost per unit, blue-top price per unit, and the finished lot prices for merchant builder parcels.

The comparable land sales have sold in raw condition and blue-top lot condition. Costs to bring the land from the condition at the time of sale to finished lot condition were made available to analyze the data. Therefore, the analysis will conclude at an indication of finished lot value for the subject parcels, and then a deduction to bring the subject from a finished lot condition to the "As Is" lot condition is made. An analysis of the finished land purchase price for all the Data Items was helpful to arrive at the "As Is" value of the subject tracts. Most weight was given to Data Nos. 1, 2 and 3 which are closest in location and product type to the subject property.

Land Sale Summary CFD No. 2004-3 Market Area Merchant Builder Parcels								
Data No./ Location	Buyer/ Seller	Sales Date	Parcel Size	No. of Lots/ Lot Size	Raw Condition Price per Lot	Blue Top Price per Lot	Finished Lot Price	Remarks
No. 1 SE of 1-15, SE of S-74 @ 3rd St. & Old Ranch Road Lake Esinore	Wasson Canyon Holdings, L Wasson Canyon Investments, L.P.	7/05	59.4 Acres	191 6,000 SF	--	--	\$185,000	raw condition at sale 1.9% tax rate
No. 2 E/O Railroad Canyon Rd. N/O Canyon Hills Rd Lake Esinore	Fulte Homes Pardee Grossman	7/05	28.5 Acres	131 4,900 SF Min	--	\$135,916	\$200,377	Blue Top condition at sale 1.8% tax rate
No. 3 E/O Railroad Canyon Rd. N/O Canyon Hills Rd Lake Esinore	Fulte Homes Pardee Grossman	7/05	40.07 Acres	131 5,000 SF Min	--	\$132,447	\$202,600	Blue Top condition at sale 1.8% tax rate
No. 4 N/S Newport Rd. @ Winter Hawk Road Menifee	U.S. Homes (Lennar) Creekside Vuilla, LLC	7/04	60 Acres	226 7,000 SF Min	--	--	\$145,000	Sold in raw condition 1.8% tax rate
No. 5 NWC Haun Road & Garbani Road Menifee	SCC-Canyon II, LLC Anil Rastogi, et al	2/05	36.1 Acres	128 7,200 SF Min	\$90,000	--	\$155,000	Sold in raw condition 1.9% tax rate
No. 6 SWC Haun Road & Craig Avenue Menifee	Confidential Burns Ranch, Inc.	Current Escrow	64.6 Acres	210± 7,200 SF Min	\$82,975	--	\$168,000	Sold in raw condition 1.9% tax rate
No. 7 NE/S Palomar Street, SE of Catt Road Wildomar	Rancho Vista II Ventures Ternecula Creek Estates	6/04	NA	114 7,200 SF Min	\$105,000	--	\$159,990	Sold in raw condition 1.7% tax rate
No. 8 N/O Simpson Road, E/ Leon Road Menifee Valley	Winchester Ranch 202, LLC Stonegate Dev. I, LLC	12/04	58.3 Acres	202 7,200 SF Min	\$77,500	--	\$155,000	Sold in raw condition 1.9% tax rate

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Land Sale Data No. 1

Location: Southeast side of I-15, southeast of S-74 and east of the intersection of 3rd Street and Old Ranch Road, Lake Elsinore

Legal Description: 347-330-019, 045, 046, 050, 051, 052, 053 and 347-360-003

Buyer: Wasson Canyon Holdings, LLC

Seller: Wasson Canyon Investments, L.P.

Parcel Size: 59.4 acres

No. of Units: 191

Lot Size: 6,000 square feet

Zoning: R-1

Intended Use: To construct 191 detached residential dwellings

Date Recorded: June 28, 2005

Sale Price: N/A, based on a finished lot value of \$185,000

Price/Unit: N/A

Finished Lot Cost: \$185,000

Site Condition: Raw at sale date with approved tentative tract map

Financing: All cash to seller

Verification: Seller, broker and Grant Deed

Comments: The effective tax rate is estimated to be 1.9%.

Land Sale Data No. 2

Location: East of Railroad Canyon Road, north of Canyon Hills Road, Lake Elsinore

Legal Description: Tract No. 30493-4, Lots 26-55, 370-379;
Tract No. 30493-5, Lots 56-84, 362-369;
Tract No. 30493-6, Lots 85-102, 326-361.

Buyer: Pulte Home

Seller: Pardee Home

Parcel Size: 28.5± gross acres

No. of Units: 131

Lot Size: 4,900 square foot minimum lot size

Zoning: SP

Intended Use: To construct 131 detached dwellings ranging in size from 1,949 to 2,458 square feet. The subdivision is known as Weatherly,

Date Recorded: July 15, 2005

Sale Price: \$17,805,000

Price/Unit: \$135,916

Finished Lot Cost: \$200,377

Site Condition: Blue-top at sale

Financing: All cash to seller

Verification: Seller & Buyer

Comments: This property is encumbered by a CFD. This site is level to rolling hillside. It is within the Canyon Hills master planned community.

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Land Sale Data No. 3

Location: East of Railroad Canyon Road, north of Canyon Hills Road, Lake Elsinore

Legal Description: Tract No. 30493-7, Lots 103-116, 137-156; 188-198, 322-325.
Tract No. 30493-8, Lots 117-136, 157-187;
Tract No. 30493, Lots 199-222, 303-321.

Buyer: Pulte Home

Seller: Pardee Home

Parcel Size: 40.7± gross acres

No. of Units: 143

Lot Size: 5,000 square foot minimum lot size

Zoning: SP

Intended Use: To construct 143 detached dwellings ranging in size from 2,607 to 3,079 square feet. The subdivision is known as Alderbrook.

Date Recorded: July 23, 2005

Sale Price: \$18,940,000

Price/Unit: \$132,447

Finished Lot Cost: \$202,600

Site Condition: Blue-top at sale

Financing: All cash to seller

Verification: Seller & Buyer

Comments: This property is encumbered by a CFD. This site is level to rolling hillside. It is within the Canyon Hills master planned community.

Land Sale Data No. 4

Location:	North side Newport Road at Winter Hawk Road, Menifee
Legal Description:	Parcel Map No. 12764
Buyer:	U.S. Home (Lennar)
Seller:	Creekside Villa, LLC
Parcel Size:	60.0 gross acres
No. of Units:	226
Lot Size:	7,200 square foot minimum size
Zoning:	R-1
Intended Use:	To construct 226 detached dwellings in two projects, dwelling size to range from 2,600 to 3,400 square feet.
Date Recorded:	July 2, 2004
Sale Price:	N/A
Price/Unit:	N/A
Finished Lot Cost:	\$145,000
Site Condition:	Sold raw, site grading underway
Financing:	All cash to seller
Verification:	Listing broker
Comments:	This site will have two developments. Emerson Lane will have homes from 2,600 to 3,400 square feet. Arbor Lane will have homes from 2,621 to 3,322 square feet. This property will have a CFD, with a tax rate similar to the subject.

Land Sale Data No. 5

Location:	Northwest corner of Haun Road and Garbani Road, Menifee
Legal Description:	TTM No. 31724
Buyer:	SCC—Canyon II, LLC
Seller:	Anil Rastogi, et al
Parcel Size:	36.13 acres
No. of Units:	128
Lot Size:	7,200 square feet
Zoning:	R-1
Intended Use:	To construct 128 detached single-family dwellings.
Date Recorded:	February 9, 2005
Sale Price:	\$11,520,000
Price/Unit:	\$90,000
Finished Lot Cost:	\$155,000
Site Condition:	Raw at sale
Financing:	All cash to seller
Verification:	Buyer
Comments:	The seller processed Tentative Tract Map No. 31724, and the sale closed with an approved tentative tract map. A CFD is being formed and the effective tax rate is approximately 1.9%. The CFD is approximately \$18,000 per lot. The finished lot price is \$155,000 per lot (net of the CFD) and \$173,000 per lot without the CFD.

HRA

Land Sale Data No. 6

Location:	Southwest corner Haun Road and Craig Avenue, Menifee
Legal Description:	Portion SE Quarter Section 10, T6S R3W
Buyer:	Confidential
Seller:	Burns Ranch, Inc.
Parcel Size:	64.55 acres
No. of Units:	210+
Lot Size:	7,200 square feet
Zoning:	R-1
Intended Use:	To construct approximately 210 detached residential dwellings.
Date Recorded:	Current escrow
Sale Price:	\$17,425,000
Price/Unit:	\$82,975
Finished Lot Cost:	\$168,000
Site Condition:	Raw at sale date
Financing:	All cash to seller
Verification:	Listing Broker
Comments:	The property is scheduled to close in mid-2006. The long escrow period allows the buyer to process the approvals and the site will close with the approval of the tentative tract map. The effective tax rate is 1.9%. The APNs are 360-240-034 and 360-260-005.

HRA

Land Sale Data No. 7

Location: Northeast side of Palomar Street, southeast of Catt Road, Wildomar

Legal Description: N/A (Rancho Vista II)

Buyer: Rancho Vista II Ventures, LLC

Seller: Temecula Creek Estates, LLC

Parcel Size: N/A

No. of Units: 114

Lot Size: 7,200 square feet

Zoning: R-1

Intended Use: To construct 114 detached residential dwellings ranging from 2,447 to 3,434 square feet. Base sales prices are estimated between \$350,000 and \$465,000.

Date Recorded: June 2004

Sale Price: \$11,970,000

Price/Unit: \$105,000

Finished Lot Cost: \$159,990

Site Condition: Raw at sale date with approved tentative tract map

Financing: All cash to seller

Verification: Seller

Comments: The effective tax rate is estimated to be 1.7%.

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Land Sale Data No. 8

Location: North of Simpson Road, east of Leon Road, Menifee Valley

Legal Description: 462-020-040, 041, 046 and 047; Parcel 1 and 2 of Parcel Map 5986 and Parcels 1, 3 and 4 of Parcel Map 6517

Buyer: Winchester Ranch 202, LLC

Seller: Stonegate Development I, LLC

Parcel Size: 58.3 acres

No. of Units: 202

Lot Size: 7,200 square feet

Zoning: R-1

Intended Use: To construct 202 detached residential dwellings

Date Recorded: December 20, 2004

Sale Price: \$15,655,000

Price/Unit: \$77,500

Finished Lot Cost: \$155,000

Site Condition: Raw at sale date with approved tentative tract map

Financing: All cash to seller

Verification: Broker and Grant Deed

Comments: The effective tax rate is estimated to be 1.9%.

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Analysis

Financing

All of the comparable sales were all cash transactions or financing considered to be cash, therefore, no adjustments for financing were warranted.

Property Rights Conveyed

All of the comparables involved the transfer of the fee simple interest. The subject's fee simple interest is appraised in this report, and therefore, no adjustment is warranted.

Time of Sale

During the past 8 years, Southern California has sharply rebounded from its lengthy recession. Demand for land sales has dramatically exceeded supply. Prices paid for residential land increased annually by 15% to 20% and more from 1997 to 2000. However, 2001 saw a leveling of land prices, only to increase again during 2002, 2003, 2004 and the first six months of 2005. Home prices have increased from the lows of 1996. The average new home price in Riverside County has increased from \$156,907 in the first quarter of 1996 to \$448,823 in the first quarter of 2006. The median price increased 4.0% in the last 12 months. This is a record high, median price level for new homes in Riverside County. However, while prices have continued up, the increase is significantly lower than in the past 5+ years. Sales activity has declined for the last eight months, compared to one year earlier sales activity. The market in general first began to plateau during August and September 2004. The price stabilization continued through February 2005. Sales prices resumed moderate increases from February 2005 to August 2005. Prices plateaued through the beginning of 2006 and appear to be declining over the last three to four months. Based on current market conditions, we have estimated a 1% per month upward adjustment through July 2005.

Conditions of Sale

Typically, adjustments for conditions of sale reflect the motivations of the buyer and the seller in the transfer of real property. The conditions of sale adjustment reflects

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the difference between the actual sales price of the comparable and its probable sales price if it were sold in an arms-length transaction with typical motivations. Some circumstances of comparable sales that will need adjustment include sales made under duress, eminent domain transactions and sales that were not arm's length. All of the transactions were reported to be arm's length in nature. Accordingly, no adjustment is indicated.

Location

The location adjustment is based on proximity to existing infrastructure and employment. Data No. 1 is closest to the subject and slightly superior in location a 5% downward adjustment is indicated. Data Nos. 2 and 3 located in the Canyon Hills Master planned Community are considered a superior location and a 10% downward adjustment is indicated. The four sales located in the Menifee area are generally considered inferior and a 10% upward adjustment is indicated. Data No. 7 in Wildomar is considered similar to the subject and has no location adjustment.

Entitlement/Map Status

All of the sales are entitled. No adjustment is required.

Tax Rate

The subject is expected to have an average overall tax rate around 1.80% to 2.00% of base sales price. The comparable sales that have similar CFDs or Assessment Districts do not require an adjustment. The merchant builders of the land are aware of the various taxes and have factored the impact of the higher tax rates into the prices paid for the land.

Lot Size

The comparables have minimum lot sizes that range from 4,900 square feet to 7,200 square feet. The minimum lot size for the subject is 5,000 square feet to 6,600 square feet. Interviews with sales persons indicated that lot size is an important feature to

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the Lake Elsinore homebuyer. Downward adjustments are required for Data Nos. 4, 5, 6, 7 and 8 which have 7,000 to 7,200 square foot minimum lot.

Condition of Lots

All of the data had prices based on a finished condition. Deductions for costs to bring the subject parcel from finished lot condition to the current "As Is" condition is made at the Conclusion of Value in this analysis.

Please refer to the next page for the adjustment grid of the 8 comparable land sales. After all adjustments, and giving consideration to all of the data, the comparable data indicated a per lot value of \$170,520 to \$185,000 per finished lot.

