

**RECORDING REQUESTED BY AND WHEN
RECORDED MAIL TO:**

Whidbey Island Bank
P.O. Box 1589
Oak Harbor, Washington 98277
[Loan No. 149017261]



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Skagit County Auditor

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CHICAGO TITLE IC31157

**BE ADVISED THAT THE PROMISSORY NOTE SECURED BY THIS
SECURITY INSTRUMENT PROVIDE FOR A VARIABLE RATE OF
INTEREST AND A BALLOON PAYMENT AT MATURITY.**

**DEED OF TRUST, SECURITY AGREEMENT,
ASSIGNMENT OF LEASES AND RENTS
AND FIXTURE FILING**

Grantor (Borrower): CHALLENGE DEVELOPMENTS II, L.L.C., a
Washington limited liability company
Grantee (Lender): WHIDBEY ISLAND BANK, a Washington
corporation
Grantee (Trustee): CHICAGO TITLE INSURANCE COMPANY
Legal Description: Ptn SE 24-35-01
Additional Legal(s) on Exhibit A
Assessor's Tax Parcel ID Number: 350124-0-139-0103

THIS DEED OF TRUST, SECURITY AGREEMENT, ASSIGNMENT OF LEASES AND RENTS AND FIXTURE FILING (this "Security Instrument"), is made this 13th day of March, 2006 among CHALLENGE DEVELOPMENTS II, L.L.C., a Washington limited liability company, the address of which is 12062 Marine Drive, Anacortes, Washington 98221, as grantor ("Borrower"); CHICAGO TITLE INSURANCE COMPANY, the address of which is 425 Commercial Street, Mount Vernon, Washington 98273 and its successors in trust and assigns, as trustee ("Trustee"); and WHIDBEY ISLAND BANK, a Washington corporation, at its offices at P.O. Box 1589, Oak Harbor, Washington 98277, as beneficiary ("Lender"). This Security Instrument is made in connection with the loan (the "Loan") evidenced by the Note (as defined in Section 3 below).

1. **GRANTING CLAUSE.** Borrower, in consideration of the acceptance by Trustee of the trust hereunder, and of other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, and in order to secure the obligations described in Section 3 below, grants, bargains, sells, assigns and conveys to Trustee and its successors in trust and assigns, forever, in trust, with power of sale, all of Borrower's estate,

right, title, interest, claim and demand in and to the property in the county of Skagit, state of Washington, described as follows, whether now existing or hereafter acquired (all of the property described in all parts of this Section 1 and all additional property, if any, described in Section 2 is called the "Property"):

1.1 **Land, Appurtenances and Leasehold.** The land described as Parcel 1 on Exhibit A hereto, and all tenements, hereditaments, rights-of-way, easements, appendages and appurtenances thereto belonging or in any way appertaining, including without limitation all of the right, title and interest of Borrower in and to any avenues, streets, ways, alleys, vaults, strips or gores of land adjoining that property, all rights to water, water stock, drains, drainage and air rights relating to that property, and all claims or demands of Borrower either in law or in equity in possession or expectancy of, in and to that property, and including but not limited to: (a) the condominium units described as Parcel 2 on Exhibit A hereto; (b) the leasehold estate created by the ground lease (the "Ground Lease") described on Exhibit B attached hereto; (c) any and all options to purchase, rights of first refusal and renewal options with respect to the Ground Lease or any real or personal property covered thereby, or any portion thereof or any interest therein; (d) any and all greater estate in such real or personal property (including but not limited to the fee estate) as may subsequently be acquired by or released to Borrower, whether under the Ground Lease or otherwise; (e) any and all interest, estate and other claims, both in law and equity, that Borrower now has or may hereafter acquire in and to any such real or personal property; and (f) any and all other rights and interests of Borrower arising under or as a result of the Ground Lease; and

1.2 **Improvements and Fixtures.** All buildings, structures and other improvements now or hereafter erected on the property described in 1.1 above, and all facilities, fixtures, machinery, apparatus, installations, goods, equipment, inventory, furniture, building materials and supplies and other properties of whatsoever nature, now or hereafter located in or used or procured for use in connection with that property, it being the intention of the parties that all property of the character described above that is now owned or hereafter acquired by Borrower and that is affixed or attached to, stored upon or used in connection with the property described in 1.1 above shall be, remain or become a portion of that property and shall be covered by and subject to the lien of this Security Instrument, together with all contracts, agreements, permits, plans, specifications, drawings, surveys, engineering reports and other work products relating to the design, construction, supply or installation of the existing or any future improvements or fixtures on the Property, any and all rights of Borrower in, to or under any architect's contracts, engineer's contracts or construction contracts relating to the design or construction of the existing or any future improvements on the Property, and any performance and/or payment bonds issued in connection therewith, together with all trademarks, trade names, copyrights, computer software and other intellectual property used by Borrower in connection with the Property; and

1.3 **Enforcement and Collection.** Any and all rights of Borrower without limitation to make claim for, collect, receive and receipt for any and all rents, income,



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revenues, issues, earnest money, deposits, refunds (including but not limited to refunds from property taxing authorities, utilities and insurers), royalties, and profits, including mineral, oil and gas rights and profits, insurance proceeds of any kind (whether or not Lender requires such insurance and whether or not Lender is named as an additional insured or loss payee of such insurance), condemnation awards and other moneys, payable or receivable from or on account of any of the Property, including interest thereon, or to enforce all other provisions of any other agreement (including those described in Section 1.2 above) affecting or relating to any of the Property, to bring any suit in equity, action at law or other proceeding for the collection of such moneys or for the specific or other enforcement of any such agreement, award or judgment, in the name of Borrower or otherwise, and to do any and all things that Borrower is or may be or become entitled to do with respect thereto, provided, however, that no obligation of Borrower under the provisions of any such agreements, awards or judgments shall be impaired or diminished by virtue hereof, nor shall any such obligation be imposed upon Trustee or Lender; and

1.4 **Accounts and Income.** Any and all rights of Borrower in any and all accounts, rights to payment, contract rights, chattel paper, documents, instruments, licenses, contracts, agreements and general intangibles relating to any of the Property, including, without limitation, income and profits derived from the operation of any business on the Property or attributable to services that occur or are provided on the Property or generated from the use and operation of the Property; and

1.5 **Leases.** All of Borrower's rights as landlord in and to all existing and future leases, subleases and tenancies, whether written or oral and whether for a definite term or month to month or otherwise, now or hereafter demising all or any portion of the property described in 1.1 and 1.2 above, including all renewals and extensions thereof and all rents, deposits and other amounts received or receivable thereunder, and including all guaranties, supporting obligations, letters of credit (whether tangible or electronic) and letter of credit rights guaranteeing or supporting any such lease, sublease or tenancy (in accepting this Security Instrument neither Lender nor Trustee assumes any liability for the performance of any such lease, sublease or tenancy); and

1.6 **Ancillary Agreements.** All right, title and interest of Borrower in, to and under the following agreements and other documents:

(a) Side Agreement for IMDC Building Purchase and Condominium Conversion dated on or about the date of this Agreement between Borrower and Skagit County Public Hospital District No. 2 (d/b/a Island Hospital) (the "Hospital");

(b) Storage Space Lease Agreement dated on or about the date of this Agreement between the Hospital as landlord and Borrower as tenant relating to certain premises consisting of 212 rentable square feet of space located in Unit LL1 of the Condominium;



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(c) Storage Space Lease Agreement dated on or about the date of this Agreement between the Hospital as landlord and Borrower as tenant relating to certain premises consisting of 247 rentable square feet of space located in Unit LL1 of the Condominium; and

(d) Storage and Support Space Lease Agreement dated on or about the date of this Agreement between the Hospital as landlord and Borrower as tenant relating to certain premises consisting of 3,070 rentable square feet of space located in Unit LL1 of the Condominium.

1.7 **Books and Records.** All books and records of Borrower relating to the foregoing in any form.

