

MONARCH BAY LAND ASSOCIATION
QUESTIONS AND ANSWERS

WHAT IS THIS ALL ABOUT?

The materials which follow set forth the agreement between the Monarch Bay Land Association ("MBLA") and the owner of the fee interest to the land which constitutes the Monarch Bay community (the "Owner"). This agreement contemplates fixing rent from the years 1990 to 2020 based on the increase in the Consumer Price Index (All Urban Consumers) from 1960 to 1990. It also provides that in the year 2020, fee interest in Monarch Bay can be purchased in cash by MBLA for 65 percent of its then (i.e., 2020) appraised fair market value.

DOESN'T THE GROUND LEASE AND MY SUBLEASE ALREADY PROVIDE FOR A RENT ADJUSTMENT IN 1990?

Yes, there is a provision for such an adjustment but the language is subject to multiple interpretations. The language as set forth in the Ground Lease and your Sublease is substantially as follows:

"...the amount of said adjustment, if any, and the increase or decrease of rental shall be proportionate to the trend in the purchasing power of the United States dollar. In connection with determining the trend hereinabove mentioned the annual averages during the first thirty years of the term hereof of applicable indices of the purchasing power of the dollar pertaining to the Los Angeles metropolitan area shall be used and thereafter during the remaining thirty years of the term of this lease, the Lessee shall pay to the Lessor such rental as so adjusted"

If there is not an agreement as to "the trend in the purchasing power of the United States dollar" based on the "applicable indices of the purchasing power of the dollar", arbitration or litigation will probably result.

The purpose of the agreement is to avoid such a controversy in exchange for a right to buy our land.

WHY IS IT IMPORTANT THAT WE HAVE THE OPTION TO BUY THE LAND AT THE END OF THE TERM OF OUR SUBLEASES?

In any landlord-tenant relationship, the risk to the tenant is that the landlord will either choose a new tenant or decide to change the use at the end of the lease. Under the Ground Lease and your Sublease, your right on July 1, 2020 is as follows:

"Upon the expiration of the term of this lease, any authorized sublessee of Lessee hereunder shall have the right to remove from the lot in said tract sublet by him his dwelling house and appurtenant improvements (exclusive of paving and underground installations), in which event Lessee, at its expense or at the expense of such sublessee, shall cause said dwelling house and improvements to be removed from said lot within sixty (60) days after the expiration of said term and shall cause any excavations to be filled and all foundations, debris and other parts of said dwelling to be removed and Lessee shall cause possession of said lot to be surrendered to Lessor in a clean and orderly condition."

Without the proposed option, it is possible that in the year 2020 the Owner might wish to put in a hotel complex, apartment structures, condominiums or some other use. In that event we have no right under our Subleases to remain in possession of our homes beyond July 1, 2020. The Option Agreement assures us that, if the Option is exercised, the residential uses in Monarch Bay will remain and that we will be able to purchase our lot at 65% of its then appraised fair market value.

CAN THE OPTION TO PURCHASE BE EXERCISED BEFORE THE YEAR 2020?

No. Moreover, even in 2020 individual homeowners do not have a separate right to purchase directly from the Owner but rather only through MBLA. In the year 2020, MBLA can exercise its option to purchase all Monarch Bay lots and in turn, individual homeowners who are members of MBLA may elect to purchase from or through MBLA at that time.

WHAT CAN I EXPECT MY RENT TO BE IN 1990?

Your existing rent will undoubtedly increase and in all likelihood increase by a multiple. It will be calculated by multiplying your existing monthly rent by a fraction, the denominator of which will be 88.7, the numerator of which will be the Consumer Price Index (All Urban Consumers) as of 1990. As of July 1988, this Consumer Price Index was 360.9. Therefore, (by way of example only) if the rental adjustment were to have occurred in July 1988, if you were paying \$50.00 per month prior to that date, your rent as adjusted under the Amendment to Sublease would be \$203.48 per month.

WHO WILL DETERMINE THE PURCHASE PRICE AND HOW WILL IT BE DONE?