Land Sale Adjustments
CFD No. 2004-3 Market Area
 Merchant Builder Lots 4,900 to 7,200 SF Minimum

Data No. Project/ Location	Sales Date	Parcel Size	No. of Lots/ Lot Size	Entitlement	Condition at sale	Price Per Lot	Time	Time Adj. Lot Cost	Location	Approved Map	Tax Rate	Lot Size	Condition of Lots	Adjusted Lot Value
No. 1 SE of 1-15, SE of S-74 @ 3rd St. & Old Ranch Road Lake Elsinore	7/05	59.4 Acres	191 6,000 SF	Entitled	Raw Land	\$185,000	0%	\$185,000	0%	0%	0%	0%	0%	\$185,000
No. 2 E/O Railroad Canyon Rd. N/O Canyon Hills Rd Lake Elsinore	7/05	28.5 Acres	131 4,900 SF Min	Entitled	Blue-top	\$200,377	0%	\$200,377	-10%	0%	0%	0%	0%	\$180,339
No. 3 E/O Railroad Canyon Rd. N/O Canyon Hills Rd Lake Elsinore	7/05	40.07 Acres	131 5,000 SF Min	Entitled	Blue-top	\$202,600	0%	\$202,600	-10%	0%	0%	0%	0%	\$182,340
No. 4 N/S Newport Rd. @ Winter Hawk Road Menifee	7/04	60 Acres	226 7,000 SF Min	Entitled	Raw Land	\$145,000	12%	\$162,400	10%	0%	0%	-5%	0%	\$170,520
No. 5 NWC Haun Road & Garbani Road Menifee	2/05	36.1 Acres	128 7,200 SF Min	Entitled	Raw Land	\$155,000	5%	\$162,750	10%	0%	0%	-5%	0%	\$170,888
No. 6 SWC Haun Road & Craig Avenue Menifee	Current Escrow	64.6 Acres	210+ 7,200 SF Min	Entitled	Raw Land	\$166,000	-5%	\$159,600	10%	0%	0%	-5%	0%	\$167,580
No. 7 NE/S Palomar Street, SE of Catt Road Wildomar	6/04	NA	114 7,200 SF Min	Entitled	Raw Land	\$159,990	13%	\$180,789	0%	0%	0%	-5%	0%	\$171,749
No. 8 N/O Simpson Road, E/O Leon Road Menifee Valley	12/04	58.3 Acres	202 7,200 SF Min	Entitled	Raw Land	\$155,000	7%	\$165,850	10%	0%	0%	-5%	0%	\$174,143

Conclusion of Finished Lot Value - Direct Comparison

After all adjustments, and giving the most emphasis to Data Nos. 1, 2 and 3, the comparable data indicated a per lot value of \$180,000 per finished lot, for lots with a minimum size of 5,000 to 6,600 square feet.

Static Residual Analysis

The land is valued by the Direct Comparison Approach and by the Static Residual Analysis. The purpose of this analysis is to estimate a value for the land assuming no direct construction has taken place. This method is particularly helpful when development for a subdivision represents the highest and best use and when competitive house sales are available. Reportedly, this analysis is by far the most commonly used by merchant builders when determining price for land.

This analysis is useful for projects that will have a typical holding period of one to two years which represents the typical holding period sought by merchant builders. The Residual Analysis best replicates the investor's analysis when determining what can be paid for the land based on proposed product. Purchase of the land is simply treated as one of the components necessary to build the houses to sell to the homeowner. When all the components of the end-product can be identified and reasonable estimates of costs and profit can be allocated, the Residual Analysis becomes the best indicator of value to a merchant builder for a specific product. Because specific product information is available, this analysis is particularly meaningful.

The analysis uses an estimated average base sales price for a specific product, then deducts the various costs including direct costs of construction, marketing, taxes and overhead, as well as the required profit margin to attract an investor in light of the risks and uncertainties of the project. This analysis is most helpful when significant lot and or view premiums are not present. When negotiating land price, builders typically will consider the value of lot premiums when they are significant, but typically do not give the premiums full consideration. When a downturn in the market occurs or a slight stall in a sales program, premiums are typically the first to be negotiated away.

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End-product Sales Prices

The analysis uses the average base sales price without lot premiums. Our estimate of sales price includes a review of the subject's sales prices included within the Improvement Description section of this report less the current incentives offered.

Direct Development Costs

We have interviewed local builders in the Southwest Riverside County market area for estimates of direct construction costs for the various proposed products. In addition, direct construction costs for the Fox and Jacobs @ Rosetta Canyon, Santa Rosa, Caraway II and Augusts II products in CFD No. 2004-3, Improvement Area 2, have been provided by the builder. We have compared this information with in-house data on actual developments throughout Riverside County and adjacent counties. Based on our understanding of the proposed quality of construction, home size and functional utility, the estimates provided appear reasonable and supportable. We have used \$50.00 per square foot for the Fox & Jacobs product, \$47.00 per square foot for the Santa Rosa product, \$54.00 per square foot for the Caraway II product and \$52.00 per square foot for the August II product.

Indirect construction costs have been estimated at 4% of sales price, which is found to be an industry standard used for this analysis.

General and Administrative

General and administrative costs are estimated at 4% of retail value. This category covers such expenses as administrative, professional fees, homeowner's association dues, real estate taxes, and miscellaneous costs. This estimate is typical and consistent with the market.

Marketing and Warranty

Marketing and sales expenses plus warranty costs are estimated at 8% of retail value. This category covers such expenses as advertising and sales commissions and home warranties. This estimate is typical and consistent with the market.

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Developer Profit

The line item for profit reflects the required margin to attract an investor in light of the risk and uncertainties of the specific project. This analysis assumes a finished lot and no on-site construction. Therefore, additional risk of development is unknown. However, given the current residential market, and demand for the proposed projects, the risk of development is less.

Based on surveys of builders and developers, profit requirements are typically between 7% and 10% of revenues, with occasional responses down to 6% and as high as 12%. These profit estimates are for projects that can be constructed and sold out in a two year period. Higher profits can be required for longer construction/sellout periods and riskier projects. Lower profits can be accepted in inexpensive land cost areas where homes sell quickly. The subject property is proposed for detached homes on a minimum lot size of 5,000 square feet in an area of good demand in Riverside County. Based on a review of the competing subdivisions, a sales rate of 6± units per month is reasonable for the Fox & Jacobs subdivision. This project is currently in a sale program and has met with good response from the market. The other three subdivisions have just recently opened for sales and indications are that they will be met with adequate response from the market. The Santa Rosa and Caraway II projects are within the current market demand range. The Augusta II project offers homes larger and more expensive than other projects currently selling in the subject's market area which equates to a slightly higher risk in development. A sales rate of 3 to 4 units per month is anticipated for each project. An 8% line item for profit is estimated for the Fox & Jacobs, Santa Rosa and Caraway II subdivisions and a 9% line item for profit is estimated for the Augusta II project.

Interest During Holding Period

A typical allowance for financing during the holding period has been between 4% and 6%. Due to the lenders requiring higher equity participation from the builders, the allowance for profit has been decreased. Based on recent interviews with builders in the subject's market area, we have chosen a 5% deduction for financing during the holding period.

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Site Costs

Because this analysis residuals to a finished lot condition, deductions for costs to bring to a finished lot condition are not required to estimate the value of the finished lot. A residual value for a finished lot is derived. The following page illustrates the Static Residual Analyses for the four projects within CFD No. 2004-3, Improvement Area 2.

Rosetta Canyon
CFD No. 2004-3, Improvement Area 2 Market Area
Static Residual Analysis Finished Land Value and Blue Top Land Value

<u>Subdivision Product</u>	<u>Fox & Jacobs</u>	<u>Santa Rosa</u>	<u>Caraway II</u>	<u>Augusta II</u>	<u>Average Lot Value Weighted Average</u>
Number of Lots	213	98	78	114	
Average Base Retail Value of Improvements	\$388,657	\$418,740	\$461,990	\$528,657	
Average Dwelling Size (Sq. Ft.)	2,615	2,917	2,941	3,639	
Average Dwelling Price per Sq. Ft.	\$148.63	\$143.55	\$157.09	\$145.28	
Direct Building Cost per Sq. Ft.	\$50.00 (1)	\$137,099	\$54.00 (1)	\$158,814	\$52.00 (1)
Indirect Construction Costs	4.00%	\$16,750	4.00%	\$18,480	4.00%
General & Administrative Costs	4.00%	\$16,750	4.00%	\$18,480	4.00%
Marketing and Warranty Costs	8.00%	\$33,499	8.00%	\$36,959	8.00%
Builder's Profit	8.00%	\$33,499	8.00%	\$36,959	9.00%
Interest During Holding Period	5.00%	\$19,433	5.00%	\$23,100	5.00%
Costs to bring to Finished Lot	\$0	\$0	\$0	\$0	\$0
Subtotal Dwelling Unit Costs	\$243,461	\$258,534	\$292,791	\$347,825	
Finished Lot Value Estimate	\$145,196	\$160,206	\$169,199	\$180,832	\$159,919
					Rounded:
					\$160,000

(1) Estimate based on Developer Construction Pro forma

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Conclusion of Finished Lot Value

The following table summarizes the conclusions of finished lot value by the Direct Comparison Approach, the Static Residual Analysis and the appraiser's concluded finished lot value.

From the Direct comparison approach, after all adjustments, the comparable data ranges from \$170,520 to \$185,000 per lot. We have given the most emphasis to Data Nos. 1, 2 and 3, and concluded at a per lot value of \$180,000 per finished lot. From the Static Residual Analysis, the indicated finished lot value ranges from \$145,196 to \$180,832. The weighted average value indication is \$160,000 per finished lot. We have concluded at \$160,000 per finished lot in the valuation of the lots in Improvement Area 2 of CFD 2004-3.

Valuation of Land Under Site Construction

The subject project has 441 detached lots in a blue-top plus condition to near finished condition in CFD No. 2004-3, I.A. 2. Based on our analysis of the eight recent merchant builder lot sales and the Static Residual Analysis, we concluded on a finished lot value of \$175,000 per detached lot. However, the lots require additional costs, including remaining fees, paving, and sidewalks to get to a finished condition. All of these costs, provided by the builder, and the anticipated bond reimbursements are applied to the remaining lots only. The cost to finish is estimated at \$25,200,000. CFD No. 2004-3, I.A. 2 bonds will reimburse approximately \$19,300,000 of the total costs, from this bond issue. The net cost to bring the remaining lots to finished lot condition is estimated at \$13,400 per remaining detached lot. The "as is" lot value is estimated at \$146,600 per detached lot. Based on the costs provided, the 441 near finished lots in CFD No. 2004-3, I.A. 2 have an estimated value of \$64,600,000 as indicated below.

441 lots x \$146,600 =	\$64,650,600
Say	\$64,600,000

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“As Is” Valuation Homes Under Construction

As previously discussed, the subject property has undergone significant site improvements within Tract No. 25477. Sixty-two production dwellings in Fox & Jacobs are under construction. The previous analysis to finished lot condition was provided, in part, because that is the condition the subject land prices are based on. In addition, the comparable land sales are sold in various stages of site construction. Bringing each land sale to a finished lot condition with costs provided by the builders, allows the appraisers to complete the analysis with fewer adjustments and avoids possible incorrect estimates of costs to blue-top lot condition.

To value the production dwellings under construction, we first inspected each product to determine the completion status of the production dwellings. Fox & Jacobs has 62 production dwellings under construction. We then determined the average base sales prices for each product. Fox & Jacobs has an average base price of \$389,000.

Units in various stages of construction were valued based on our inspection of the property. An estimate of completion (stated as a percent) of each unit as of the date of value is used to value the units. The estimate of completion has been arrived at with input from the merchant builder and review of the builder's cost estimates. That percent is then applied to the base sales price of the average size unit.

A physical inspection of the subject property indicated that there were 62 homes under construction. Thirty Fox & Jacobs production dwellings are in a framed condition and considered 50% complete. Thirty-two Fox & Jacobs dwellings are in wrapped condition and considered 65% complete.

The following table summarizes the estimated values for CFD No. 2004-3, I.A. 2 which indicates an “as is” value of \$78,500,000 for the 503 units/lots in various stages of unit and site construction, under the Centex ownership

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CITY OF LAKE ELSINORE CFD 2004-3, I.A. 2

441 Lots	\$64,600,000
30 Dwellings U/C 50% @ \$194,500	\$5,835,000
32 Dwellings U/C 65% @ \$253,000	<u>\$8,096,000</u>
Total Value CFD No. 2004-3, I.A. 2	\$78,531,000
Say	\$78,500,000

VALUATION CONCLUSION

Based on the investigation and analyses undertaken, our experience as real estate appraisers, and subject to all the premises, assumptions and limiting conditions set forth in this report, the following opinion of Market Value is formed as of August 5, 2006.

SEVENTY-EIGHT MILLION FIVE HUNDRED THOUSAND DOLLARS

\$78,500,000

The estimated value assumes bond proceeds of about \$19,300,000 for eligible facilities and/or fees, as described in the Community Facilities Report, are available at the time of sale.

CERTIFICATION

We hereby certify that during the completion of this assignment, we personally inspected the property that is the subject of this appraisal and that, except as specifically noted:

We have no present or contemplated future interest in the real estate or personal interest or bias with respect to the subject matter or the parties involved in this appraisal.

To the best of our knowledge and belief, the statements of fact contained in this appraisal report, upon which the analyses, opinions, and conclusions expressed herein are based, are true and correct.

Our engagement in this assignment was not contingent upon developing or reporting predetermined results. The compensation is not contingent upon the reporting of a predetermined value or direction in value that favors the cause of the client, the amount of the value estimate, the attainment of a stipulated result, or the occurrence of a subsequent event.

The appraisal assignment was not based on a requested minimum valuation, a specific valuation, or the approval of a loan.

The reported analyses, opinions, and conclusions were developed, and this report has been prepared, in conformity with the requirements of the Code of Professional Ethics & Standards of Professional Appraisal Practice of the Appraisal Institute, which include the Uniform Standards of Professional Appraisal Practice.