2. SECURITY AGREEMENT AND ASSIGNMENT OF LEASES AND RENTS.

2.1 **Security Agreement.** To the extent any of the property described in Section 1 is personal property, Borrower, as debtor, grants to Lender, as secured party, a security interest therein together with a security interest in all other personal property of whatsoever nature that is located on or used or to be used in connection with any of the property described in Section 1, and any products or proceeds of any thereof, pursuant to the Uniform Commercial Code of the state of Washington (the "UCC"), on the terms and conditions contained herein. Lender hereby assigns such security interest to Trustee, in trust, for the benefit of Lender to be dealt with as a portion of the "Property" except as otherwise specified herein. Borrower hereby authorizes Lender to file any financing statement, fixture filing or similar filing to perfect the security interests granted in this Security Instrument without Borrower's signature. Borrower shall: (a) execute and deliver such documents as Lender deems necessary to create, perfect and continue the security interests contemplated by this Security Instrument; (b) not change its name, or, as applicable, its chief executive office, its principal residence (or, if Borrower is a trust or one or more trustees acting with respect to property held in trust, the identity or principal residence of any trustee), the jurisdiction in which it is organized, or otherwise change its location (as that term is used in Article 9 of the UCC), without giving Lender at least 30 days' prior written notice thereof; and (c) cooperate with Lender in perfecting all security interests granted in this Security Instrument and in obtaining such agreements from third parties as Lender deems necessary, proper or desirable in connection with the preservation, perfection or enforcement of any of Lender's rights under this Security Instrument.

2.2 **Assignment of Leases and Rents.**

(a) **Absolute Assignment.** Borrower hereby absolutely and unconditionally grants, transfers, conveys, sells, sets over and assigns to Lender all of



Borrower's right, title and interest now existing and hereafter arising in and to the leases, subleases, concessions, licenses, franchises, occupancy agreements, tenancies, subtenancies and other agreements, either oral or written, now existing and hereafter arising which affect the Property, Borrower's interest therein or any improvements located thereon, together with any and all security deposits, guaranties of the lessees' or tenants' obligations (including any and all security therefor), and other security under any such leases, subleases, concessions, licenses, franchises, occupancy agreements, tenancies, subtenancies and other agreements, and all supporting obligations, letters of credit (whether tangible or electronic) and letter of credit rights guaranteeing or supporting any of the foregoing (all of the foregoing, and any and all extensions, modifications and renewals thereof, shall be referred to, collectively, as the "Leases"), and hereby gives to and confers upon Lender the right to collect all the income, rents, issues, profits, royalties and proceeds from the Leases and any business conducted on the Property and any and all prepaid rent and security deposits thereunder (collectively, the "Rents"). The term "Rents" includes, but is not limited to all minimum rents, additional rents, percentage rents, deficiency rents, common area maintenance charges, lease termination payments, purchase option payments, refunds of any type, prepayment of rents, settlements of litigation, settlements of past due rents, and liquidated damages following default, and all proceeds payable under any policy of insurance covering loss of rents, together with any and all rights and claims of any kind that Borrower may have against any tenant under the Leases or any other occupant of the Property. This Security Instrument is intended by Lender and Borrower to create and shall be construed to create an absolute assignment to Lender of all of Borrower's right, title and interest in and to the Leases and the Rents and shall not be deemed merely to create a security interest therein for the payment of any indebtedness or the performance of any obligations under the Loan Documents (as defined below). Borrower irrevocably appoints Lender its true and lawful attorney at the option of Lender at any time to demand, receive and enforce payment, to give receipts, releases and satisfactions and to sue, either in the name of Borrower or in the name of Lender, for all such Rents and apply the same to the Secured Obligations.

(b) **Revocable License to Collect.** Notwithstanding the foregoing assignment of Rents, so long as no Event of Default (as defined below) remains uncured, Borrower shall have a revocable license, to collect all Rents, and to retain any portion thereof not required to pay the expenses of the Property or the obligations secured thereby. Upon any Event of Default, Borrower's license to collect and retain Rents shall terminate automatically and without the necessity for any notice.

(c) **Collection and Application of Rents by Lender.** While any Event of Default remains uncured: (i) Lender may at any time, without notice, in person, by agent or by court-appointed receiver, and without regard to the adequacy of any security for the Secured Obligations, enter upon any portion of the Property and/or, with or without taking possession thereof, in its own name sue for or otherwise collect Rents (including past due amounts); and (ii) without demand by Lender therefor, Borrower shall promptly deliver to Lender all prepaid rents, deposits relating to Leases or Rents, and all other



Rents then held by or thereafter collected by Borrower whether prior to or during the continuance of any Event of Default. Any Rents collected by or delivered to Lender may be applied by Lender against the Secured Obligations, less all expenses, including attorneys' fees and disbursements, in such order as Lender shall determine in its sole and absolute discretion. No application of Rents against any Secured Obligation or other action taken by Lender under this Section 2.2 shall be deemed or construed to cure or waive any Event of Default, or to invalidate any other action taken in response to such Event of Default, or to make Lender a mortgagee-in-possession of the Property.

(d) **Direction to Tenants.** Borrower hereby irrevocably authorizes and directs the tenants under all Leases to pay all amounts owing to Borrower thereunder to Lender following receipt of any written notice from Lender that states that an Event of Default remains uncured and that all such amounts are to be paid to Lender. Borrower further authorizes and directs all such tenants to pay all such amounts to Lender without any right or obligation to inquire as to the validity of Lender's notice and regardless of the fact that Borrower has notified any such tenants that Lender's notice is invalid or has directed any such tenants not to pay such amounts to Lender.

3. **OBLIGATIONS SECURED.** This Security Instrument is given for the purpose of securing the following (the "Secured Obligations"):

3.1 **Performance and Payment.** The performance of the obligations contained herein and in the construction and permanent loan agreement (the "Loan Agreement") of even date herewith between Borrower and Lender, and the payment of \$3,692,636 with interest thereon and all other amounts payable according to the terms of the Loan Agreement and of a promissory note (the "Note") of even date herewith in such amount made by Borrower, payable to Lender or order, and any and all extensions, renewals, modifications or replacements of either thereof, whether the same be in greater or lesser amounts. The Loan Agreement and Note provide for a variable rate of interest and a balloon payment at maturity.

3.2 **Future Advances.** The repayment of any and all sums advanced or expenditures made by Lender subsequent to the execution of this Security Instrument for the construction of improvements on the Property, or the maintenance or preservation of the Property, or advanced or expended by Lender for any other purpose pursuant to any provision of this Security Instrument or the other Loan Documents (as defined below) on or after the date hereof, together with interest thereon. Borrower intends that all such advances, whenever made and whether or not Lender is obligated to make the same, shall be secured by this Security Instrument and shall be a lien on the Property having priority as of the date this Security Instrument is recorded.

3.3 **Other Amounts.** All other obligations and amounts now or hereafter owing by Borrower to Lender under this Security Instrument, the Note or any other document.



instrument or agreement evidencing, securing or otherwise relating to the Loan and any and all extensions, renewals, modifications or replacements of any thereof (collectively, the "Loan Documents"); provided, however, that this Security Instrument does not and shall not in any event be deemed to, secure the obligations owing to Lender under: (a) any certificate and indemnity agreement regarding hazardous substances (the "Indemnity Agreement") executed in connection with the Loan (or any obligations that are the substantial equivalent thereof); or (b) any guaranty of the Loan.

4. **WARRANTIES AND COVENANTS OF BORROWER.** Borrower warrants, covenants, and agrees:

4.1 **Warranties.**

(a) Borrower has full power and authority to grant the Property to Trustee and warrants the Property to be free and clear of all liens, charges, and other monetary encumbrances except those appearing in the title insurance policy accepted by Lender in connection with this Security Instrument.

(b) None of the Property is used principally or at all for agricultural or farming purposes.

(c) The Property is free from damage and no matter has come to Borrower's attention (including, but not limited to, knowledge of any construction defects or nonconforming work) that would materially impair the value of the Property as security.

(d) Borrower is the lawful owner of the tenant's interest in the Ground Lease and the holder of the leasehold premises thereunder and has good right, by and with the consent of the lessor thereunder ("Ground Lessor"), to assign and encumber the Ground Lease as provided in this Security Instrument. The rentals accrued and due under the Ground Lease are fully paid and the Ground Lease is in all other respects in good standing, is valid and is in full force and effect without any default by any party.

(e) The Loan is primarily for commercial, industrial or business purposes and is not primarily for personal, family or household purposes.