Assuming MBLA and the Owner are unable to agree on value, the Option Agreement provides for a comprehensive appraisal mechanism, which you should read carefully in the enclosed Option Agreement (Tab 7). In summary, MBLA and the Owner will each appoint an appraiser for each of the 214 lots in the community each such lot to be appraised as a "finished lot." In other words, in the appraisal process it will be assumed that your house has been demolished and removed from the lot and the remainder will be appraised only as a finished lot (i.e., graded with curbed gutters and other amenities of the then-existing Monarch Bay). After agreement on value is reached, the appraised values of each of the 214 lots will be totalled, added to any residual or unallocated value of the Beach Club, multiplied by 65 percent, and that will be the option price to MBLA. At that time, those existing members of MBLA will have a right to purchase their lot at 65 percent of the lot's appraised value.

WHAT HAPPENS IF I ELECT NOT TO JOIN?

Participation is voluntary. In order for MBLA to satisfy its obligations to the Owner, it must have at least 150 homeowners participate. If you have not filled out the Receipt for Documents and Application for Membership, Certificate of Membership and Beneficial Interest, and delivered those documents and your check in the amount of \$2,000.00 to MBLA by November 4, 1988, you will not be re-considered for MBLA membership for 60 months and at that time, the cost of membership will undoubtedly have increased. The more Monarch Bay residents who join initially, the less the initial cost of the overall program will be and possibly a portion of the \$2,000.00 membership fee can be returned. If you do not join, you are bound by the present terms of your Sublease.

WHAT ARE THE COSTS?

Initially, \$2000.00 per lot (assuming 150 residents elect to participate) will fund the \$400,000.00 of option payments and the other expenses of MBLA (legal, printing, mailing, etc.) in finalizing this transaction. In addition to this, your rent will increase effective July 1, 1990 as described above and in 2020 in order to purchase your lot, you will have to pay 65% of its then appraised fair market value.

CAN MY OPTION RIGHT BE SOLD SEPARATELY FROM MY HOUSE?

No. Your beneficial interest through MBLA under the Option Agreement is "appurtenant" to your subleasehold estate, meaning it is inseparable from your subleasehold interest in your lot and any attempt to sell it separately from the lot is automatically void by the MBLA charter documents.

WHAT HAPPENS IF WE DO NOT GET 150 RESIDENTS WHO ARE INTERESTED?

Under the Delivery Escrow Instructions (Tab 6) to Fred Forgy (attorney for the Owner), if certified copies of Amended Subleases executed by 150 residents are not presented by December 31, 1988, he has been instructed to destroy the signed Option Agreement, in which case it will have no further force or effect.

**IF I PARTICIPATE NOW, WILL THE BENEFICIAL INTEREST OPTION
BENEFIT FUTURE OWNERS?**

Yes.. Your beneficial interest in the Option Agreement through your ownership in MBLA attaches to your subleasehold estate and is transferable to all future owners provided they continue to make payments under the Sublease Agreement and become and remain members in good standing of MBLA.

WHAT WILL ALL OF THIS DO TO THE VALUE OF THE PROPERTY?

No assurance can be given that participation in MBLA will increase the present or future value of your home.

WHY IS THE MONARCH BAY LAND ASSOCIATION NECESSARY?

You are referred to Tab 5, paragraph 3.

WHAT IF I AM UNCERTAIN?

MBLA officers and directors urge you to seek counsel from your business/legal/accounting advisor to the extent you deem it necessary and/or prudent.

**WHAT IS LEFT TO BE DONE BY MBLA WITH RESPECT TO THIS OPTION
AGREEMENT?**

Once 150 residents have signed up and contributed their appropriate payment, it is necessary that we obtain the signatures of Avco Community Developers, Inc., ("Avco") to the Amendment to Ground Lease and of California Western Home Financing Partners ("Western") to each Amendment to Subleasehold. No assurance is given that such signatures will be forthcoming. No assurance can be given that Avco or Western will not require additional changes to the documents and you should be aware that in joining MBLA, you are authorizing the existing Board of Directors to make the decision as to whether such changes should be made.