As of the date of this report, James B. Harris has completed the requirements of the continuing education program of the Appraisal Institute.

The reported analyses, opinions, and conclusions are limited only by the reported assumptions and limiting conditions, and are our personal, unbiased professional analyses, opinions, and conclusions.

No one provided professional assistance to the persons signing this report.

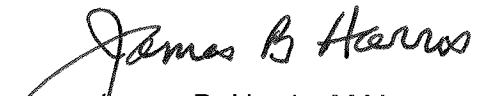
The use of this report is subject to the requirements of the Appraisal Institute relating to review by its duly authorized representatives. In furtherance of the aims of the Appraisal Institute to develop higher standards of professional performance by its

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Members, we may be required to submit to authorized committees of the Appraisal Institute copies of this appraisal and any subsequent changes or modifications thereof.

Respectfully submitted,


Berri J. Cannon Harris
Vice President
AG009147


James B. Harris, MAI
President
AG001846

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ADDENDA

QUALIFICATIONS

HARRIS REALTY APPRAISAL

5100 Birch Street, Suite 200

Newport Beach, CA 92660

(949) 851-1227

**QUALIFICATIONS
OF
JAMES B. HARRIS, MAI**

PROFESSIONAL BACKGROUND

Actively engaged as a real estate analyst and consulting appraiser since 1971. President and Principal of **Harris Realty Appraisal**, with offices at:

5100 Birch Street, Suite 200
Newport Beach, California 92660

Before forming Harris Realty Appraisal, in 1982, was employed with Real Estate Analysts of Newport, Inc. (REAN) as a Principal and Vice President. Prior to employment with REAN was employed with the Bank of America as the Assistant Urban Appraisal Supervisor. Previously, was employed by the Verne Cox Company as a real estate appraiser.

PROFESSIONAL ORGANIZATIONS

Member of the Appraisal Institute, with MAI designation No. 6508
Director, Southern California Chapter – 1998, 1999
Chair, Orange County Branch, Southern California Chapter -1997
Vice-Chair, Orange County Branch, Southern California Chapter - 1996
Member, Region VII Regional Governing Committee - 1991 to 1995, 1997, 1998
Member, Southern California Chapter Executive Committee - 1990, 1997 to 1999
Chairman, Southern California Chapter Seminar Committee - 1991
Chairman, Southern California Chapter Workshop Committee - 1990
Member, Southern California Chapter Admissions Committee - 1983 to 1989
Member, Regional Standards of Professional Practice Committee -1985 - 1997

Member of the International Right-of-Way Association, Orange County Chapter 67.

California State Certified Appraiser, Number AG001846

EDUCATIONAL ACTIVITIES

B.S., California State Polytechnic University, Pomona, 1972.

Successfully completed the following courses sponsored by the Appraisal Institute and the Right-of-Way Association:

Course I-A	Principles of Real Estate Appraisal
Course I-B	Capitalization Theory
Course II	Urban Properties
Course IV	Litigation Valuation
Course VI	Investment Analysis
Course VIII	Single-Family Residential Appraisal
Course SPP	Standards of Professional Practice
Course 401	Appraisal of Partial Acquisitions

Has attended numerous seminars sponsored by the Appraisal Institute and the International Right-of-Way Association.

TEACHING AND LECTURING ACTIVITIES

Seminars and lectures presented to the Appraisal Institute, the University of California-Irvine, UCLA, California Debt and Investment Advisory Commission, Stone & Youngberg and the National Federation of Municipal Analysts.

MISCELLANEOUS

Member of the Advisory Panel to the California Debt and Investment Advisory Commission, regarding Appraisal Standards for Land Secured Financing (March 2003 through June 2004)

LEGAL EXPERIENCE

Testified as an expert witness in the Superior Court of the County of Los Angeles and the County of San Bernardino and in the Federal Bankruptcy Courts five times concerning the issues of Eminent Domain, Bankruptcy, and Specific Performance. He has been deposed numerous times concerning these and other issues. This legal experience has been for both Plaintiff and Respondent clients. He has prepared numerous appraisals for submission to the IRS, without having values overturned. He has worked closely with numerous Bond Counsel in the completion of 100 Land Secured Municipal Bond Financing appraisals over the last five years.

SCOPE OF EXPERIENCE

Feasibility and Consultive Studies

Feasibility and market analyses, including the use of computer-based economic models for both land developments and investment properties such as shopping centers, industrial parks, mobile home parks, condominium projects, hotels, and residential projects.

Appraisal Projects

Has completed all types of appraisal assignments from San Diego to San Francisco, California. Also has completed out-of-state appraisal assignments in Arizona, Florida, Georgia, Hawaii, Nevada, New Jersey, Oklahoma, Oregon, and Washington.

Residential

Residential subdivisions, condominiums, planned unit developments, mobile home parks, apartment houses, and single-family residences.

Commercial

Office buildings, hotels, motels, retail store buildings, restaurants, power shopping centers, neighborhood shopping centers, and convenience shopping centers.

Industrial

Multi-tenant industrial parks, warehouses, manufacturing plants, and research and development facilities.

Vacant Land

Community Facilities Districts, Assessment Districts, master planned communities, residential, commercial and industrial sites; full and partial takings for public acquisitions.

**QUALIFICATIONS
OF
BERRI J. CANNON HARRIS**

PROFESSIONAL BACKGROUND

Actively engaged as a real estate appraiser since 1982. Vice President of ***Harris Realty Appraisal***, with offices at:

5100 Birch Street, Suite 200
Newport Beach, California 92660

Before joining Harris Realty Appraisal was employed with Interstate Appraisal Corporation as Assistant Vice President. Prior to employment with Interstate Appraisal was employed with Real Estate Analysts of Newport Beach as a Research Assistant.

PROFESSIONAL ORGANIZATIONS

Candidate of the Appraisal Institute for the MAI designation.

Co-Chair, Southern California Chapter Hospitality Committee - 1994 - 1998

Chair, Southern California Chapter Research Committee - 1992, 1993

Women in Commercial Real Estate, Member Orange County Chapter.

Chair, Special Events – 1998, 1999, 2000, 2001, 2002, 2003

Second Vice-President - 1996, 1997

Treasurer - 1993, 1994, 1995

Chair, Network Luncheon Committee - 1991, 1992

California State Certified Appraiser, Number AG009147

EDUCATIONAL ACTIVITIES

B.S.B.A., University of Redlands, Redlands, California

Successfully completed the following courses sponsored by the Appraisal Institute:

Principles of Real Estate Appraisal
Basic Valuation Procedures
Capitalization Theory and Techniques - A
Capitalization Theory and Techniques - B
Report Writing and Valuation Analyses
Standards of Professional Practice
Case Studies in Real Estate Valuation

Has attended numerous seminars sponsored by the Appraisal Institute. Has also attended real estate related courses through University of California-Irvine.

LECTURING ACTIVITIES

Seminars and lectures presented to UCLA, California Debt and Investment Advisory Commission, and Stone & Youngberg.

MISCELLANEOUS

Member of the Advisory Panel to the California Debt and Investment Advisory Commission, regarding Appraisal Standards for Land Secured Financing (March 2003 through June 2004)

SCOPE OF EXPERIENCE

Appraisal Projects

Has completed all types of appraisal assignments from San Diego to San Francisco, California. Also has completed out-of-state appraisal assignments in Arizona and Hawaii.

Residential

Residential subdivisions, condominiums, planned unit developments, mobile home parks, apartment houses, and single-family residences.

Commercial

Office buildings, retail store buildings, restaurants, neighborhood-shopping centers, strip retail centers.

Industrial

Multi-tenant industrial parks, warehouses, manufacturing plants, and research and development facilities.

Vacant Land

Residential sites, commercial sites, industrial sites, large multi-unit housing, master planned unit developments, and agricultural acreage. Specializing in Community Facilities District and Assessment District appraisal assignments.

PARTIAL LIST OF CLIENTS

Lending Institutions

Bank of America	NationsBank
Bank One	Preferred Bank
Commerce Bank	Santa Monica Bank
Downey S&L Assoc.	Tokai Bank
Fremont Investment and Loan	Union Bank
Institutional Housing Partners	Wells Fargo Bank

Public Agencies

Army Corps of Engineers	City of Palm Springs
California State University	City of Perris
Caltrans	City of Riverside
City of Aliso Viejo	City of San Marcos
City of Beaumont	City of Tustin
City of Corona	City of Victorville
City of Costa Mesa	County of Orange
City of Encinitas	County of Riverside
City of Fontana	County of San Bernardino
City of Fullerton	Eastern Municipal Water District
City of Hesperia	Orange County Sheriff's Department
City of Honolulu	Ramona Municipal Water District
City of Huntington Beach	Rancho Santa Fe Comm. Services District
City of Indian Wells	Capistrano Unified School District
City of Irvine	Hemet Unified School District
City of Lake Elsinore	Hesperia Unified School District
City of Loma Linda	Romoland School District
City of Los Angeles	Saddleback Valley Unified School District
City of Moreno Valley	Santa Ana Unified School District
City of Newport Beach	Val Verde Unified School District
City of Oceanside	Yucaipa-Calimesa Unified School District

Developers and Landowners

DMB - Ladera	Lennar Homes
Foothill Ranch Company	Rancho Mission Viejo
Hon Development Co.	Santa Margarita Company
Irvine Apartment Communities	Shapell Industries
The Irvine Company.	Sterling Development

Law Firms

Arter & Hadden	McClintock, Weston, Benshoof, Rocheffort & MacCuish
Bronson, Bronson & McKinnon	Palmiri, Tyler, Wiener, Wilhelm, & Waldron
Bryan, Cave, McPheeters & McRoberts	Sonnenschein Nath & Rosenthal
Richard Clements	Strauss & Troy
Cox, Castle, Nicholson	Wyman, Bautzer, Rothman, Kuchel & Silbert
Gibson, Dunn & Crutcher	
Hill, Farrer & Burrill	

MARKET ABSORPTION STUDY (A PORTION)

**EXPECTED PRODUCT MIX CHARACTERISTICS
CFD NO. 2004-3 IMPROVEMENT AREA NO. 2
(ROSETTA CANYON)**

August 10, 2006; Subject to Revision

Projects	Residential Product Types			
	Fox & Jacobs	Santa Rosa	Caraway	Augusta
Product Types	Single-Family	Single-Family	Single-Family	Single-Family
Lot Size, Average	6,600	8,300	7,300	7,800
Housing Unit Mix - Estimated				
Plan # 1	23	24	23	33
Plan # 2	23	17	28	38
Plan # 3	32	30	27	43
Plan # 4	43	27		
Plan # 5	45			
Plan # 6	47			
Totals	213	98	78	114
Share	42.3%	19.5%	15.5%	22.7%
Housing Prices - Base				
Plan # 1	\$359,990	\$376,990	\$414,990	\$494,990
Plan # 2	\$379,990	\$407,990	\$475,990	\$536,990
Plan # 3	\$386,990	\$429,990	\$494,990	\$553,990
Plan # 4	\$386,990	\$459,990		
Plan # 5	\$399,990			
Plan # 6	\$417,990			
Overall Average	\$392,905	\$421,459	\$464,580	\$531,244
Living Area				
Plan # 1	1,979	2,266	2,648	3,242
Plan # 2	2,400	2,710	2,916	3,613
Plan # 3	2,613	3,206	3,258	4,063
Plan # 4	2,710	3,487		
Plan # 5	2,873			
Plan # 6	3,113			
Overall Average	2,706	2,967	2,955	3,675
Value Ratio	\$145	\$142	\$157	\$145

SITE DEVELOPMENT COST SUMMARY

ROSETTA II - TRACTS 25476 & 25477
 BUDGET: 08/02/06

ITEM	BUDGET AMOUNT	COST SPENT TO DATE	COST TO GO
Civil Engineer	\$ 1,196,600.00	\$ 1,112,143.00	\$ 84,457.00
Misc Consultants	\$ 230,197.45	\$ 218,939.36	\$ 11,258.09
Blueprints	\$ 65,200.00	\$ 57,906.02	\$ 7,293.98
Surveying/Layout	\$ 765,900.00	\$ 432,750.50	\$ 333,149.50
Permit Charges	\$ 114,671.30	\$ 63,725.56	\$ 50,945.74
Land Legal Fees	\$ 50,000.00	\$ 7,242.48	\$ 42,757.52
Inspection Fees/Plan Check	\$ 764,179.07	\$ 762,188.86	\$ 1,990.21
Water/Sewer/Storm Fees	\$ 220,185.65	\$ -	\$ 220,185.65
Bonds	\$ 100,000.00	\$ 12,791.00	\$ 87,209.00
Legal Fees-HOA	\$ 30,000.00	\$ 14,997.25	\$ 15,002.75
DRE Processing	\$ 69,680.00	\$ 63,800.00	\$ 5,880.00
DRE Budget Preparation	\$ 24,000.00	\$ 2,800.00	\$ 21,200.00
CC&R Preparation	\$ 17,527.82	\$ 1,097.69	\$ 16,430.13
Sediment/Erosion Control	\$ 309,100.00	\$ 87,484.54	\$ 221,615.46
Site Clearing/Demo	\$ 103,000.00	\$ 74,447.65	\$ 28,552.35
Grading	\$ 8,580,000.00	\$ 7,861,021.40	\$ 718,978.60
Rock Crushing/Excavation	\$ 256,856.87	\$ 254,549.00	\$ 2,307.87
Sanitary Sewer	\$ 1,723,719.00	\$ 1,640,393.00	\$ 83,326.00
Water Mains	\$ 2,292,004.00	\$ 1,955,254.00	\$ 336,750.00
Electrical Underground/Overhead	\$ 4,394,000.00	\$ 2,557,007.44	\$ 1,836,992.56
Refundable Dry Utilities	\$ (990,284.74)	\$ -	\$ (990,284.74)
Concrete Curb	\$ 720,472.00	\$ 360,934.77	\$ 359,537.23
Sidewalk/Aprons	\$ 1,412,741.00	\$ -	\$ 1,412,741.00
Asphalt Paving	\$ 2,287,963.00	\$ 201,261.30	\$ 2,086,701.70
Street Name Signs	\$ 77,680.00	\$ -	\$ 77,680.00
Street Lights	\$ 230,490.50	\$ 231,654.50	\$ (1,164.00)
Perimeter Wall/Fence	\$ 2,384,913.00	\$ 172,166.85	\$ 2,212,746.15
Common Area Landscape	\$ 3,414,459.51	\$ 32,781.60	\$ 3,381,677.91
Site Trash/Clean-Up	\$ 109,900.00	\$ -	\$ 109,900.00
Utility Bills	\$ 360,500.00	\$ -	\$ 360,500.00
Curb Acceptance	\$ 503,000.00	\$ 307,284.27	\$ 195,715.73
Contingency Reserve	\$ 1,291,927.83	\$ -	\$ 1,291,927.83
Total	\$ 33,110,583.26	\$ 18,486,622.04	\$ 14,623,961.22