4.2 **Preservation of Lien.** Borrower will preserve and protect the priority of this Security Instrument as a first lien on the Property (but subject to the Ground Lease). If Borrower fails to do so, Lender may take any and all actions necessary or appropriate to do so and all sums expended by Lender in so doing shall be treated as part of the Secured Obligations, shall be paid by Borrower upon demand by Lender and shall bear interest at the highest rate borne by any of the Secured Obligations.



4.3 **Repair and Maintenance of Property.** Borrower will keep the Property in good condition and repair, which duty shall include but is not limited to cleaning, painting, landscaping, repairing, and refurbishing of the Property; will complete and not remove or demolish, alter, or make additions to any building or other improvement that is part of the Property, or construct any new structure on the Property, without the express written consent of Lender; will underpin and support when necessary any such building or other improvement and protect and preserve the same; will complete or restore promptly and in good and workmanlike manner any such building or other improvement that may be damaged or destroyed and pay when due all claims for labor performed and materials furnished therefor; will not commit, suffer, or permit any act upon the Property in violation of law; and will do all other acts that from the character or use of the Property may be reasonably necessary for the continued operation of the Property in a safe and legal manner, the specific enumerations herein not excluding the general. If Lender at any time reasonably determines that Borrower is not maintaining and repairing the Property as required under this section, Lender may, by written notice to Borrower and without waiving any of its other rights or remedies hereunder or under the other Loan Documents, require that Borrower begin funding a reserve (the "Deferred Maintenance Reserve"), to be held by Lender, with monthly deposits in an amount determined by Lender in its reasonable discretion and payable with each monthly payment on the Note. If no Event of Default exists, Lender shall from time to time release the funds in the Deferred Maintenance Reserve, if applicable, to Borrower to reimburse Borrower for the reasonable cost of reasonably required maintenance and repairs to the Property provided Borrower establishes to Lender's satisfaction (including provision of paid receipts for all such work and materials) that such work is carried out in a workmanlike fashion, free of liens, and consistent with such other reasonable requirements as Lender may impose. Borrower shall execute a deferred maintenance reserve agreement on Lender's then-current form providing for the terms of the Deferred Maintenance Reserve in greater detail. Borrower hereby grants Lender a lien on and security interest in any Deferred Maintenance Reserve established under this Security Instrument as security for the Note and all other Secured Obligations.

4.4 **Insurance.** Borrower shall provide and maintain insurance as required by this Security Instrument and the acknowledgment of insurance requirements entered into by Borrower in connection with the Loan (the "Acknowledgment"). Certain insurance requirements set forth in the Acknowledgment apply only during the Period of Construction (as defined in the Acknowledgment) and certain of those requirements supersede the requirements of this Section 4.4 during the Period of Construction, as provided in the Acknowledgment. The insurance provisions of the Acknowledgment will control over the provisions of this Section 4.4 to the extent of any express inconsistency.

4.4.1 **Property.** Borrower will provide and maintain, as further security for the faithful performance of the Secured Obligations, insurance covering fire and other perils substantially equivalent to those insured under the Causes of Loss—Special Form published by the Insurance Service Office ("ISO"), with boiler and machinery coverage and

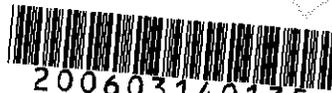


coverage against such other perils as may be specified by Lender (including insurance against earthquake/earth movement and/or against terrorism, if required by Lender on a case-by-case basis) in an amount not less than 100% of the replacement cost of the Property. Such insurance must include an ordinance or law coverage endorsement. If Lender permits coverage of less than 100% replacement cost in its sole discretion, then such policy must contain an agreed amount endorsement covering at least 80% of such replacement cost. Such insurance policy or policies shall include rental income and business income interruption coverage as more specifically described in Section 4.4.3 below. If any of the improvements on the Property are at any time located in a federally-designated special flood hazard area in which flood insurance is available, Borrower must provide Lender with flood insurance in an amount, and with deductibles, as specified by Lender. All policies of insurance on the Property, whether or not required by the terms of this Security Instrument (including but not limited to earthquake/earth movement insurance), shall name Lender as mortgagee and loss payee pursuant to a mortgage endorsement on a form acceptable to Lender, which form must provide that Lender will not have its interest voided by the act or omission of Borrower and that Lender may file a claim directly with the insurer (an "Acceptable Mortgage Endorsement"). Lender shall have the right to control or direct the proceeds of all such policies of insurance, whether or not required by the terms of this Security Instrument, as provided in Section 4.4.6 below, and all proceeds thereof are hereby assigned to Lender as security for the Secured Obligations. Each policy of insurance must have a deductible of an amount satisfactory to Lender in its sole discretion. Borrower shall be responsible for all uninsured losses and deductibles.

4.4.2 **Liability.** Borrower will maintain commercial general liability insurance on an occurrence form substantially equivalent to ISO form CG 0001 covering the legal liability of Borrower against claims occurring on, in, or about the Property with coverage of not less than \$1,000,000 per occurrence and \$2,000,000 in the aggregate, naming Lender an additional insured and having a deductible of an amount satisfactory to Lender in its sole discretion.

4.4.3 **Income Interruption.** Borrower will maintain income interruption insurance in an amount equal to at least 12 months' gross rental income from the Property as determined by Lender from time to time, and naming Lender as loss payee on an Acceptable Mortgage Endorsement. The amount collected under any and all income interruption insurance on the Property, whether or not required by this Security Instrument, shall be applied as provided in Section 4.4.6.

4.4.4 **Changes in Insurance Requirements.** Lender may change its insurance requirements from time to time throughout the term of the Secured Obligations by giving notice of such changes to Borrower. Without limiting the generality of the foregoing, Borrower shall from time to time obtain such additional coverages or make such increases in the amounts of existing coverage as may be required by written notice from Lender.



4.4.5 **General Provisions.** All policies of insurance required to be maintained by Borrower pursuant to this Section 4.4 shall: (i) be primary and noncontributory with any other insurance Borrower may carry; and (ii) be in form and substance and with companies acceptable to Lender which are authorized to conduct business in the state in which the Property is located and which have a current rating from the Best Key Rating Guide that is acceptable to Lender. Lender reserves the right, in its reasonable discretion, to increase the amount of the required coverages, require insurance against additional risks, or withdraw approval of any insurance company at any time. Borrower shall deliver to Lender evidence (in such form as Lender may require) of all insurance coverage on the Property and, if requested by Lender, a certified copy of all policies of such insurance. Borrower shall obtain renewals or replacements of any policies that expire and deliver evidence of such renewals to Lender no later than the expiration date of the policy being renewed or replaced. All policies and renewals thereof shall contain provision for ten days' notice to Lender prior to cancellation for nonpayment of premiums and 30 days' notice to Lender prior to cancellation for any other reason. If Borrower fails to maintain insurance in accordance with this Security Instrument and the other Loan Documents, Lender may, but need not, obtain insurance to protect Lender's interest in the Property ("Force Placed Insurance"). For instance, without limitation, Lender may obtain Force Placed Insurance if: (a) Borrower fails to deliver to Lender, prior to the expiration of any such required insurance coverage, evidence satisfactory to Lender that Borrower has renewed or replaced such coverage; (b) the amount of insurance is reduced below Lender's requirements; (c) the deductible is increased above Lender's requirements; or (d) the insurer providing the insurance does not meet Lender's insurance company rating requirements.