IN THE YEAR 2020, WILL THE APPRAISER BE TAKING INTO ACCOUNT THE VALUE OF MY HOUSE?

No. The Option Agreement specifically defines what the appraiser will be considering and it is defined as a "finished lot." You should read the Option Agreement (Tab 7) for more detail of what will be included and excluded but to give you a rough picture of what will be valued, think of the existing development at Ritz Cove as those lots are completed but before the construction of any homes. The reason for this approach is that under the Ground Lease as passed along to you under your Sublease, it is provided that at the conclusion of the term you have a right to remove your house and its foundation and take it with you. Therefore, it is improper to include the value of the house in valuing the finished lot since we would be paying the Owner for our own property!

WILL THIS WHOLE ARRANGEMENT HELP ME OBTAIN FINANCING FOR MY HOUSE?

No assurance can be given as to how any particular lender will react to the Option Agreement. However, common sense would tell you that it certainly cannot hurt since it eliminates some of the uncertainty regarding rent in 1990 and gives you an indirect right to purchase your lot which you presently do not have. Please remember, however, your right to purchase is not a direct right, is subject to the satisfaction of certain contingencies, and is passed on to you only if the Option is exercised by MBLA in 2020. In other words, you do not have a direct agreement with the Owner to purchase your lot. It is a secondary right which you enjoy only by virtue of your membership in MBLA.

ARE ALL RESIDENTS BEING TREATED THE SAME?

Yes - there are no "special deals." In fact, the individuals identified in Table of Organization and Committees for MBLA (Tab 2) have each advanced \$700.00 to pay for out-of-pocket expenses (e.g., printing) with no assurance that they would receive any benefit from or return of this money. Those individuals' right to purchase the beneficial interest will be on the same basis of everyone else's except their \$700.00 will be credited against the initial \$2,000.00 membership fee.

WHAT ABOUT LEGAL FEES?

Three of our residents, Messrs. Miles, McClung and Scallon, have performed legal services without any compensation for up to three years. Their agreement with MBLA was that if the transaction was not successful, they would not be compensated for their effort. Conversely, if the transaction was successful, it was agreed that they would be compensated; however, you should be aware that their charges for legal services to the community are on a basis substantially less than would have otherwise been made in an "arms length" transaction.

WHAT HAPPENS TO THE BEACH CLUB WHEN THE OPTION IS EXERCISED?

The Beach Club Lots become one of the common area amenities for Monarch Bay for the private use of the MLBA members who elect to buy their lots.

WHY DOES OPTION PROVIDE FOR THE PURCHASE IN 2020 AT LESS THAN FAIR MARKET?

The Owner is entitled only to the 2020 value of the land and not any subdivision improvements then in place. This discount allows for the return of those costs to the sublessees. This reduction also reflects the bargain struck in the negotiations in exchange for the indemnity afforded the Owner under the Option Agreement.

WHY NOT AN EARLIER PURCHASE DATE?

The Owner would not consider a sale while the Ground Lease was in effect because too many interests must be considered.

WILL OUR OPTION POSITION BE INSURED?

Yes, by First American Title Insurance Company. The coverage will be approximately \$5 million.

HOW WILL THE FUTURE OPTION PAYMENTS BE FUNDED?

It is the intent of MBLA to purchase Zero Coupon Tax Exempt Bonds with due dates corresponding to the dates of the required option payments (Tab 12). In turn, MBLA may place these Bonds in trust in Sanwa Bank with instructions including notice in the event of early call. The Budget (Tab 11) currently shows an estimate of \$90,000.00 as the amount necessary to make the Bond purchase.

THESE QUESTIONS AND ANSWERS SHOULD NOT TO BE RELIED ON IN MAKING YOUR DECISION TO JOIN OR NOT JOIN MONARCH BAY LAND ASSOCIATION. RATHER, YOU ARE ADVISED TO READ CAREFULLY ALL OF THE INFORMATION CONTAINED IN THE PACKAGE AND IF YOU HAVE ANY QUESTIONS, TO SEEK THE ADVICE OF YOUR PROFESSIONAL ADVISOR.

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