ROSETTA II - TRACTS 25476 & 25477
 CFD BUDGET: 08/02/06

ITEM	BUDGET AMOUNT	COST SPENT TO DATE	COST TO GO
Purchase of Easement	\$ 4,345.00	\$ 4,345.00	\$ -
Geotechnical Consultant	\$ 79,224.00	\$ -	\$ 79,224.00
Civil Engineer	\$ 333,079.00	\$ 75,123.64	\$ 257,955.36
Misc Consultants	\$ 61,911.00	\$ 43,439.98	\$ 18,471.02
Blueprints	\$ 10,000.00	\$ 2,679.59	\$ 7,320.41
Surveying/Layout	\$ 204,246.00	\$ 25,279.50	\$ 178,966.50
Permit Charges	\$ 1,512.00	\$ 1,512.00	\$ -
Impact Fees	\$ 1,957,676.00	\$ 1,755,599.55	\$ 202,076.45
Inspection Fees/Plan Check	\$ 696,858.00	\$ 652,841.73	\$ 44,016.27
Water/Sewer/Storm Fees	\$ 3,620,008.32	\$ 1,134,781.12	\$ 2,485,227.20
Reimbursement Fee Credits	\$ (5,577,684.32)	\$ -	\$ (5,577,684.32)
Reimbursement Structural Costs	\$ (18,734,064.00)	\$ -	\$ (18,734,064.00)
Legal Fees - CFD	\$ 15,000.00	\$ 12,076.15	\$ 2,923.85
Sanitary Sewer	\$ 1,819,074.02	\$ 1,634,499.54	\$ 184,574.48
Water Mains	\$ 7,648,940.00	\$ 3,273,875.68	\$ 4,375,064.32
Storm Drain	\$ 1,994,917.00	\$ 1,686,195.42	\$ 308,721.58
Electrical Underground/Overhead	\$ 16,556.46	\$ 16,556.46	\$ -
Street Name Signs	\$ 330,000.00	\$ -	\$ 330,000.00
Common Area Landscape	\$ 6,200.00	\$ -	\$ 6,200.00
Contingency Reserve	\$ 2,108,510.20	\$ -	\$ 2,108,510.20
Development Cost Reimbursements	\$ -	\$ -	\$ -
Total	\$ (3,403,691.32)	\$ 10,318,805.36	\$ (13,722,496.68)

ROSETTA II - TRACTS 25476 & 25477
 CFD BUDGET: 08/02/06

ITEM	BUDGET AMOUNT	COST SPENT TO DATE	COST TO GO
Purchase of Easement	\$ 4,345.00	\$ 4,345.00	\$ -
Geotechnical Consultant	\$ 79,224.00	\$ -	\$ 79,224.00
Civil Engineer	\$ 333,079.00	\$ 75,123.64	\$ 257,955.36
Misc Consultants	\$ 61,911.00	\$ 43,439.98	\$ 18,471.02
Blueprints	\$ 10,000.00	\$ 2,679.59	\$ 7,320.41
Surveying/Layout	\$ 204,246.00	\$ 25,279.50	\$ 178,966.50
Permit Charges	\$ 1,512.00	\$ 1,512.00	\$ -
Impact Fees	\$ 1,957,676.00	\$ 1,755,599.55	\$ 202,076.45
Inspection Fees/Plan Check	\$ 696,858.00	\$ 652,841.73	\$ 44,016.27
Water/Sewer/Storm Fees -	\$ 3,620,008.32	\$ 1,134,781.12	\$ 2,485,227.20
Reimbursement Fee Credits	\$ (5,577,684.32)	\$ -	\$ (5,577,684.32)
Reimbursement Structural Costs	\$ (18,734,064.00)	\$ -	\$ (18,734,064.00)
Legal Fees - CFD	\$ 15,000.00	\$ 12,076.15	\$ 2,923.85
Sanitary Sewer	\$ 1,819,074.02	\$ 1,634,499.54	\$ 184,574.48
Water Mains	\$ 7,648,940.00	\$ 3,273,875.68	\$ 4,375,064.32
Storm Drain	\$ 1,994,917.00	\$ 1,686,195.42	\$ 308,721.58
Electrical Underground/Overhead	\$ 16,556.46	\$ 16,556.46	\$ -
Street Name Signs	\$ 330,000.00	\$ -	\$ 330,000.00
Common Area Landscape	\$ 6,200.00	\$ -	\$ 6,200.00
Contingency Reserve	\$ 2,108,510.20	\$ -	\$ 2,108,510.20
Development Cost Reimbursements	\$ -	\$ -	\$ -
Total	\$ (3,403,691.32)	\$ 10,318,805.36	\$ (13,722,496.68)

APPENDIX E
RATE AND METHOD OF APPORTIONMENT

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**RATE AND METHOD OF APPORTIONMENT FOR
CITY OF LAKE ELSINORE COMMUNITY FACILITIES DISTRICT No. 2004-3
IMPROVEMENT AREA No. 2 (ROSETTA CANYON)**

A Special Tax shall be levied on all Assessor's Parcels in City of Lake Elsinore Community Facilities District No. 2004-3 (Improvement Area No. 2) (Rosetta Canyon) ("CFD No. 2004-3 (IA No. 2)") and collected each Fiscal Year commencing in Fiscal Year 2005-2006, in an amount determined through the application of the Rate and Method of Apportionment as described below. All of the real property in CFD No. 2004-3 (IA No. 2), unless exempted by law or by the provisions hereof, shall be taxed for the purposes, to the extent and in the manner herein provided.

A. DEFINITIONS

The terms hereinafter set forth have the following meanings:

"Acre or Acreage" means the land area of an Assessor's Parcel as shown on an Assessor's Parcel Map, or if the land area is not shown on an Assessor's Parcel Map, the land area shown on the applicable final map, parcel map, condominium plan, or other recorded County parcel map.

"Act" means the Mello-Roos Community Facilities Act of 1982, being Chapter 2.5, Division 2 of Title 5 of the California Government Code.

"Administrative Expenses" means the following actual or reasonably estimated costs directly related to the administration of CFD No. 2004-3 (IA No. 2): the costs of computing the Special Taxes and preparing the annual Special Tax collection schedules (whether by the City or designee thereof or both); the costs of collecting the Special Taxes (whether by the City or otherwise); the costs of remitting the Special Taxes to the Trustee; the costs of the Trustee (including its legal counsel) in the discharge of the duties required of it under the Indenture; the costs to the City, CFD No. 2004-3 (IA No. 2) or any designee thereof of complying with arbitrage rebate requirements; the costs to the City, CFD No. 2004-3 (IA No. 2) or any designee thereof of complying with disclosure requirements of the City, CFD No. 2004-3 (IA No. 2) or obligated persons associated with applicable federal and state securities laws and the Act; the costs associated with preparing Special Tax disclosure statements and responding to public inquiries regarding the Special Taxes; the costs of the City, CFD No. 2004-3 (IA No. 2) or any designee thereof related to an appeal of the Special Tax; the costs associated with the release of funds from an escrow account; and the City's annual administration fees and third party expenses. Administrative Expenses shall also include amounts estimated by the CFD Administrator or advanced by the City or CFD No. 2004-3 (IA No. 2) for any other administrative purposes of CFD No. 2004-3 (IA No. 2), including attorney's fees and other costs related to commencing and pursuing to completion any foreclosure of delinquent Special Taxes.

"Assessor's Parcel" means a lot or parcel shown in an Assessor's Parcel Map with an assigned Assessor's Parcel number.

"Assessor's Parcel Map" means an official map of the County Assessor of the County designating parcels by Assessor's Parcel number.

"Assigned Special Tax" means the Special Tax for each Land Use Class of Developed Property in each Zone, as determined in accordance with Section C.1.b. below.

"Authorized Facilities" means those authorized improvements, as listed on Exhibit "A" to the Resolution of Formation.

"Backup Special Tax" means the Special Tax applicable to each Assessor's Parcel of Developed Property, as determined in accordance with Section C.1.d. below.

"CFD Administrator" means an official of the City, or designee thereof, responsible for determining the Special Tax Requirement and providing for the levy and collection of the Special Taxes.

"CFD No. 2004-3" means City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon).

"CFD No. 2004-3 (IA No. 2)" means Improvement Area No. 2 of CFD No. 2004-3, as identified on the boundary map for CFD No. 2004-3.

"CFD No. 2004-3 (IA No. 2) Bonds" means any bonds or other debt (as defined in Section 53317(d) of the Act), whether in one or more series, issued by CFD No. 2004-3 and secured solely by Special Taxes levied on property within the boundaries of CFD No. 2004-3 (IA No. 2) under the Act.

"City" means the City of Lake Elsinore.

"City Council" means the City Council of the City of Lake Elsinore, acting as the legislative body of CFD No. 2004-3 (IA No. 2).

"County" means the County of Riverside.

"Developed Property" means, for each Fiscal Year, all Taxable Property, exclusive of Taxable Public Property and Taxable Property Owner Association Property, for which the Final Subdivision was recorded on or before January 1 of the prior Fiscal Year and a building permit for new construction was issued after January 1, 2004 and on or before May 1 of the Fiscal Year preceding the Fiscal Year for which the Special Taxes are being levied.

"Final Subdivision" means a subdivision of property by recordation of a final map, parcel map, or lot line adjustment, pursuant to the Subdivision Map Act (California Government Code Section 66410 et seq.) or recordation of a condominium plan pursuant to California Civil Code 1352 that creates individual lots for which building permits may be issued without further subdivision.

"Fiscal Year" means the period starting July 1 and ending on the following June 30.

"Indenture" means the indenture, fiscal agent agreement, resolution or other instrument pursuant to which CFD No. 2004-3 (IA No. 2) Bonds are issued, as modified, amended and/or supplemented from time to time, and any instrument replacing or supplementing the same.

"Land Use Class" means any of the classes listed in Table 1.

"Maximum Special Tax" means the maximum Special Tax, determined in accordance with Section C below, that can be levied in any Fiscal Year on any Assessor's Parcel.

"Non-Residential Property" means all Assessor's Parcels of Developed Property for which a building permit permitting the construction of one or more non-residential units or facilities has been issued by the City.

"Outstanding Bonds" means all CFD No. 2004-3 (IA No. 2) Bonds which are deemed to be outstanding under the Indenture.

"Property Owner Association Property" means, for each Fiscal Year, any property within the boundaries of CFD No. 2004-3 (IA No. 2) that was owned by a property owner association, including any master or sub-association, as of January 1 of the prior Fiscal Year.

"Proportionately" means for Developed Property that the ratio of the actual Special Tax levy to the Assigned Special Tax is equal for all Assessor's Parcels of Developed Property, or where the Backup Special Tax is being levied, that the ratio of the actual Special Tax levy to the Maximum Special Tax is equal for all Assessor's Parcels upon which a Backup Special Tax is being levied. For Undeveloped Property, "Proportionately" means that the ratio of the actual Special Tax levy per Acre to the Maximum Special Tax per Acre is equal for all Assessor's Parcels of Undeveloped Property. The term "Proportionately" may similarly be applied to other categories of Taxable Property as listed in Section D below.

"Public Property" means property within the boundaries of CFD No. 2004-3 (IA No. 2) owned by, irrevocably offered or dedicated to, or over, through or under which an easement for purposes of public right-of-way has been granted, to the federal government, the State, the County, the City, or any local government or other public agency, provided that any property leased by a public agency to a private entity and subject to taxation under Section 53340.1 of the Act shall be taxed and classified according to its use.

"Residential Floor Area" means all of the square footage of living area within the perimeter of a residential structure, not including any carport, walkway, garage, overhang, patio, enclosed patio, or similar area. The determination of Residential Floor Area for an Assessor's Parcel shall be made by reference to the building permit(s) issued for such Assessor's Parcel.

"Residential Property" means all Assessor's Parcels of Developed Property for which a building permit permitting the construction thereon of one or more residential dwelling units has been issued by the City.

"Resolution of Formation" means the Resolution of Formation for CFD No. 2004-3 (IA No. 2).

"Special Tax" means the special tax to be levied in each Fiscal Year on each Assessor's Parcel of Developed Property, Taxable Property Owner Association Property, Taxable Public Property, and Undeveloped Property to fund the Special Tax Requirement.

"Special Tax Requirement" means that amount required in any Fiscal Year for CFD No. 2004-3 (IA No. 2) to: (i) pay debt service on all Outstanding Bonds due in the calendar year commencing in such Fiscal Year; (ii) pay periodic costs on the CFD No. 2004-3 (IA No. 2) Bonds, including but not limited to, credit enhancement and rebate payments on the CFD No. 2004-3 (IA No. 2) Bonds due in the calendar year commencing in such Fiscal Year; (iii) pay Administrative Expenses; (iv) pay any amounts required to establish or replenish any reserve funds for all Outstanding Bonds; (v) pay for reasonably anticipated Special Tax delinquencies based on the delinquency rate for the Special Tax levy in the previous Fiscal Year; (vi) pay directly for acquisition or construction of Authorized Facilities to the extent that the inclusion of such amount does not increase the Special Tax levy on Undeveloped Property; less (vii) a credit for funds available to reduce the annual Special Tax levy, as determined by the CFD Administrator pursuant to the Indenture.