4.4.6 **Damage and Destruction.**

(a) **Borrower's Obligations.** As used in this Security Instrument, the term "Casualty Threshold Amount" means one percent of the original face principal amount of the Note. In the event of any damage to or loss or destruction of the Property (a "Casualty"): (i) if it could reasonably be expected to cost more than the Casualty Threshold Amount to repair the Casualty, Borrower shall give prompt written notice of the Casualty to Lender and to Borrower's insurer, and shall make a claim under each insurance policy providing coverage therefor; (ii) Borrower shall take such actions as are necessary or appropriate to preserve and protect the Property; (iii) if the aggregate proceeds of any and all insurance policies insuring the Property, whether or not required by this Security Instrument, that are payable as a result of the Casualty (collectively, the "Insurance Proceeds") could reasonably be expected to exceed the Casualty Threshold Amount, or if a Default exists, Borrower shall take such actions as are necessary or appropriate to ensure that all Insurance Proceeds are paid to Lender forthwith to be held by Lender until applied to the Secured Obligations or disbursed in accordance with this Section 4.4.6; and (iv) unless otherwise instructed by Lender, regardless of whether the Insurance Proceeds, if any, are sufficient for the purpose, Borrower shall promptly commence and diligently pursue to completion in a good, workmanlike and lien-free manner the restoration, replacement and rebuilding of the



Property as nearly as possible to its value, condition and character immediately prior to the Casualty (collectively, the "Restoration"). If the Restoration will cost more than the Casualty Threshold Amount to repair, Borrower shall submit the proposed plans and specifications for the Restoration, and all construction contracts, architect's contracts, other contracts in connection with the Restoration, and such other documents as Lender may reasonably request to Lender for its review and approval. Borrower shall not begin the Restoration unless and until Lender gives its written approval of such plans, specifications, contracts and other documents, with such revisions as Lender may reasonably require. Notwithstanding the foregoing, Lender shall not be responsible for the sufficiency, completeness, quality or legality of any such plans, specifications, contracts or other documents. Borrower shall pay, within ten days after demand by Lender, all costs reasonably incurred by Lender in connection with the adjustment, collection and disbursement of Insurance Proceeds pursuant to this Security Instrument or otherwise in connection with the Casualty or the Restoration.

(b) **Lender's Rights.** Lender shall have the right and power to receive and control all Insurance Proceeds required to be paid to it pursuant to subsection (a)(iii) above. So long as no Event of Default has occurred and is continuing at the time, (i) Borrower shall have the right to adjust, compromise and settle any claim under any insurance policy on the Property that is less than or equal to the Casualty Threshold Amount without the participation or consent of Lender and (ii) Lender shall have the right to participate in, and Lender's written consent shall be required for, any adjustment, compromise or settlement of any such claim exceeding the Casualty Threshold Amount. If an Event of Default has occurred and is continuing at the time, Borrower hereby irrevocably empowers Lender, in the name of Borrower, as Borrower's true and lawful attorney in fact, to commence, appear in, defend, prosecute, adjust, compromise and settle all claims under any insurance policy on the Property; provided, however, Lender shall not be responsible for any failure to undertake any or all of such actions regardless of the cause of the failure. Borrower will pay Lender's expenses reasonably incurred in the adjustment, collection and disbursement of such Insurance Proceeds or otherwise in connection with the Casualty or the Restoration. Each insurance company concerned is hereby irrevocably authorized and directed to make payment of all Insurance Proceeds directly to Lender. Notwithstanding anything to the contrary, Lender shall not be responsible for any such insurance, the collection of any Insurance Proceeds, or the insolvency of any insurer.

(c) **Application of Proceeds.** If, at any time while Lender holds any Insurance Proceeds, an Event of Default exists or Lender determines in its reasonable discretion that the security for the Secured Obligations is impaired, Lender shall have the option, in its sole discretion, to apply the Insurance Proceeds to the Secured Obligations in such order as Lender may determine (or to hold such Insurance Proceeds for future application to the Secured Obligations). Without limiting the generality of the foregoing, Lender's security will be deemed to be impaired if: (i) an Event of Default exists; (ii) Borrower fails to satisfy any condition precedent to disbursement of Insurance Proceeds to pay the cost of the Restoration within a reasonable time; or (iii) Lender determines in its



reasonable discretion that it could reasonably be expected that (A) Borrower will not have sufficient funds to complete the Restoration and timely pay all expenses of the Property and all payments due under the Note and the other Loan Documents through the completion of the Restoration and any leaseup period thereafter, (B) the rental income from the Property will be insufficient to timely pay all expenses of the Property and payments due under the Note and the other Loan Documents on an ongoing basis after completion of the Restoration, or (C) the Restoration cannot be completed at least six months prior to the maturity date of the Note and within one year after the date of the Casualty.

(d) **Disbursement of Proceeds.** If Lender is not entitled to apply the Insurance Proceeds to the Secured Obligations, Lender (or at Lender's election, a disbursing or escrow agent selected by Lender and whose fees shall be paid by Borrower) shall disburse the Insurance Proceeds for the Restoration from time to time as the Restoration progresses, but only after satisfaction, at Borrower's expense, of such conditions precedent to such disbursements as Lender may reasonably require including but not limited to the following: (i) Borrower shall have delivered to Lender evidence reasonably satisfactory to Lender of the estimated cost of the Restoration; (ii) Lender shall have approved the plans, specifications and contracts for the Restoration as required by Section 4.4.6(a); (iii) Borrower shall have delivered to Lender funds in addition to the Insurance Proceeds in an amount sufficient in Lender's reasonable judgment to complete and fully pay for the Restoration; (iv) Borrower shall have delivered to Lender such building permits, other permits, architect's certificates, waivers of lien, contractor's sworn statements, title insurance endorsements, plats of survey and other evidence of cost, payment and performance as Lender may reasonably require and approve; and (v) if required by Lender, Borrower shall have entered into an agreement providing in greater detail for the Restoration, the disbursement of Insurance Proceeds and related matters. No payment made prior to the final completion of the Restoration shall exceed ninety percent of the value of the work performed and materials incorporated into the Property from time to time, as such value is determined by Lender in its reasonable judgment. Disbursements may, at Lender's election, be made on a percentage of completion basis or on such other basis as is acceptable to Lender. Disbursements shall be subject to Borrower's delivery of such lien waivers and paid receipts as Lender may require, and otherwise on terms and subject to conditions acceptable to Lender. From time to time after commencement of the Restoration, if so requested by Lender, Borrower shall deposit with Lender funds in excess of the Insurance Proceeds which, together with the Insurance Proceeds and all funds previously deposited with Lender in connection with the Restoration, must at all times be at least sufficient in the reasonable judgment of Lender to pay the entire unpaid cost of the Restoration. Funds so deposited by Borrower may at Lender's option be disbursed prior to the disbursement of Insurance Proceeds. Lender may retain a construction consultant to inspect the Restoration and related matters on Lender's behalf and to advise Lender with respect thereto and Borrower shall pay the cost thereof; provided that neither Borrower nor any other person or entity other than Lender shall have any right to rely on any inspection or advice of such consultant. Such consultant shall not be the agent of Lender and shall not have the power to bind Lender in any way. Any surplus Insurance Proceeds or other



funds held by Lender pursuant to this Section 4.4.6 that may remain after payment of all costs of the Restoration shall be paid to Borrower (or to such other person or entity as Lender reasonably determines is entitled thereto) so long as no Default then exists. No interest shall be allowed to Borrower on account of any Insurance Proceeds or other funds held by Lender pursuant to this Section 4.4.6, but at Borrower's request, Lender will deposit such amounts into a blocked interest-bearing account with Lender over which Lender has sole possession, authority and control, in which Lender has a perfected first-priority security interest to secure the Secured Obligations, and otherwise on terms and conditions satisfactory to Lender in its sole discretion. Notwithstanding the above, if an Event of Default exists prior to full disbursement of the Insurance Proceeds and any other funds held by Lender pursuant to this Section 4.4.6, any undisbursed portion thereof may, at Lender's option, be applied against the Secured Obligations, whether or not then due, in such order and manner as Lender shall select.

(e) **Effect on the Indebtedness.** Any reduction in the Secured Obligations resulting from the application of Insurance Proceeds or other funds pursuant to this subsection 4.4.6 shall be deemed to take effect only on the date of such application; provided that, if any Insurance Proceeds are received after the Property is sold in connection with a judicial or nonjudicial foreclosure of this Security Instrument, or is transferred by deed in lieu of such foreclosure, notwithstanding any limitation on Borrower's liability contained herein or in the Note, the purchaser at such sale (or the grantee under such deed) shall have the right to receive and retain all such Insurance Proceeds and all unearned premiums for all insurance on the Property. No application of Insurance Proceeds or other funds to the Secured Obligations shall result in any adjustment in the amount or due dates of installments due under the Note. No application of Insurance Proceeds to the Secured Obligations shall, by itself, cure or waive any Default or any notice of default under this Security Instrument or invalidate any act done pursuant to such notice or result in the waiver of any collateral securing the Note.

(f) **Conflicts Among Documents.** To the extent of any inconsistency between the provisions of this Section 4.4.6 and the provisions of the Loan Agreement regarding the settlement, collection and application of Insurance Proceeds and condemnation Awards, the provisions of the Loan Agreement will govern prior to the Permanent Term Commencement Date (as defined in the Note). Thereafter, the provisions of this Section 4.4.6 will govern such matters.

4.5 **Right of Inspection.** Subject to the rights of tenants, Borrower shall permit Lender or its agents or independent contractors (including, but not limited to, appraisers, environmental consultants and construction consultants), at all reasonable times, to enter upon and inspect the Property.

4.6 **Compliance With Laws, Etc.; Preservation of Licenses.** Borrower shall comply in all material respects with (a) all laws, statutes, ordinances, rules, regulations,



licenses, permits, approvals, orders, judgments and other requirements of governmental authorities relating to the Property or Borrower's use thereof, and (b) all easements, licenses and agreements relating to the Property or Borrower's use thereof. Borrower shall observe and comply with all requirements necessary to the continued existence and validity of all rights, licenses, permits, privileges, franchises and concessions relating to any existing or presently contemplated use of the Property, including but not limited to any zoning variances, special exceptions and nonconforming use permits.

4.7 **Further Assurances.** Borrower will, at its expense, from time to time execute and deliver any and all such instruments of further assurance and other instruments and do any and all such acts, or cause the same to be done, as Trustee or Lender deems necessary or advisable to grant the Property to Trustee or to carry out more effectively the purposes of this Security Instrument.

4.8 **Legal Actions.** Borrower will appear in and defend any action or proceeding before any court or administrative body purporting to affect the security hereof or the rights or powers of Lender or Trustee; and will pay all costs and expenses, including cost of evidence of title, title insurance premiums and any fees of attorneys, appraisers, environmental inspectors and others, incurred by Lender or Trustee, in a reasonable sum, in any such action or proceeding in which Lender or Trustee may appear, in any suit brought by Lender or Trustee to foreclose this Security Instrument and in any nonjudicial foreclosure under this Security Instrument.

4.9 **Taxes, Assessments and Other Liens.** To the extent that Borrower has not deposited funds for payment thereof with Lender pursuant to Section 4.16 below, Borrower will pay prior to delinquency all taxes, assessments, encumbrances, charges and liens on the Property or any part thereof, including but not limited to any tax on or measured by rents of the Property, the Note, this Security Instrument, or any Secured Obligation or part thereof.

4.10 **Expenses.** Borrower will pay all costs, fees and expenses reasonably incurred by Lender or Trustee in connection with this Security Instrument.

4.11 **Repayment of Expenditures.** Borrower will pay within five days after written demand all amounts expended by Lender and reimbursable to Lender by Borrower pursuant to this Security Instrument or the other Loan Documents, together with interest thereon from the date of expenditure by Lender at the rate of interest borne by the Note, and the repayment thereof shall be secured by this Security Instrument.

4.12 **Financial and Operating Information.** Borrower shall provide Lender with financial and operating information as provided in the Loan Agreement.



4.13 **Sale, Transfer or Encumbrance of the Property.** Borrower shall not, without the prior written consent of Lender, sell, transfer, otherwise convey or further encumber the Property or any interest therein, or agree to do any of the foregoing without first repaying in full the Note and all other Secured Obligations. Lender may withhold its consent to any of the foregoing in its sole discretion and, if such consent is granted, Lender may impose such conditions thereto as it may elect in its sole discretion. Consent to any one such occurrence shall not be deemed a waiver of the right to require consent to any future occurrences.

4.14 **Borrower Existence.** If Borrower is a corporation, partnership, limited liability company or other entity, Lender is making the Loan in reliance on Borrower's continued existence, ownership and control in its present form. Borrower will not alter its name, jurisdiction of organization, structure, ownership or control without the prior written consent of Lender and will do all things necessary to preserve and maintain said existence and to ensure its continuous right to carry on its business. If Borrower is a partnership, Borrower will not permit the addition, removal or withdrawal of any general partner without the prior written consent of Lender. The withdrawal or expulsion of any general partner from Borrower partnership shall not in any way affect the liability of the withdrawing or expelled general partner hereunder or on the Note.

4.15 **Information for Participants, Etc.** Borrower agrees to furnish such information and confirmation as may be required from time to time by Lender on request of potential loan participants and assignees and agrees to make adjustments in this Security Instrument, the Note, and the other documents evidencing or securing the Loan to accommodate such participant's or assignee's requirements, provided that such requirements do not vary the economic terms of the Loan. Borrower hereby authorizes Lender to disclose to potential participants and assignees any information in Lender's possession with respect to Borrower, any guarantors of the Loan, principals in Borrower or in such guarantors, the Property and the Loan.

4.16 **Tax and Insurance Impounds.**

(a) **Impounds.** In addition to the payments required by the Note, Borrower agrees to pay Lender, at Lender's request, such sums as Lender may from time to time estimate will be required: (i) to pay, at least one month before delinquency, the next due taxes, assessments, ground rents, insurance premiums and similar charges affecting the Property (collectively, the "Impositions"), less all sums already paid therefor divided by the number of months to elapse before one month prior to the date when the applicable Impositions will become delinquent; and (ii) at the option of Lender, to maintain a reserve equal to one-sixth of the total annual amount of the Impositions. Lender shall hold such amounts without interest or other income to Borrower to pay Impositions. Should this estimate of the Impositions prove insufficient, Borrower upon demand shall pay Lender such additional sums as may be required to pay the Impositions at least one month before delinquency.



(b) **Application.** If the total of the payments to Lender under subsection (a) of this Section (collectively, the "Impounds") in any one year exceed the amounts actually paid by Lender for Impositions, such excess may be credited by Lender on subsequent payments under this section. At any time after the occurrence and during the continuance of an Event of Default and at or prior to the foreclosure sale, Lender may apply any balance of Impounds it holds to any of the Secured Obligations and in such order as Lender may elect. If Lender does not so apply such Impounds at or prior to the foreclosure sale, the purchaser at such sale shall be entitled to all such Impounds. If Lender acquires the Property in lieu of realizing on this Security Instrument, the balance of Impounds it holds shall become the property of Lender. Any transfer in fee of all or a part of the Property shall automatically transfer to the grantee all or a proportionate part of Borrower's rights and interest in the Impounds.

(c) **Tax Reporting Service.** Lender may, but need not, contract with a tax reporting service covering the Property. Borrower agrees that Lender may rely on the information furnished by such tax service and agrees to pay the cost of that service within 30 days after receipt of a billing for it.

(d) **Limited Waiver.** Notwithstanding the foregoing, Lender will not require Borrower to deposit the Impounds as provided in subsection (a) of this Section so long as: (i) the Property is owned in its entirety by the original Borrower named below (and not by any successor or transferee Borrower) and there is no change in the individuals exercising day-to-day powers of decision-making, management and control over either Borrower or the Property (regardless of whether Lender has consented to any such transfer or change); (ii) Borrower pays, prior to delinquency, all payments of Impositions that would otherwise be paid from the Impounds and, if required by Lender, Borrower provides Lender with proof of such payment; and (iii) no Event of Default occurs (regardless of whether it is later cured). If at any time Borrower fails to meet any of the foregoing requirements, Lender may at any time thereafter require the payment of all Impounds upon ten days written notice to Borrower.

4.17 **Leasing Matters.**

(a) **Lease Representations and Warranties.** As of the date hereof, except as otherwise noted in an estoppel certificate delivered to and accepted by Lender in connection with the Loan: (i) Borrower is the sole owner of the entire lessor's interest in the Leases; (ii) the Leases are the valid, binding and enforceable obligations of Borrower and the applicable tenant or lessee thereunder; (iii) the terms of all alterations, modifications and amendments to the Leases have been disclosed to Lender in writing; (iv) none of the Rents reserved in the Leases have been assigned or otherwise pledged or hypothecated except to Lender; (v) none of the Rents have been collected for more than one month in advance; (vi) the premises demised under the Leases have been completed and the



tenants under the Leases have accepted the same and have taken possession of the same on a rent-paying basis; (vii) there exists no offset or defense to the payment of any portion of the Rents; (viii) no Lease contains an option to purchase, right of first refusal to purchase, expansion right, or any other similar provision; and (ix) no person or entity has any possessory interest in, or right to occupy the Property, except under and pursuant to a Lease that has been delivered to Lender.