"State" means the State of California.

"Taxable Property" means all of the Assessor's Parcels within the boundaries of CFD No. 2004-3 (IA No. 2) which are not exempt from the Special Tax pursuant to law or Section E below.

"Taxable Property Owner Association Property" means all Assessor's Parcels of Property Owner Association Property that are not exempt pursuant to Section E below.

"Taxable Public Property" means all Assessor's Parcels of Public Property that are not exempt pursuant to Section E below.

"Trustee" means the trustee, fiscal agent, or paying agent under the Indenture.

"Undeveloped Property" means, for each Fiscal Year, all Taxable Property not classified as Developed Property, Taxable Property Owner Association Property, or Taxable Public Property.

"Zone" means Zone 1 or Zone 2, as applicable.

"Zone 1" means the land geographically identified within the boundaries of zone 1 as delineated in Exhibit A to this Rate and Method of Apportionment.

"Zone 2" means the land geographically identified within the boundaries of zone 2 as delineated in Exhibit A to this Rate and Method of Apportionment.

B. ASSIGNMENT TO LAND USE CATEGORIES

Each Fiscal Year, all Taxable Property within CFD No. 2004-3 (IA No. 2) shall be assigned to a Zone and further classified as Developed Property, Taxable Public Property, Taxable Property Owner Association Property, or Undeveloped Property, and shall be subject to Special Taxes in accordance with this Rate and Method of Apportionment determined pursuant to Sections C and D below. Residential Property shall be assigned to Land Use Classes 1 through 11 as listed in Table 1 below based on the Residential Floor Area for each unit. Non-Residential Property shall be assigned to Land Use Class 12.

C. MAXIMUM SPECIAL TAX RATE

1. Developed Property

a. Maximum Special Tax

The Maximum Special Tax for each Assessor's Parcel classified as Developed Property shall be the greater of (i) the amount derived by application of the Assigned Special Tax or (ii) the amount derived by application of the Backup Special Tax.

b. Assigned Special Tax

The Assigned Special Tax for each Land Use Class is shown below in Table 1.

TABLE 1

**Assigned Special Taxes for Developed Property
Community Facilities District No. 2004-3
Improvement Area No. 2
Fiscal Year 2005-2006**

Land Use Class	Description	Residential Floor Area	Zone 1 Assigned Special Tax	Zone 2 Assigned Special Tax
1	Residential Property	> 3,950 s.f.	\$3,271.79 per unit	\$3,565.47 per unit
2	Residential Property	3,701 – 3,950 s.f.	\$3,174.02 per unit	\$3,504.87 per unit
3	Residential Property	3,451 – 3,700 s.f.	\$3,076.25 per unit	\$3,443.77 per unit
4	Residential Property	3,201 – 3,450 s.f.	\$2,978.48 per unit	\$3,290.64 per unit
5	Residential Property	2,951 – 3,200 s.f.	\$2,880.71 per unit	\$3,172.60 per unit
6	Residential Property	2,701 – 2,950 s.f.	\$2,727.85 per unit	\$3,055.06 per unit
7	Residential Property	2,451 – 2,700 s.f.	\$2,659.26 per unit	\$2,975.78 per unit
8	Residential Property	2,201 – 2,450 s.f.	\$2,590.67 per unit	\$2,844.10 per unit
9	Residential Property	1,951 – 2,200 s.f.	\$2,411.94 per unit	\$2,770.55 per unit
10	Residential Property	1,700 – 1,950 s.f.	\$2,353.03 per unit	\$2,688.11 per unit
11	Residential Property	< 1,700 s.f.	\$2,294.11 per unit	\$2,590.62 per unit
12	Non-Residential Property	NA	\$17,817 per Acre	\$16,754 per Acre

c. Increase in the Assigned Special Tax

The Assigned Special Taxes identified in Table 1 above shall be applicable for Fiscal Year 2005-2006, and shall increase thereafter, commencing on July 1, 2006 and on July 1 of each Fiscal Year thereafter, by an amount equal to two percent (2%) of the Assigned Special Tax for the previous Fiscal Year.

d. Backup Special Tax

The Fiscal Year 2005-2006 Backup Special Tax attributable to a Final Subdivision in Zone 1 or Zone 2 will equal \$19,868 multiplied by the Acreage of all Taxable Property, exclusive of any Taxable Property Owner Association Property and Taxable Public Property, therein. The Backup Special Tax for each Assessor's Parcel of Residential Property shall be computed by dividing the Backup Special Tax attributable to the applicable Final Subdivision by the number of Assessor's Parcels for which building permits for residential construction have or may be issued (i.e., the number or

residential lots). The Backup Special Tax for each Assessor's Parcel of Non-Residential Property therein shall equal \$19,868 multiplied by the Acreage of such Assessor's Parcel.

If a Final Subdivision includes Assessor's Parcels of Taxable Property for which building permits for both residential and non-residential construction may be issued, exclusive of Taxable Property Owner Association Property and Taxable Public Property, then the Backup Special Tax for each Assessor's Parcel of Residential Property shall be computed exclusive of the Acreage and Assessor's Parcels of property for which building permits for non-residential construction may be issued.

Notwithstanding the foregoing, if all or any portion of the Final Subdivision(s) described in the preceding paragraphs is subsequently changed or modified, then the Backup Special Tax for each Assessor's Parcel of Developed Property in such Final Subdivision area that is changed or modified shall be a rate per square foot of Acreage calculated as follows:

1. Determine the total Backup Special Taxes anticipated to apply to the changed or modified Final Subdivision area prior to the change or modification.
2. The result of paragraph 1 above shall be divided by the Acreage of Taxable Property which is ultimately expected to exist in such changed or modified Final Subdivision area, as reasonably determined by the CFD Administrator.
3. The result of paragraph 2 above shall be divided by 43,560. The result is the Backup Special Tax per square foot of Acreage which shall be applicable to Assessor's Parcels of Developed Property in such changed or modified Final Subdivision area for all remaining Fiscal Years in which the Special Tax may be levied.

i. Release of Obligation to Pay and Disclose Backup Special Tax

All Assessors' Parcels within CFD No. 2004-3 (IA No. 2) will be relieved simultaneously and permanently from the obligation to pay and disclose the Backup Special Tax if the CFD Administrator determines that the annual debt service required for the Outstanding Bonds, when compared to the Assigned Special Taxes that may be levied against all Assessors' Parcels of Developed Property result in 110% debt service coverage (i.e., the Assigned Special Taxes that may be levied against all Developed Property in each remaining Fiscal Year based on then existing development in CFD No. 2004-3 (IA No. 2) is at least equal to the sum of (i) the Administrative

Expenses and (ii) 1.10 times maximum annual debt service, in each remaining Fiscal Year on the Outstanding Bonds).

e. Increase in the Backup Special Tax

On each July 1, commencing on July 1, 2006, the Backup Special Tax shall be increased by an amount equal to two percent (2%) of the Backup Special Tax for the previous Fiscal Year.

f. Multiple Land Use Classes

In some instances an Assessor's Parcel of Developed Property may contain more than one Land Use Class. The Maximum Special Tax levied on an Assessor's Parcel shall be the sum of the Maximum Special Tax for all Land Use Classes located on that Assessor's Parcel. The CFD Administrator's allocation to each type of property shall be final.

2. Taxable Property Owner Association Property, Taxable Public Property, and Undeveloped Property

The Fiscal Year 2005-2006 Maximum Special Tax for Taxable Property Owner Association Property, Taxable Public Property, and Undeveloped Property in Zone 1 or Zone 2 shall be \$19,868 per Acre, and shall increase thereafter, commencing on July 1, 2006 and on July 1 of each Fiscal Year thereafter, by an amount equal to two percent (2%) of the Maximum Special Tax for the previous Fiscal Year.

D. METHOD OF APPORTIONMENT OF THE SPECIAL TAX

Commencing with Fiscal Year 2005-2006 and for each following Fiscal Year, the City Council shall levy the Special Tax until the amount of Special Taxes levied equals the Special Tax Requirement. The Special Tax shall be levied each Fiscal Year as follows:

First: The Special Tax shall be levied on each Assessor's Parcel of Developed Property in Zone 1 and Zone 2 in an amount equal to 100% of the applicable Assigned Special Tax;

Second: If additional monies are needed to satisfy the Special Tax Requirement after the first step has been completed, the Special Tax shall be levied Proportionately on each Assessor's Parcel of Undeveloped Property in Zone 1 and Zone 2 at up to 100% of the applicable Maximum Special Tax for Undeveloped Property;

Third: If additional monies are needed to satisfy the Special Tax Requirement after the first two steps have been completed, then the levy of the Special Tax on each Assessor's Parcel of Developed Property in Zone 1 and Zone 2 whose Maximum Special Tax is determined through the application of the Backup Special Tax shall be increased Proportionately from the Assigned Special Tax up to the Maximum Special Tax for each such Assessor's Parcel;

Fourth: If additional monies are needed to satisfy the Special Tax Requirement after the first three steps have been completed, then the Special Tax shall be levied Proportionately on each Assessor's Parcel of Taxable Property Owner Association Property and Taxable Public Property in Zone 1 and Zone 2 at up to the applicable Maximum Special Tax for Taxable Property Owner Association Property or Taxable Public Property.

Notwithstanding the above the City Council may, in any Fiscal Year, levy Proportionately less than 100% of the Assigned Special Tax in step one (above), when (i) the City Council is no longer required to levy the Special Tax pursuant to steps two through four above in order to meet the Special Tax Requirement; and (ii) all authorized CFD No. 2004-3 (IA No. 2) Bonds have already been issued or the City Council has covenanted that it will not issue any additional CFD No. 2004-3 (IA No. 2) Bonds (except refunding bonds) to be supported by the Special Tax.

Further notwithstanding the above, under no circumstances will the Special Tax levied against any Assessor's Parcel of Residential Property for which an occupancy permit for private residential use has been issued be increased by more than ten percent as a consequence of delinquency or default by the owner of any other Assessor's Parcel within CFD No. 2004-3 (IA No. 2).

E. EXEMPTIONS

The City shall classify Property Owner Association Property and/or Public Property in CFD No. 2004-3 (IA No. 2) as exempt property, provided that no such classification would reduce the Acreage of all Taxable Property to less than 75.86 Acres. Tax-exempt status will be assigned by the CFD Administrator in the chronological order in which property becomes Property Owner Association Property or Public Property. However, should an Assessor's Parcel no longer be classified as Property Owner Association Property or Public Property, its tax-exempt status will be revoked.

Property Owner Association Property or Public Property that is not exempt from Special Taxes under this section shall be subject to the levy of the Special Tax and shall be taxed Proportionately as part of the fourth step in Section D above, at up to 100% of the applicable Maximum Special Tax for Taxable Property Owner Association Property or Taxable Public Property.

F. MANNER OF COLLECTION

The Special Tax shall be collected in the same manner and at the same time as ordinary *ad valorem* property taxes; provided, however, that CFD No. 2004-3 (IA No. 2) may directly bill the Special Tax, may collect Special Taxes at a different time or in a different manner if necessary to meet its financial obligations, and may covenant to foreclose and may actually foreclose on delinquent Assessor's Parcels as permitted by the Act.

G. APPEALS

Any landowner or resident who feels that the amount of the Special Tax levied on their Assessor's Parcel is in error may submit a written appeal to CFD No. 2004-3 (IA No. 2). The CFD Administrator shall review the appeal and if the CFD Administrator concurs, the amount of the Special Tax levied shall be appropriately modified.

The City Council may interpret this Rate and Method of Apportionment for purposes of clarifying any ambiguity and make determinations relative to the annual administration of the Special Tax and any landowner or resident appeals. Any decision of the City Council shall be final and binding as to all persons.

H. PREPAYMENT OF SPECIAL TAX

The following definitions apply to this Section H:

"Buildout" means, for CFD No. 2004-3 (IA No. 2), that all expected building permits have been issued.

"CFD Public Facilities" means either \$27,000,000 in 2006 dollars, which shall increase by the Construction Inflation Index on July 1, 2007, and on each July 1 thereafter, or such lower number as (i) shall be determined by the CFD Administrator as sufficient to provide the public facilities to be provided by CFD No. 2004-3 (IA No. 2) under the authorized bonding program for CFD No. 2004-3 (IA No. 2), or (ii) shall be determined by the City Council concurrently with a covenant that it will not issue any more CFD No. 2004-3 (IA No. 2) Bonds (except refunding bonds) to be supported by the Special Taxes levied under this Rate and Method of Apportionment as described in Section D.

"Construction Inflation Index" means the annual percentage change in the Engineering News Record Building Cost Index for the City of Los Angeles, measured as of the calendar year which ends in the previous Fiscal Year. In the event this index ceases to be published, the Construction Inflation Index shall be another index as determined by the CFD Administrator that is reasonably comparable to the Engineering News Record Building Cost Index for the City of Los Angeles.

"Future Facilities Costs" means the CFD Public Facilities minus (i) public facility costs previously paid from the Improvement Fund, (ii) moneys currently on deposit in the Improvement Fund, and (iii) moneys currently on deposit in an escrow fund that are expected to be available to finance the cost of CFD Public Facilities.

"Improvement Fund" means an account specifically identified in the Indenture to hold funds which are currently available for expenditure to acquire or construct CFD Public Facilities eligible under the Act.

"Previously Issued Bonds" means, for any Fiscal Year, all Outstanding Bonds that are deemed to be outstanding under the Indenture after the first interest and/or principal payment date following the current Fiscal Year.

1. Prepayment in Full

Only an Assessor's Parcel of Developed Property, or Undeveloped Property for which a building permit has been issued, may be prepaid. The obligation of the Assessor's Parcel to pay any Special Tax may be permanently satisfied as described herein, provided that a prepayment may be made with respect to a particular Assessor's Parcel only if there are no delinquent Special Taxes with respect to such Assessor's Parcel at the time of prepayment. An owner of an Assessor's Parcel intending to prepay the Special Tax obligation shall provide the CFD Administrator with written notice of intent to prepay. Within 30 days of receipt of such written notice, the CFD Administrator shall notify such owner of the prepayment amount for such Assessor's Parcel. The CFD Administrator may charge a reasonable fee for providing this service. Prepayment must be made not less than 45 days prior to the next occurring date that notice of redemption of CFD No. 2004-3 (IA No. 2) Bonds from the proceeds of such prepayment may be given by the Trustee pursuant to the Indenture.

The Special Tax Prepayment Amount (defined below) shall be calculated as summarized below (capitalized terms as defined below):

	Bond Redemption Amount
plus	Redemption Premium
plus	Future Facilities Amount
plus	Defeasance Amount
plus	Administrative Fees and Expenses
less	Reserve Fund Credit
less	<u>Capitalized Interest Credit</u>
Total: equals	Prepayment Amount

As of the proposed date of prepayment, the Special Tax Prepayment Amount shall be calculated as follows:

Paragraph No.:

1. Confirm that no Special Tax delinquencies apply to such Assessor's Parcel.
2. For Assessor's Parcels of Developed Property, compute the Assigned Special Tax and Backup Special Tax. For Assessor's Parcels of Undeveloped Property for which a building permit has been issued, compute the Assigned Special Tax and Backup Special Tax for that Assessor's Parcel as though it was already designated as Developed Property, based upon the building permit which has already been issued for that Assessor's Parcel.

3. (a) Divide the Assigned Special Tax computed pursuant to paragraph 2 by the total estimated Assigned Special Taxes for the entire CFD No. 2004-3 (IA No. 2) based on the Developed Property Special Taxes which could be levied in the current Fiscal Year on all expected development through Buildout of CFD No. 2004-3 (IA No. 2), excluding any Assessor's Parcels which have been prepaid, and

(b) Divide the Backup Special Tax computed pursuant to paragraph 2 by the total estimated Backup Special Taxes at Buildout for the entire CFD No. 2004-3 (IA No. 2), excluding any Assessor's Parcels which have been prepaid.
4. Multiply the larger quotient computed pursuant to paragraph 3(a) or 3(b) by the Previously Issued Bonds to compute the amount of Previously Issued Bonds to be retired and prepaid (the "*Bond Redemption Amount*").
5. Multiply the Bond Redemption Amount computed pursuant to paragraph 4 by the applicable redemption premium (e.g., the redemption price-100%), if any, on the Previously Issued Bonds to be redeemed (the "*Redemption Premium*").
6. Compute the current Future Facilities Costs.
7. Multiply the larger quotient computed pursuant to paragraph 3(a) or 3(b) by the amount determined pursuant to paragraph 6 to compute the amount of Future Facilities Costs to be prepaid (the "*Future Facilities Amount*").
8. Compute the amount needed to pay interest on the Bond Redemption Amount from the first bond interest and/or principal payment date following the current Fiscal Year until the earliest redemption date for the Previously Issued Bonds.
9. Determine the Special Tax levied on the Assessor's Parcel in the current Fiscal Year which has not yet been paid.
10. Compute the minimum amount the CFD Administrator reasonably expects to derive from the reinvestment of the Special Tax Prepayment Amount less the Future Facilities Amount and the Administrative Fees and Expenses (defined below) from the date of prepayment until the redemption date for the Previously Issued Bonds to be redeemed with the prepayment.
11. Add the amounts computed pursuant to paragraphs 8 and 9 and subtract the amount computed pursuant to paragraph 10 (the "*Defeasance Amount*").
12. The administrative fees and expenses of CFD No. 2004-3 (IA No. 2) are as calculated by the CFD Administrator and include the costs of computation of the prepayment, the costs to invest the prepayment proceeds, the costs of redeeming CFD No. 2004-3

(IA No. 2) Bonds, and the costs of recording any notices to evidence the prepayment and the redemption (the "*Administrative Fees and Expenses*").

13. The reserve fund credit (the "*Reserve Fund Credit*") shall equal the lesser of: (a) the expected reduction in the reserve requirement (as defined in the Indenture), if any, associated with the redemption of Previously Issued Bonds as a result of the prepayment, or (b) the amount derived by subtracting the new reserve requirement (as defined in the Indenture) in effect after the redemption of Previously Issued Bonds as a result of the prepayment from the balance in the reserve fund on the prepayment date, but in no event shall such amount be less than zero. No Reserve Fund Credit shall be granted if the amount then on deposit in the reserve fund for the Previously Issued Bonds is below 100% of the reserve requirement (as defined in the Indenture).
14. If any capitalized interest for the Previously Issued Bonds will not have been expended as of the date immediately following the first interest and/or principal payment following the current Fiscal Year, a capitalized interest credit shall be calculated by multiplying the larger quotient computed pursuant to paragraph 3(a) or 3(b) by the expected balance in the capitalized interest fund or account under the Indenture after such first interest and/or principal payment (the "*Capitalized Interest Credit*").
15. The Special Tax prepayment is equal to the sum of the amounts computed pursuant to paragraphs 4, 5, 7, 11 and 12, less the amounts computed pursuant to paragraphs 13 and 14 (the "*Prepayment Amount*").

From the Prepayment Amount, the amounts computed pursuant to paragraphs 4, 5, 11, 13 and 14 shall be deposited into the appropriate fund as established under the Indenture and be used to retire CFD No. 2004-3 (IA No. 2) Bonds or make debt service payments. The amount computed pursuant to paragraph 7 shall be deposited into the Improvement Fund. The amount computed pursuant to paragraph 12 shall be retained by CFD No. 2004-3 (IA No. 2).

The Special Tax Prepayment Amount may be insufficient to redeem a full \$5,000 increment of CFD No. 2004-3 (IA No. 2) Bonds. In such cases, the increment above \$5,000 or integral multiple thereof will be retained in the appropriate fund established under the Indenture to be used with the next prepayment of CFD No. 2004-3 (IA No. 2) Bonds or to make debt service payments.

As a result of the payment of the current Fiscal Year's Special Tax levy as determined under paragraph 9 (above), the CFD Administrator shall remove the current Fiscal Year's Special Tax levy for such Assessor's Parcel from the County tax rolls. With respect to any Assessor's Parcel that is prepaid, the City Council shall cause a suitable notice to be recorded in compliance with the Act, to indicate the prepayment of the Special Tax and the release of the Special Tax lien on such Assessor's Parcel, and the obligation of such Assessor's Parcel to pay the Special Tax shall cease.

Notwithstanding the foregoing, no Special Tax prepayment shall be allowed unless, at the time of such proposed prepayment, the amount of Maximum Special Taxes that may be levied on Taxable Property within CFD No. 2004-3 (IA No. 2) both prior to and after the proposed prepayment is at least equal to the sum of (i) the Administrative Expenses and (ii) 1.10 times maximum annual debt service, in each remaining Fiscal Year on the Outstanding Bonds.

2. Prepayment in Part

The Special Tax on an Assessor's Parcel of Developed Property or an Assessor's Parcel of Undeveloped Property for which a building permit has been issued may be partially prepaid. The amount of the prepayment shall be calculated as in Section H.1; except that a partial prepayment shall be calculated according to the following formula:

$$PP = [(P_E - A) \times F] + A$$

These terms have the following meaning:

PP = the partial prepayment.

P_E = the Special Tax Prepayment Amount calculated according to Section H.1.

F = the percentage, expressed as a decimal, by which the owner of the Assessor's Parcel is partially prepaying the Special Tax.

A = the Administrative Fees and Expenses calculated according to Section H.1.

The owner of any Assessor's Parcel who desires such prepayment shall notify the CFD Administrator of such owner's intent to partially prepay the Special Tax and the percentage by which the Special Tax shall be prepaid. The CFD Administrator shall provide the owner with a statement of the amount required for the partial prepayment of the Special Tax for an Assessor's Parcel within 30 days of the request and may charge a reasonable fee for providing this service. With respect to any Assessor's Parcel that is partially prepaid, the City Council shall (i) distribute the funds remitted to it according to Section H.1, and (ii) indicate in the records of CFD No. 2004-3 (IA No. 2) that there has been a partial prepayment of the Special Tax and that a portion of the Special Tax with respect to such Assessor's Parcel, equal to the outstanding percentage (1.00 - F) of the remaining Maximum Special Tax, shall continue to be levied on such Assessor's Parcel pursuant to Section D.

I. TERM OF SPECIAL TAX

The Special Tax shall be levied for a period not to exceed forty years commencing with Fiscal Year 2005-2006, provided however that Special Taxes will cease to be levied in an earlier Fiscal Year if the CFD Administrator has determined (i) that all required interest and principal payments on the CFD No. 2004-3 (IA No. 2) Bonds have been paid; and (ii) all Authorized Facilities have been constructed.

**RATE AND METHOD OF APPORTIONMENT FOR
CITY OF LAKE ELSINORE COMMUNITY FACILITIES DISTRICT No. 2004-3
IMPROVEMENT AREA No. 2 (ROSETTA CANYON)**

EXHIBIT A

MAP OF ZONE 1 AND ZONE 2

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APPENDIX F

FORMS OF CONTINUING DISCLOSURE AGREEMENTS

CONTINUING DISCLOSURE AGREEMENT

(City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon))

This Continuing Disclosure Agreement (the “Disclosure Agreement”), dated as of September 1, 2006, is executed and delivered by the City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon) (the “CFD”) and Union Bank of California, N.A., as dissemination agent (the “Dissemination Agent”) hereunder, in connection with the issuance of the \$23,460,000 City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon) Special Tax Bonds (Improvement Area No. 2) 2006 Series A (the “Bonds”). The Bonds are being issued pursuant to provisions of a Fiscal Agent Agreement, dated as of September 1, 2006 (the “Fiscal Agent Agreement”), by and between the CFD and Union Bank of California, N.A., as fiscal agent (the “Fiscal Agent”). The CFD and the Dissemination Agent covenant and agree as follows:

SECTION 1. Purpose of the Disclosure Agreement. This Disclosure Agreement is being executed and delivered by the CFD, the Dissemination Agent and the Fiscal Agent 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 Fiscal Agent Agreement, which apply to any capitalized term used in this Disclosure Agreement unless otherwise defined in this Section, the following capitalized terms shall have the following meanings:

“Annual Report” shall mean any Annual Report or any addendum thereto provided by the CFD 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.

“CFD” means City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon), a community facilities district organized and existing under the laws of the State of California, and such area of land comprising that community facilities district.

“City” means the City of Lake Elsinore, California.

“Disclosure Representative” shall mean the Mayor of the City of Lake Elsinore or his or her designee, or such other officer or employee as the City Council of the City of Lake Elsinore

(the “Council”) shall designate in writing to the Fiscal Agent and Dissemination Agent from time to time.

“Dissemination Agent” shall mean the Fiscal Agent, acting in its capacity as Dissemination Agent hereunder, or any successor Dissemination Agent designated in writing by the CFD and which has filed with the Fiscal Agent 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. The National Repositories currently approved by the Securities and Exchange Commission are set forth in the SEC website located at <http://www.sec.gov>.

“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” shall mean the State of California.

“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 CFD shall, or shall cause the Dissemination Agent to, not later than 225 days after the end of the City’s fiscal year, commencing with fiscal year ending June 30, 2006, provide to each Repository and the Participating Underwriter an Annual Report which is consistent with the requirements of Section 4 of this Disclosure Agreement. The Annual Report may be provided in electronic format to each Repository and may be provided through the services of a “Central Post Office” approved by the Securities and Exchange Commission. 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 City’s Fiscal Year changes, it shall give notice of such change in the same manner as for a Listed Event under Section 5(f). Furthermore, upon receipt of a written request of any Beneficiary Owner, the Dissemination Agent shall provide a copy of the Annual Report to such Beneficial Owner.

(b) Not later than fifteen (15) Business Days prior to the date specified in subsection (a) for providing the Annual Report to Repositories, the CFD shall provide the Annual Report to the Dissemination Agent and the Fiscal Agent (if the Fiscal Agent is not the Dissemination

Agent). If by such date, the Dissemination Agent has not received a copy of the Annual Report, the Dissemination Agent shall notify the CFD and the Fiscal Agent of such failure to receive the Annual Report. The CFD shall provide a written certification with each Annual Report furnished to the Dissemination Agent and the Fiscal Agent to the effect that such Annual Report constitutes the Annual Report required to be furnished by it hereunder. The Dissemination Agent and Fiscal Agent may conclusively rely upon such certification of the CFD and shall have no duty or obligation to review such Annual Report.

(c) If the Dissemination Agent is unable to verify that an Annual Report has been provided to Repositories by the date required in subsection (a), the Dissemination Agent 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 CFD and (if the Dissemination Agent is not the Fiscal Agent) the Fiscal Agent 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 CFD's Annual Report shall contain or include by reference the following:

(i) The audited financial statements of the City, prepared in accordance with generally accepted accounting principles in effect from time to time. If the City's audited financial statements are not available by the time the Annual Report is required to be filed pursuant to Section 3(a), the Annual Report shall contain unaudited financial statements in a format similar to the financial statements contained in the Official Statement, and the audited financial statements shall be filed in the same manner as the Annual Report when they become available.

(ii) The balance in the Reserve Account held under the Fiscal Agent Agreement.

(iii) Total assessed valuation (per the Riverside County Assessor records) of all parcels currently subject to the Special Tax within Improvement Area No. 2 of the CFD, showing the total assessed valuation for all land and the total assessed valuation for all improvements within Improvement Area No. 2 of the CFD and distinguishing between the assessed value of developed property and undeveloped property.