(b) **Lease Covenants; Retenancing Reserve.** Borrower shall not alter, modify, amend or change the terms of any of the Leases or give any consent or permission or exercise any option required or permitted by the terms thereof or waive any obligation required to be performed by any lessee or execute, cancel or terminate any of the Leases or accept a surrender thereof or enter into Leases after the date hereof without the prior written consent of Lender. Borrower shall deliver to Lender, promptly upon receipt thereof, copies of any and all demands, claims and notices of default received by Borrower from any lessee under any of the Leases. Borrower shall keep and perform, in all material respects, all terms, conditions and covenants required to be performed by lessor under the Leases. Borrower shall, in all material respects, enforce the Leases and all remedies available to Borrower against the lessees thereunder in case of default under the Leases by lessees. Borrower shall forthwith deposit with Lender any sums received by Borrower in consideration of any full or partial termination, modification or amendment of any Lease or any release or discharge of any tenant under any Lease from any obligation thereunder and any such sums received by Borrower shall be held in trust by Borrower for such purpose. Notwithstanding the foregoing, so long as no Event of Default exists, the portion of any such sum received by Borrower with respect to any Lease that is less than five percent of the original amount of the Note shall be payable to Borrower. All such sums received by Lender with respect to any Lease shall be deemed a reserve (the "Retenancing Reserve") for the costs of retenancing the space affected by the termination, modification or amendment and shall be deposited by Lender into a pledged account with Lender and under the sole control of Lender. Borrower hereby grants Lender a security interest in such account and in all funds from time to time on deposit therein as collateral security for all Secured Obligations. If no Event of Default exists, Lender shall release the Retenancing Reserve to Borrower from time to time as necessary to pay or reimburse Borrower for such tenant improvements, leasing commissions and other leasing costs as may be required to retenant the affected space; provided, however, Lender shall have received and approved each of the following for each tenant for which such costs were incurred: (i) Borrower's written request for such release, including the name of the tenant, the location and net rentable area of the space and a description and cost breakdown of the tenant improvements or other leasing costs covered by the request; (ii) Borrower's certification that any tenant improvements have been completed lien-free and in a workmanlike manner; (iii) a fully executed Lease, or extension or renewal of the current Lease as approved by Lender (or otherwise permitted as provided below); (iv) an estoppel certificate executed by the tenant including its acknowledgement that all tenant improvements have been satisfactorily completed; (v) the agreement pursuant to which any leasing commission is owing; and (vi) such other information with respect to such costs as Lender



may require. Following the retenancing of all affected space (including, without limitation, the completion of all tenant improvements), and provided no Event of Default exists, Lender shall release any remaining Retenancing Reserve relating to the affected space to Borrower. Borrower shall construct all tenant improvements in a workmanlike manner and in accordance with all applicable laws, ordinances, rules and regulations.

(c) **Permitted Leases.** Notwithstanding the foregoing, Borrower shall be permitted, in the ordinary course of business, to enter into, extend, renew, amend or modify (but not terminate) any Lease that covers less than 20% of the net rentable area of the Property and generates less than 20% of the annual Rent from the Property without Lender's specific prior written consent; provided that all of the following conditions are satisfied:

- (i) No Event of Default exists;
- (ii) No purchase option, right of first refusal or expansion right is thereby granted;
- (iii) A new Lease must be commercially reasonable and executed on a standard lease form that has previously been approved in writing by Lender (the "Standard Form") with only minor non-material changes or pre-approved changes to the Standard Form;
- (iv) The same (A) is in the ordinary course of business of Borrower; (B) is commercially reasonable; (C) does not involve the relocation of a tenant to space not located within the Property; and (D) does not provide for reduction of rent or other tenant reimbursement amounts;
- (v) The same does not and will not cause a default under the Ground Lease, any Lease, or any other document or instrument (recorded or otherwise) in any way burdening or affecting the Property; and
- (vi) The tenant's business does not and will not involve the presence of any Hazardous Substance (as defined in the Indemnity Agreement) on the Property (other than medical supplies, medical wastes and supplies for cleaning or maintenance, all in commercially reasonable amounts required for use in the ordinary course of business, provided the Lease requires that such items be stored, used and disposed of in compliance with all applicable laws, rules and regulations).

Borrower shall furnish to Lender a true and complete copy of each fully-executed Lease, extension, renewal, amendment or modification of lease, hereafter made by Borrower with respect to space in the Property within 30 days after delivery of each such Lease, extension, renewal, amendment or modification by the parties thereto. The delivery by



Borrower of each Lease, extension, renewal, amendment or modification that does not require Lender's specific consent hereunder shall constitute a representation by Borrower that the conditions contained in this Section have been complied with.

(d) **Tenant Estoppel Certificates.** Within 30 days after request by Lender, Borrower shall deliver to Lender and to any party designated by Lender, estoppel certificates relating to the Leases executed by Borrower and by each of the tenants, in form and substance acceptable to Lender; provided, however, if any tenant shall fail or refuse to so execute and deliver any such estoppel certificate upon request, Borrower shall use reasonable efforts to cause such tenant to execute and deliver such estoppel certificate but such tenant's continued failure or refusal to do so, despite Borrower's reasonable efforts, shall not constitute a Default by Borrower under this Section.

(e) **Right of Subordination.** Notwithstanding anything in this Security Instrument to the contrary, Lender may, upon written notice to Borrower, elect to: (i) exclude from the assignment provided in this Security Instrument any of the Leases as specified in such notice so that the interest under such specified Lease is not assigned to Lender; (ii) subordinate the lien and other terms and provisions of this Security Instrument to any of the Leases as indicated in such notice to Borrower; and (iii) require Borrower to use best efforts to obtain a subordination, nondisturbance and attornment agreement, in form and substance approved by Lender, from any of the lessees under any of the Leases as indicated in such notice to Borrower.

(f) **Letters of Credit.** Borrower shall notify Lender in writing prior to becoming the beneficiary under any letter of credit supporting any of the Leases, or otherwise in connection with the Property, and will take all actions, and execute all documents, necessary or appropriate to give Lender control (as defined in the Uniform Commercial Code, as enacted by any relevant jurisdiction, including but not limited to such jurisdiction's version of Section 9-107 thereof) of such letter of credit and all letter of credit rights thereunder and, if so required by Lender, to constitute Lender the transferee beneficiary of such letter of credit.

(g) **Security Deposits.** Borrower shall maintain all security deposits collected from tenants or others with respect to the Property in accordance with all applicable legal requirements.

4.18 **Use of Property; Zoning Changes.** Unless required by applicable law or approved by Lender in writing, Borrower shall not: (a) allow any material change in the use to which the Property is being put by Borrower as an owner-occupant of the Property; or (b) initiate or acquiesce in a change in the zoning classification of the Property.

4.19 **Publicity.** Borrower hereby grants permission to Lender and any subsequent holder of the Loan to issue press releases, advertisements and other promotional



materials concerning the financing of the Property, which materials may include the property name and description, loan amount, major tenants, loan term and amortization and the identity of Borrower and any guarantors.

4.20 **Construction Mortgage.** This Security Instrument shall constitute a "construction mortgage" as that term is defined in the version of Uniform Commercial Code Sections 9-334 and 2A-309 enacted in the state where the land described in Exhibit A is located.

4.21 **Condominium Covenants.** The Property includes three units (collectively, the "Condominium Units") in, together with an undivided interest in the common elements of, a condominium project known as the Island Medical Center Condominium (the "Condominium Project"). The Property also includes Borrower's interest in the owners' association (the "Owners' Association") and the uses, proceeds and benefits of Borrower's interest.

4.21.1 **Condominium Obligations.** Borrower shall perform all of Borrower's obligations under the Condominium Project's Constituent Documents (as defined below) as the same may be amended from time to time. The "Constituent Documents" are the: (i) declaration or any other document that creates the Condominium Project, (ii) rules and regulations affecting the Condominium Project and adopted or promulgated by the Owners' Association; and (iii) other equivalent documents. Borrower shall promptly pay, when due, all dues and assessments imposed pursuant to the Constituent Documents.

4.21.2 **Hazard Insurance.** So long as the Owners' Association maintains, with an accepted insurance carrier acceptable to Lender, a "master" or "blanket" policy on the Condominium Project that is satisfactory to Lender and that provides insurance coverage in the amounts, for the periods and against the hazards Lender requires, then:

(a) Lender waives the provision in subsection 4.16 for the payment to Lender of the premium installments for hazard insurance on the Property; and

(b) Borrower's obligation under subsection 4.4.1 to maintain hazard insurance on the Property is deemed satisfied to the extent that the required coverage is provided by the Owners' Association policy.

Borrower shall give Lender prompt notice of any lapse in required insurance coverage. In the event of a distribution of hazard insurance proceeds in lieu of restoration or repair following a loss to the Property, whether to the Condominium Units or to common elements, any proceeds payable to Borrower are hereby assigned and shall be paid to Lender for application by Lender as provided in this Security Instrument.



4.21.3 **Public Liability Insurance.** Borrower shall take such actions as may be reasonable to ensure that the Owners' Association maintains a public liability insurance policy acceptable in form, amount and extent of coverage to Lender.

4.21.4 **Condemnation.** The proceeds of any award or claim for damages, direct or consequential, payable to Borrower in connection with any condemnation or other taking of all or any part of the Property, whether of the Condominium Units or of the common elements, or for any conveyance in lieu of condemnation, are hereby assigned and shall be paid to Lender. Such proceeds shall be applied by Lender as provided in this Security Instrument.

4.21.5 **Lender's Prior Consent.** Borrower shall not, except after notice to Lender and with Lender's prior written consent, either partition or subdivide the Property or consent to:

(a) Abandonment or termination of the Condominium Project, except for abandonment or termination required by law in the case of substantial destruction by fire or other casualty or in the case of a taking by condemnation or eminent domain;

(b) Any material amendment to any provision of the Constituent Documents, including, but not limited to, any amendment that would change the percentage interest of the Unit owners in the Condominium Project;

(c) Termination of professional management and assumption of self-management of the Owners' Association; or

(d) Any action that would have the effect of rendering the public liability insurance coverage maintained by the Owners' Association unacceptable to Lender.

4.21.6 **Voting Rights; Notice of Meetings.** Borrower hereby assigns to Lender all of Borrower's voting rights under the Constituent Documents and irrevocably appoints Lender as its attorney and proxy to cast its votes at all times permitted or required pursuant thereto at any time after the occurrence of an Event of Default. If Lender's representative fails to attend a duly called meeting either in person or by proxy, then Borrower may cast its votes as though this power had not been granted to Lender. It is agreed that this power is coupled with an interest and may not be revoked by Borrower until this Security Instrument is fully satisfied and reconveyed of record. Borrower will, from time to time, execute and deliver to Lender such other proxies as Lender deems necessary or advisable to further confirm Lender as Borrower's proxy hereunder. Borrower agrees that it will cause copies of all notices of meetings and other notices required or permitted under the

Constituent Documents to be sent to Lender promptly so as to provide Lender with a reasonable opportunity to respond thereto.

4.21.7 **Remedies.** If Borrower does not pay condominium dues and assessments when due, Lender may pay them. Any amounts disbursed by Lender under this subsection 4.21.7 shall become additional Secured Obligations from the date of disbursement, shall bear interest at the Default Rate specified in the Note and shall be payable, with interest, upon notice from Lender to Borrower requesting payment.

4.22 **Ground Lease.**

(a) Borrower will in all respects promptly and faithfully keep, perform and comply with all of the terms, provisions, covenants, conditions and agreements of the tenant under the Ground Lease ("Ground Tenant") and will promptly enforce its rights to require other parties to the Ground Lease to comply with all their material obligations thereunder. Borrower shall immediately furnish to Lender all notices of default and other material notices given by any party under the Ground Lease. Lender shall have the right to participate in all legal proceedings, including but not limited to mediation, arbitration and bankruptcy proceedings, affecting or pertaining to the Ground Lease or the property leased under the Ground Lease and Borrower shall pay all attorneys' fees and other costs incurred by Lender in connection with such legal proceedings.

(b) Borrower hereby assigns and sets over to Lender, as security for the obligations secured by this Security Instrument, all right, title and interest in and to Borrower's interest in the Ground Lease, including, without limitation, Borrower's options to extend the term of the Ground Lease, if any, and Lender shall have the right and power to exercise such options on behalf of Borrower at any time that Borrower could do so if, in the sole judgment of Lender, it is appropriate to do so in order to protect Lender's interests. Borrower hereby grants to Lender a power of attorney to execute and deliver such extension notices on behalf of Borrower, it being stipulated that such power of attorney is coupled with an interest and irrevocable for so long as this Security Instrument remains in effect. Upon the request of Lender, Borrower shall execute any documents or instruments reasonably requested by Lender or Ground Lessor in order to confirm the existence of the power of attorney set forth in this subsection, including, without limitation, a separate power of attorney in recordable form with respect to the matters covered by this subsection. Lender shall further have a power of attorney, it being stipulated that such power of attorney is coupled with an interest and is irrevocable for so long as this Security Instrument remains in effect, to execute any and all other documents required by this Security Instrument with respect to the Ground Lease, and to perform any and all acts required of Borrower under this Security Instrument, if Borrower fails to do so promptly after demand by Lender.

(c) In the event Borrower or any other Ground Tenant fails to make any payment required under the Ground Lease or to perform any other obligation of



Ground Tenant under the Ground Lease in a timely fashion, in addition to any such failure constituting an Event of Default under this Security Instrument, Lender may, at its option make the defaulted payment or perform the obligation and, if it does so: (i) Borrower shall reimburse Lender upon demand for all such payments and all other costs and expenses incurred by Lender in connection with such failure by Borrower, together with interest thereon at the Default Rate from the date such amounts are paid by Lender until reimbursed by Borrower; and (ii) Lender may add all amounts described in the foregoing clause (i) to the amount secured by this Security Instrument without waiving any of its rights under this Security Instrument or the other Loan Documents.

(d) No merger shall occur by reason of any acquisition by Borrower or any other person or entity of any additional right, title, interest or estate in or to the property leased under the Ground Lease or any part thereof. Without limiting the generality of the foregoing, unless Lender otherwise expressly consents in writing, which consent may be withheld by Lender in its sole discretion, the leasehold estate under the Ground Lease and any other interest or estate in such property shall not merge but shall always remain separate and distinct, notwithstanding any common ownership of the leasehold estate and any other interest or estate.

(e) If Borrower, at any time prior to the payment in full of all indebtedness secured by this Security Instrument, acquires fee title to the property leased under the Ground Lease or any other interest in such property, such fee title or other interest shall immediately and automatically, without further action on the part of Borrower, Lender or any other person or entity, become subject to the lien of this Security Instrument. In the event of such acquisition by Borrower, Borrower shall execute and deliver to Lender such further instruments, conveyances and assurances as Lender may request in order to further confirm and assure that the fee title or other interest so acquired by Borrower is subject to the terms, provisions and lien of this Security Instrument.

(f) Borrower will not enter into, or permit, any modification, amendment, termination, cancellation, surrender, subordination or replacement of the Ground Lease without Lender's prior written consent.

4.23 **Certain Bankruptcy and Insolvency Proceedings.** If Ground Lessor, Borrower or any other Ground Tenant becomes a debtor in any case or proceeding (each, a "Proceeding") under the United States Bankruptcy Code, title 11 U.S.C., or any successor thereto, as now or hereafter in effect (as applicable, the "Bankruptcy Code"), or under any other insolvency law:

(a) Borrower shall immediately notify Lender in writing of the pendency of such Proceeding and thereafter shall immediately provide Lender with copies of all notices and pleadings in any way affecting, proposing to affect or purporting to affect the Ground Lease or the Property including but not limited to any and all notices and



pleadings relating to any proposed assumption or rejection of the Ground Lease or any proposed sale of the Property or of Ground Lessor's interest in the Ground Lease.

(b) If, in connection with a Proceeding in which Ground Tenant is the debtor, the Ground Lease is rejected, in addition to all other rights Lender may have, such rejection shall be deemed an assignment by Ground Tenant to Lender (or to such designee of Lender as Lender may specify by written notice) of the leasehold estate and all of Ground Tenant's interest under or arising out of the Ground Lease, in the nature of an assignment in lieu of foreclosure (without in any way satisfying any portion of the obligations secured by this Security Instrument), and the Ground Lease shall not terminate, unless Lender shall reject such deemed assignment by written notice to Ground Lessor within 30 days following Lender's receipt of written notice of the rejection of the Ground Lease. No such deemed assignment shall constitute an assumption by Lender of Ground Tenant's obligations under the Ground Lease.