(iv) Identification of each parcel within Improvement Area No. 2 of the CFD for which any Special Tax payment is delinquent, together with the following information respecting each such parcel: (A) the amount delinquent; (B) the date of each delinquency; (C) in the event a foreclosure complaint has been filed respecting such delinquent parcel and such complaint has not yet been dismissed, the date on which the complaint was filed; and (D) in the

event a foreclosure sale has occurred respecting such delinquent parcel, a summary of the results of such foreclosure sale.

(v) The number of certificates of occupancy issued by the City within Improvement Area No. 2 of the CFD and the principal amount of prepayments of the Special Tax with respect to the CFD for the prior Fiscal Year.

(vi) A land ownership summary listing property owners responsible for more than five percent (5%) of the annual Special Tax levy, as shown on the Riverside County Assessor's last equalized tax roll prior to the September next preceding the Annual Report date.

(vii) A description of the status of the facilities being constructed with proceeds of the Bonds as of the date of the Annual Report (but only so long as such facilities are not completed).

(viii) The number of building permits issued in Improvement Area No. 2 of the CFD during the prior Fiscal Year.

(ix) The amount of Special Taxes generated by the developed parcels and undeveloped parcels within Improvement Area No. 2 of the CFD.

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 City 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 CFD 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 CFD 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 Dissemination Agent 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 CFD promptly notify the Dissemination Agent in writing whether or not to report the event pursuant to subsection (f) and promptly direct the Fiscal Agent whether or not to report such event to the Bondholders. In the absence of such direction the Dissemination Agent shall not report such event unless otherwise required to be reported by the Fiscal Agent to the Bondholders under the Fiscal Agent Agreement. The Dissemination Agent 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 Fiscal Agent or the Dissemination Agent with regular responsibility for the administration of matters related to the Fiscal Agent Agreement. Neither the Fiscal Agent nor the Dissemination Agent shall have any responsibility to determine the materiality of any of the Listed Events.

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

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

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

(f) If the Dissemination Agent has been instructed by the CFD 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 Fiscal Agent Agreement.

SECTION 6. Termination of Reporting Obligation. The CFD’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

CFD shall give notice of such termination in the same manner as for a Listed Event under Section 5(f).

SECTION 7. Dissemination Agent. The CFD 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 CFD pursuant to this Disclosure Agreement. The initial Dissemination Agent shall be Union Bank of California, N.A. The Dissemination Agent may resign by providing thirty days written notice to the CFD and the Fiscal Agent. 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 CFD in a timely manner and in a form suitable for filing.

SECTION 8. Amendment; Waiver. Notwithstanding any other provision of this Disclosure Agreement, the CFD, Dissemination Agent and the Fiscal Agent may amend this Disclosure Agreement (and the Fiscal Agent and Dissemination Agent shall agree to any amendment so requested by the CFD) provided, neither the Fiscal Agent 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 Fiscal Agent Agreement for amendments to the Fiscal Agent Agreement with the consent of Holders, or (ii) does not, in the opinion of 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 CFD 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 CFD.

SECTION 9. Additional Information. Nothing in this Disclosure Agreement shall be deemed to prevent the CFD 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 CFD 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 CFD 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 CFD or the Dissemination Agent to comply with any provision of this Disclosure Agreement, the Fiscal Agent (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 Fiscal Agent 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 Fiscal Agent 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 CFD or Fiscal Agent, 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 Fiscal Agent Agreement, and the sole remedy under this Disclosure Agreement in the event of any failure of the CFD or the Fiscal Agent to comply with this Disclosure Agreement shall be an action to compel performance.

SECTION 11. Duties, Immunities and Liabilities of Fiscal Agent and Dissemination Agent. Article VII of the Fiscal Agent Agreement pertaining to the Fiscal Agent is hereby made applicable to this Disclosure Agreement as if this Disclosure Agreement were (solely for this purpose) contained in the Fiscal Agent Agreement and the Fiscal Agent and Dissemination Agent shall be entitled to the protections, limitations from liability and indemnities afforded the Fiscal Agent thereunder. The Dissemination Agent shall have only such duties as are specifically set forth in this Disclosure Agreement, and the CFD agrees to indemnify and save the Dissemination Agent, its officers, directors, employees and agents, harmless against any loss, expense and liabilities which they may incur arising out of or in the exercise or performance of its powers and duties hereunder, including the costs and expenses (including attorneys fees) of defending against any claim of liability, but excluding liabilities due to the Dissemination Agent's negligence or willful misconduct. The Dissemination Agent shall be paid compensation by the CFD for its services provided hereunder in accordance with its schedule of fees as amended from time to time and all expenses, legal fees and advances made or incurred by the Dissemination Agent in the performance of its duties hereunder. The Dissemination Agent shall have no duty or obligation to review any information provided to them hereunder and shall not be deemed to be acting in any fiduciary capacity for the CFD, the Bondholders, or any other party. The Dissemination Agent shall have no liability to the Bondholders or any other party for any monetary damages or financial liability of any kind whatsoever related to or arising from this Agreement. The obligations of the CFD under this Section shall survive resignation or removal of the Dissemination Agent and payment of the Bonds.

SECTION 12. Notices. Any notices or communications to or among any of the parties to this Disclosure Agreement may be given as follows:

To the City: City of Lake Elsinore
130 South Main Street
Lake Elsinore, California 92530
Attn: City Manager
Fax: (951) 674-3124

To the Fiscal Agent: Union Bank of California, N.A.
120 South San Pedro Street, Suite 400
Los Angeles, California 90012
Attn: Corporate Trust Department
Fax: (213) 972-5676
Fax: (213) 972-5694

Any person may, by written notice to the other persons listed above, designate a different address or telephone number(s) to which subsequent notices or communications should be sent.

SECTION 13. Beneficiaries. This Disclosure Agreement shall inure solely to the benefit of the CFD, the Fiscal Agent, the Dissemination Agent, the Participating Underwriter and Holders and Beneficial Owners from time to time of the Bonds, and shall create no rights in any other person or entity.

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.

CITY OF LAKE ELSINORE COMMUNITY
FACILITIES DISTRICT NO. 2004-3
(ROSETTA CANYON)

By _____
City Manager of the City of Lake Elsinore

UNION BANK OF CALIFORNIA, N.A., as
Dissemination Agent and Fiscal Agent

By _____
Authorized Officer

EXHIBIT A

NOTICE TO REPOSITORIES OF FAILURE TO FILE ANNUAL REPORT

Name of Obligated Party: City of Lake Elsinore
Community Facilities District No. 2004-3 (Rosetta Canyon)

Name of Bond Issue: City of Lake Elsinore
Community Facilities District No. 2004-3 (Rosetta Canyon)
Special Tax Bonds (Improvement Area No. 2) 2006 Series A

Date of Issuance: September 19, 2006

NOTICE IS HEREBY GIVEN that the CFD has not provided an Annual Report with respect to the above-named Bonds as required by the Continuing Disclosure Agreement, dated as of September 1, 2006, with respect to the Bonds. The CFD anticipates that the Annual Report will be filed by _____.

Dated: _____

UNION BANK OF CALIFORNIA, N.A.,
on behalf of CFD

cc: Issuer

DEVELOPER CONTINUING DISCLOSURE AGREEMENT
(Centex Homes)

This Developer Continuing Disclosure Agreement (the “Disclosure Agreement”), dated as of September 1, 2006, is executed and delivered by Centex Homes, a Nevada general partnership (the “Property Owner”) and Union Bank of California, N.A., as dissemination agent (the “Dissemination Agent”), in connection with the issuance of the \$23,460,000 City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon) Special Tax Bonds (Improvement Area No. 2) 2006 Series A (the “Bonds”). The Bonds are being issued pursuant to provisions of a Fiscal Agent Agreement, dated as of September 1, 2006 (the “Fiscal Agent Agreement”), by and between the City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon) (the “Issuer”) and Union Bank of California, N.A. as fiscal agent (the “Fiscal Agent”). The Property Owner and the Dissemination Agent covenant and agree as follows:

SECTION 1. Purpose of the Disclosure Agreement. This Disclosure Agreement is being executed and delivered by the Property Owner and the Dissemination Agent 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 Fiscal Agent Agreement, which apply to any capitalized term used in this Disclosure Agreement unless otherwise defined in this Section, the following capitalized terms shall have the following meanings:

“Affiliate” of another Person means (a) a Person directly or indirectly owning, controlling, or holding with power to vote, five percent (5%) or more of the outstanding voting securities of such other Person, (b) any Person whose outstanding voting securities of five percent (5%) or more are directly or indirectly owned, controlled, or held with power to vote, by such other Person, and (c) any Person directly or indirectly controlling, controlled by, or under common control with, such other Person; for purposes hereof, control means the power to exercise a controlling influence over the management or policies of a Person, unless such power is solely the result of an official position with such Person.

“Annual Report” shall mean any Annual Report or its addendum provided by the Property Owner or Major Owner, as applicable, pursuant to, and as described in, Sections 3 and 4 of this Disclosure Agreement.

“Assumption Agreement” means an undertaking of a Major Owner, or an Affiliate thereof, for the benefit of the holders and beneficial owners of the Bonds containing terms substantially similar to this Disclosure Agreement (as modified for such Major Owner’s development and financing plans with respect to the Property), whereby such Major Owner or Affiliate agrees to provide annual reports and notices of significant events, setting forth the information described in sections 4 and 5 hereof, respectively, with respect to the portion of the property in Improvement Area No. 2 of the District owned by such Major Owner and its Affiliates and, at the option of the Property Owner or such Major Owner, agrees to indemnify the Dissemination Agent pursuant to a provision substantially in the form of Section 11 hereof.

“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 Chief Financial Officer of the Property Owner or his or her designee, or such other officer or employee as the Property Owner shall designate in writing to the Dissemination Agent from time to time.

“Dissemination Agent” shall mean Union Bank of California, N.A., acting in its capacity as dissemination agent hereunder, or any successor dissemination agent designated in writing by the Issuer and which has filed with the Property Owner a written acceptance of such designation.

“District” shall mean City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon).

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

“Major Owner” shall mean an owner (including all Affiliates of such owner) of land in Improvement Area No. 2 of the District responsible in the aggregate for 20% or more of the annual Special Taxes levied in Improvement Area No. 2 of the District.

“National Repository” shall mean any Nationally Recognized Municipal Securities Information Repository for purposes of the Rule. The National Repositories currently approved by the Securities and Exchange Commission are set forth in the SEC website located at <http://www.sec.gov>.

“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.

“Person” means an individual, a corporation, a partnership, a limited liability company, an association, a joint stock company, a trust, any unincorporated organization or a government or political subdivision thereof.

“Property” means, at the time of inquiry, all real property then-owned by Property Owner or Major Owner within Improvement Area No. 2 of the District.

“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.

“Special Taxes” shall mean the special taxes to be levied within Improvement Area No. 2 of the District pursuant to the Fiscal Agent Agreement.

“State” shall mean the State of California.

“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) Property Owner shall, or, upon written direction, shall cause the Dissemination Agent to, not later than February 15 of each year, commencing February 15, 2007, provide to each Repository and the Participating Underwriter an Annual Report which is consistent with the requirements of Section 4 of this Disclosure Agreement with a copy to the Issuer. Not later than February 1 in each year, commencing February 1, 2007, Property Owner shall provide the Annual Report to the Dissemination Agent. Property Owner shall provide a written certification with each Annual Report furnished to the Dissemination Agent and the Issuer to the effect that such Annual Report constitutes the Annual Report required to be furnished by it hereunder. The Dissemination Agent and the Issuer may conclusively rely upon such certification of Property Owner and shall have no duty or obligation to review such Annual Report. In lieu of filing with each Repository, the Annual Report may be provided in electronic format through the services of a “Central Post Office” approved by the Securities and Exchange Commission. 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.

(b) If the Dissemination Agent is unable to verify that an Annual Report has been provided to Repositories by the date required in subsection (a), the Dissemination Agent 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.

(c) 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 Issuer and the Property Owner 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 Property Owner’s Annual Report shall contain or include by reference the following:

(i) Relating to the Property, a summary of the Property Owner’s development activity on the Property as of the preceding January 1, consisting of the following: (A) number of acres/lots owned by the Property Owner or its Affiliates as of such date, (B) progress of construction activities on the Property as of such date, and (C) number of acres/lots sold by Property Owner or its Affiliates to end users or builders as of such date.

(ii) Unless such information has already been provided in a previous Annual Report, any material changes in the information relating to the Property Owner and/or the Property contained in the Official Statement under the caption “IMPROVEMENT AREA NO. 2.”

(iii) A description of the status of any pending land purchase contracts with regard to the Property (other than sales to individual homebuyers).

(iv) Unless such information has already been provided in a previous Annual Report, a description of any change in the legal structure of the Property Owner and/or the financial condition of the Property Owner that would materially interfere with its ability to complete the development plan for the Property as described in the Official Statement under the caption “IMPROVEMENT AREA NO. 2 – Description of Development” (the “Development Plan”) or to pay its Special Taxes.

(v) A description of any material changes in the Development Plan.

(vi) A pro forma financing statement relating to the Development Plan described in the Official Statement under the caption “IMPROVEMENT AREA NO. 2 – Facilities and Fees to be Financed by the District” detailing (A) amount spent to date, (B) the remaining costs to complete the Development Plan including timing of such disbursements and (C) the source of financing for such remaining development costs.

(vii) A description of any previously undisclosed material amendment to the land use entitlements for the Property.

(viii) An update of the status of any previously reported Listed Event described in Section 5 hereof.

(ix) A statement as to whether or not the Property Owner and all of its Affiliates paid, prior to their becoming delinquent, all special taxes levied on the property owned by the Property Owner and such Affiliates within Improvement Area No. 2 of the District and if such Property Owner or any of such Affiliates is delinquent in the payment of such special taxes, a statement identifying each entity that is so delinquent, specifying the amount of each such delinquency and describing any plans to resolve such delinquency.

(x) Unless such information has already been provided in a previous Annual Report, a description of any material changes in the financing plan of the Property Owner for the Development Plan described in the Official Statement under the caption “IMPROVEMENT AREA NO. 2 – Financing Plan” (the “Financing Plan”) that are reasonably likely to have a significant impact on the Property Owner’s ability to complete the Development Plan and the causes or rationale for such changes.

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 Property Owner or related 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 Property Owner 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 Property Owner 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. bankruptcy or insolvency proceedings commenced by or against Property Owner or Affiliate thereof that would materially interfere with the Property Owner's ability to complete the Development Plan or to pay its Special Taxes when due;

2. failure to pay any taxes, special taxes or assessments due with respect to the Property prior to the delinquency date;

3. filing of a lawsuit against Property Owner or, to the Property Owner's actual knowledge, an Affiliate thereof (with service of process accomplished) seeking damages, or a judgment in a lawsuit against Property Owner or, to the Property Owner's actual knowledge, an Affiliate thereof, which, if decided adversely to Property Owner or Affiliate thereof, could have a significant impact on the Property Owner's ability to pay Special Taxes or to complete the Development Plan;

4. any conveyance by the Property Owner of property to an entity that is not an Affiliate of such Property Owner, the result of which conveyance is to cause the transferee to become a Major Owner and the related assumption of any obligation by a Major Owner pursuant to Section 6;

5. any denial or termination of credit, any denial or termination of, or default under, any line of credit or loan or any other loss of a source of funds that would have a material adverse affect on the Property Owner's most recently disclosed Financing Plan or the ability of the Property Owner or any Affiliate thereof owning property in Improvement Area No. 2 of the District to pay Special Taxes when due;

6. any significant amendments to land use entitlement for the Property Owner's property that would materially interfere with the Property Owner's ability to complete the Development Plan;

7. any previously undisclosed governmentally-imposed preconditions to commencement or continuation of development of the Property that would materially interfere with the Property Owner's ability to complete the Development Plan;

8. any previously undisclosed legislative, administrative or judicial challenges to development of the Property that would materially interfere with the Property Owner's ability to complete the Development Plan;

9. any material change in the alignment, design or likelihood of completion of significant public improvement being constructed by the Property Owner affecting the Property, including major thoroughfares, sewers, water conveyance systems and similar facilities; and

(b) The Disclosure Representative 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, promptly notify the Dissemination Agent in writing whether or not to report the event pursuant to subsection (f) and to the Bondholders.

(c) Whenever Disclosure Representative obtains knowledge of the occurrence of a Listed Event, the Disclosure Representative shall as soon as possible determine if such event would be material under applicable federal securities laws.

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

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

(f) If the Dissemination Agent has been instructed by the Disclosure Representative 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.

SECTION 6. Duration of Reporting Obligation. (a) All of the Property Owner's obligations hereunder shall commence on such date as property owned by the Property Owner is responsible for payment of 20% or more of the Special Taxes and shall terminate (except as provided in Section 11) upon the earlier to occur of (i) the legal defeasance, prior redemption or payment in full of all the Bonds, (ii) so long as the Bonds are outstanding, at such time as property owned by the Property Owner is no longer responsible for payment of 20% or more of the Special Taxes or (iii) the date on which all Special Taxes are paid or prepaid in full. Upon the occurrence of any such termination or suspension prior to the final maturity of the Bonds, the Property Owner shall give notice of such termination or suspension in the same manner as for a Listed event under Section 5.

(b) If a portion of the Property is conveyed to a Person that, upon such conveyance, will be a Major Owner, the obligations of Property Owner hereunder with respect to such property owned by such Major Owner and its Affiliates shall be assumed by such Major Owner or by an Affiliate thereof and the Property Owner obligations hereunder will be terminated. In order to effect such an assumption, such Major Owner or Affiliate shall enter into an Assumption Agreement. The entering into an Assumption Agreement by such Major Owner or Affiliate shall be a condition precedent to the conveyance of such property and the Property Owner shall provide a copy of the executed Assumption Agreement to the Issuer prior to such conveyance.

SECTION 7. Dissemination Agent. The Property Owner 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 Property Owner pursuant to this Disclosure Agreement. The initial Dissemination Agent shall be Union Bank of California, N.A. The Dissemination Agent may resign by providing thirty days written notice to the Property Owner and the Issuer. 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 Property Owner in a timely manner and in a form suitable for filing.

SECTION 8. Amendment; Waiver. Notwithstanding any other provision of this Disclosure Agreement, the Property Owner and the Dissemination Agent may amend this Disclosure Agreement (and the Dissemination Agent shall agree to any amendment so requested by the Property Owner) provided, 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 Fiscal Agent Agreement for amendments to the Fiscal Agent Agreement with the consent of Holders, or (ii) does not, in the opinion of 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 Property Owner 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 Property Owner.

SECTION 9. Additional Information. Nothing in this Disclosure Agreement shall be deemed to prevent the Property Owner 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 Property Owner 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 Property Owner 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 Property Owner to comply with any provision of this Disclosure Agreement, 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 Property Owner or the Dissemination Agent, 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 Fiscal Agent Agreement, and the sole remedy under this Disclosure Agreement in the event of any failure of the Property Owner or the Dissemination Agent to comply with this Disclosure Agreement shall be an action to compel performance.

SECTION 11. Duties, Immunities and Liabilities of Dissemination Agent. Article VII of the Fiscal Agent Agreement pertaining to the Fiscal Agent is hereby made applicable to this Disclosure Agreement as if this Disclosure Agreement were (solely for this purpose) contained in the Fiscal Agent Agreement and the Dissemination Agent shall be entitled to the protections, limitations from liability and indemnities afforded the Fiscal Agent thereunder. The Dissemination Agent shall have only such duties as are specifically set forth in this Disclosure Agreement, and the Property Owner agrees to indemnify and save the Dissemination Agent, its officers, directors and employees (the "Indemnified Party"), harmless against any loss, expense and liabilities which they may incur arising out of or in the reasonable exercise or performance of its powers and duties hereunder, including the reasonable costs and expenses (including reasonable attorneys fees) of defending against any claim of liability, but excluding losses, expenses or liabilities due to any Indemnified Party's respective negligence or willful misconduct. The Dissemination Agent shall be paid compensation by the Property Owner for its services provided hereunder in accordance with its schedule of fees as amended from time to time. The Dissemination Agent shall have no duty or obligation to review any information provided to it hereunder and shall not be deemed to be acting in any fiduciary capacity for the Property Owner, the Bondholders, or any other party. The Dissemination Agent shall not have any liability to the Bondholders or any other party for any monetary damages or financial liability of any kind whatsoever related to or arising from this Disclosure Agreement. The obligations of the Property Owner under this Section shall survive resignation or removal of the Dissemination Agent and payment of the Bonds.

SECTION 12. Notices. Any notices or communications to or among any of the parties to this Disclosure Agreement may be given as follows:

To the Issuer:	City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon) c/o City of Lake Elsinore 130 S. Main Street Lake Elsinore, California 92530 Attn: City Manager Telephone: (951) 674-3124 Facsimile: (951) 674-2392
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To the Dissemination Agent: Union Bank of California, N.A.
120 S. San Pedro Street, 4th Floor
Los Angeles, California 90012
Attn: Corporation Trust Department
Telephone: (213) 972-5676
Facsimile: (213) 972-5694

To the Property Owner: Centex Homes – Inland Empire Division
1265 Corona Pointe Court
Corona, California 92879
Attn: Chief Financial Officer
Telephone: (951) 479-9300
Facsimile: (951) 479-7521

with a copy to:

Centex Homes
2527 Camino Ramon, Suite 250
San Ramon, California 94583
Attn: Lisa Forbes, Regional General Counsel
Telephone: (925) 415-1834
Facsimile: (925) 415-1801

Any person may, by written notice to the other persons listed above, designate a different address or telephone number(s) to which subsequent notices or communications should be sent.

SECTION 13. Beneficiaries. This Disclosure Agreement shall inure solely to the benefit of the Issuer, the Property Owner, the Dissemination Agent, the Participating Underwriter and Holders and Beneficial Owners from time to time of the Bonds, and shall create no rights in any other person or entity.

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.

CENTEX HOMES, a Nevada general partnership

By Centex Real Estate Corporation, a Nevada corporation, its managing partner

By _____

Name: David L. Hahn

Title: Division President

UNION BANK OF CALIFORNIA, N.A.,
as Dissemination Agent

By _____

Authorized Officer

EXHIBIT A

NOTICE TO REPOSITORIES OF FAILURE TO FILE ANNUAL REPORT

Name of Obligated Party: Centex Homes
Name of Bond Issue: City of Lake Elsinore Community Facilities District
No. 2004-3 (Rosetta Canyon) Special Tax Bonds
(Improvement Area No. 2) 2006 Series A
Date of Issuance: September 19, 2006

NOTICE IS HEREBY GIVEN that the Property Owner has not provided an Annual Report with respect to the above-named Bonds as required by the Developer Continuing Disclosure Agreement, dated as of September 1, 2006, with respect to the Bonds. [The Property Owner anticipates that the Annual Report will be filed by _____.]

Dated: _____

UNION BANK OF CALIFORNIA, N.A.,
on behalf of Property Owner

cc: Issuer
Property Owner

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APPENDIX G

PROPOSED FORM OF BOND COUNSEL OPINION

City of Lake Elsinore
130 S. Main Street
Lake Elsinore, California 92530

\$23,460,000
City of Lake Elsinore
Community Facilities District No. 2004-3 (Rosetta Canyon)
Special Tax Bonds (Improvement Area No. 2) 2006 Series A

Members of the City Council:

We have acted as bond counsel to the City of Lake Elsinore (the “City”) in connection with the issuance of the \$23,460,000, aggregate principal amount of City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon) Special Tax Bonds (Improvement Area No. 2) 2006 Series A (the “Bonds”), pursuant to the provisions of Mello-Roos Community Facilities Act of 1982, as amended, being Chapter 2.5, Part 1, Division 2, Title 5 of the Government Code of the State of California (the “Act”) and pursuant to a Fiscal Agent Agreement, dated as of September 1, 2006 (the “Fiscal Agent Agreement”), by and between the City of Lake Elsinore Community Facilities District No. 2004-3 (Rosetta Canyon) (the “District”) and Union Bank of California, N.A., as fiscal agent (the “Fiscal Agent”). We have examined the Act and such certified proceedings and other papers as we deem necessary to render this opinion.

As to questions of fact material to our opinion, we have relied upon representations of the District contained in the Fiscal Agent Agreement and in the certified proceedings and certifications of public officials and others furnished to us, without undertaking to verify the same by independent investigation.

Based upon the foregoing we are of the opinion, under existing law, as follows:

1. The Fiscal Agent Agreement has been duly and validly authorized, executed and delivered by the District and, assuming such Fiscal Agent Agreement constitutes the legally valid and binding obligation of the Fiscal Agent, constitutes the legally valid and binding obligation of the District enforceable against the District in accordance with its terms.
2. The Bonds constitute valid and binding limited obligations of the District as provided in the Fiscal Agent Agreement, and are entitled to the benefits of the Fiscal Agent Agreement.
3. The Bonds are secured by a valid pledge of the Special Taxes (as defined in the Fiscal Agent Agreement) and all moneys in the funds and accounts under the Fiscal Agent Agreement, including all amounts derived from the investment of such moneys, subject to the application thereof on the terms and conditions as set forth in the Fiscal Agent Agreement.
4. The Internal Revenue Code of 1986, as amended (the “Code”) sets forth certain requirements that must be met subsequent to the issuance and delivery of the Bonds for interest thereon to be and remain excluded from the gross income of the owners thereof for federal income tax purposes. Noncompliance with such requirements could cause the interest on the Bonds to be included in gross

income retroactive to the date of issue of the Bonds. The District has covenanted in the Fiscal Agent Agreement to maintain the exclusion of interest on the Bonds from the gross income of the owners thereof for federal income tax purposes.

In our opinion, under existing law, interest on the Bonds is exempt from personal income taxation of the State of California and, assuming compliance with the aforementioned covenant, interest on the Bonds is excluded pursuant to section 103(a) of the Code from the gross income of the owners thereof for federal income tax purposes. We are further of the opinion that under existing statutes, regulations, rulings and court decisions, the Bonds are not “specified private activity bonds” within the meaning of section 57(a)(5) of the Code and, therefore, the interest on the Bonds will not be treated as an item of tax preference for purposes of computing the alternative minimum tax imposed by section 55 of the Code. The receipt or accrual of interest on Bonds owned by a corporation may affect the computation of the alternative minimum taxable income, upon which the alternative minimum tax is imposed, to the extent that such interest is taken into account in determining the adjusted current earnings of that corporation (75 percent of the excess, if any, of such adjusted current earnings over the alternative minimum taxable income being an adjustment to alternative minimum taxable income (determined without regard to such adjustment or to the alternative tax net operating loss deduction)).

Except as stated in the preceding two paragraphs, we express no opinion as to any federal or state tax consequences of the ownership or disposition of the Bonds. Furthermore, we express no opinion as to any federal, state or local tax law consequences with respect to the Bonds, or the interest thereon, if any action is taken with respect to the Bonds or the proceeds thereof predicated or permitted upon the advice or approval of other bond counsel.

No opinion is expressed herein on the accuracy, completeness or sufficiency of the Official Statement or other offering materials relating to the Bonds.

The rights of the owners of the Bonds and the enforceability of the Bonds and the Fiscal Agent Agreement may be subject to bankruptcy, insolvency, reorganization, moratorium and other similar laws affecting creditors’ rights heretofore or hereafter enacted and may also be subject to the exercise of judicial discretion in appropriate cases.

Our opinions are based on existing law, which is subject to change. Such opinions are further based on our knowledge of facts as of the date hereof. We assume no duty to update or supplement our opinions to reflect any facts or circumstances that may thereafter come to our attention or to reflect any changes in any law that may thereafter occur or become effective. Moreover, our opinions are not a guarantee of result and are not binding on the Internal Revenue Service; rather, such opinions represent our legal judgment based upon our review of existing law that we deem relevant to such opinions and in reliance upon the representations and covenants referenced above.

Respectfully submitted,