(c) If, in connection with a Proceeding in which Ground Lessor is the debtor, the Ground Lease is rejected:

(i) Borrower shall not have the right to treat the Ground Lease as terminated except with the prior written consent of Lender, which may be granted or withheld in Lender's sole discretion, and Borrower hereby assigns to Lender, as security for the obligations secured by this Security Instrument, the right under Bankruptcy Code Section 365(h), or any successor thereto or similar provision of any law, to elect to treat the Ground Lease as terminated in such event.

(ii) If the Ground Lease is not treated as terminated in accordance with subsection (c)(i) above, then the Ground Lease shall continue in effect upon all the terms and conditions set forth therein and the lien of this Security Instrument shall extend to the continuing possessory rights and other rights of Ground Tenant following such rejection (whether under the Ground Lease, Bankruptcy Code Section 365 or otherwise) with the same priority as it would have enjoyed had such rejection not taken place.

(iii) If Ground Lessor seeks permission of a bankruptcy court or other applicable court or governing body to sell or transfer any of the property covered by the Ground Lease free and clear of the Ground Lease under Section 363(f) of the Bankruptcy Code or any successor thereto or similar provision of any law, unless otherwise directed in writing by Lender, Borrower (A) shall not consent to such attempted sale or transfer, (B) shall timely file a written objection thereto, and (C) shall timely assert and pursue its right to adequate protection of its leasehold estate, in a manner acceptable to Lender, under Section 363(e) of the Bankruptcy Code or any successor thereto or similar provision of any law.



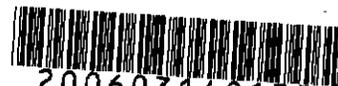
(d) The lien of this Security Instrument does and shall encumber and attach to all of Borrower's rights and remedies at any time arising under or pursuant to Sections 361, 363 and 365 of the Bankruptcy Code, or any successor thereto or similar provisions of any law, including without limitation, all of Borrower's rights to remain in possession of the Property and the leasehold estate under the Ground Lease.

(e) Borrower hereby appoints Lender as its attorney in fact to act on behalf of Borrower in connection with all matters relating to or arising out of the assumption, rejection or termination of the Ground Lease, or out of the sale or proposed sale of the Property or any part thereof, in any Proceeding. This grant of power of attorney is present, unconditional, irrevocable, durable and coupled with an interest.

4.24 **Management of Property.** Borrower represents and warrants that, as of the date hereof, no third party management company has been engaged to manage the Property. In the event that Borrower decides to engage a third-party management company to manage the Property, Borrower agrees to engage a management company satisfactory to Lender, pursuant to a management agreement satisfactory to Lender, and to execute, and to cause such management company to execute, an agreement assigning the management agreement to Lender, subordinating such management agreement and the terms thereof, including but not limited to such management company's right to payment of management fees, and containing certain other agreements of Borrower and such management company, in Lender's then-current form of such agreement (the "Assignment of Management Agreement"), and to deliver to Lender promptly upon such engagement, a fully-executed copy of the management agreement, together with the Assignment of Management Agreement signed by Borrower and such manager.

4.25 **Debt Service Coverage Ratio.** Borrower will not permit the Debt Service Coverage Ratio (as defined below) to be less than 1.15 to 1.00 (the "Minimum Debt Service Coverage Ratio") for any fiscal year of Borrower. As used herein, "Debt Service Coverage Ratio" means the ratio, calculated annually as of the close of each of Borrower's fiscal years, of (a) the gross rental or operating income actually collected by Borrower from the Property during the previous twelve months less operating expenses incurred for the Property during such period (excluding depreciation, amortization and payments on the obligations secured by this Security Instrument), to (b) all principal and interest payments required under the obligations secured by this Security Instrument. Lender will calculate the Debt Service Coverage Ratio in accordance with a methodology established by Lender in its reasonable discretion and, in doing so, may: (i) employ estimates made by Lender in good faith of relevant factors including but not limited to the interest rate on the Note for the relevant time period if that interest rate is variable during that period; and (ii) employ such other good faith assumptions as Lender may determine in its sole discretion.

4.26 **Improvements to Remain Real Property.** Notwithstanding any current or future severance of ownership of any improvements now or hereafter located on the



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land described as Parcel 1 in Exhibit A attached hereto from the ownership of such land, such improvements shall at all times be and remain real property.

5. **DEFAULT.**

5.1 **Definition.** Any of the following shall constitute an "Event of Default" as that term is used in this Security Instrument (and the term "Default" shall mean any of the following, whether or not any requirement for notice or lapse of time has been satisfied):

(a) Any regular monthly payment under the Note is not paid so that it is received by Lender within 10 days after the date when due, or any other Secured Obligation (including but not limited to any payment of principal or interest due on the Maturity Date, as defined in the Note) is not paid so that it is received by Lender when due;

(b) Any representation or warranty made by Borrower to or for the benefit of Lender herein or elsewhere in connection with the Loan, including but not limited to any representation in connection with the security therefor, proves to have been incorrect or misleading in any material respect;

(c) Borrower or any other party thereto (other than Lender) fails to perform its obligations under any other covenant or agreement contained in this Security Instrument, the Note, any other Loan Document or the Indemnity Agreement, which failure continues for a period of 30 days after written notice of such failure by Lender to Borrower, but no such notice or cure period shall apply in the case of: (i) any such failure that could, in Lender's judgment, absent immediate exercise by Lender of a right or remedy under this Security Instrument, the other Loan Documents or the Indemnity Agreement, result in harm to Lender, impairment of the Note or this Security Instrument or any other security given under any other Loan Document; (ii) any such failure that is not reasonably susceptible of being cured during such 30-day period; (iii) breach of any provision that contains an express cure period; or (iv) any breach of Section 4.13 or Section 4.14 of this Security Instrument;

(d) Borrower or any other person or entity liable for the repayment of the Secured Obligations becomes unable or admit in writing its inability to pay its debts as they become due, or file, or has filed against it, a voluntary or involuntary petition in bankruptcy, or makes a general assignment for the benefit of creditors, or becomes the subject of any other receivership or insolvency proceeding, provided that if such petition or proceeding is not filed or acquiesced in by Borrower or the subject thereof, it shall constitute an Event of Default only if it is not dismissed within 60 days after it is filed or if prior to that time the court enters an order substantially granting the relief sought therein;

(e) Borrower or any other signatory thereto defaults in the performance of any covenant or agreement contained in any mortgage, deed of trust or similar

security instrument encumbering the Property, or the note or any other agreement evidencing or securing the indebtedness secured thereby, which default continues beyond any applicable cure period;

(f) A tax, charge or lien is placed upon or measured by the Note, this Security Instrument, or any Secured Obligation that Borrower does not or may not legally pay in addition to the payment of all principal and interest as provided in the Note;

(g) Construction of the Improvements (as defined in the Loan Agreement) is abandoned or, subject to any extension provided for by the Loan Agreement, is not completed by the Completion Date (as defined in the Loan Agreement);

(h) A court of competent jurisdiction enters an order enjoining construction of the Improvements, or such a court or an authorized governmental agency orders that leasing of the Improvements be suspended or halted, or any approval, license or permit required for construction or operation of the Improvements is withdrawn or suspended, and the order, withdrawal or suspension remains in effect for a period of 30 days;

(i) Borrower is in default under any Project Contract (as defined in the Loan Agreement) after the expiration of any applicable grace or cure period;

(j) Borrower fails to satisfy the conditions to Disbursements (as defined in the Loan Agreement) for a period in excess of 30 days at any time prior to final completion of the Improvements and payment of all costs thereof;

(k) Damage to or destruction of the Property or Improvements by fire or other casualty, whether insured against or not, where Lender determines, in its sole discretion, that such damage or destruction cannot be repaired and the Improvements completed in accordance with the Loan Agreement;

(l) A material adverse change in the assets, liabilities or financial position of any of Borrower or Guarantor;

(m) Any of Borrower or Guarantor dies or becomes incompetent, or revokes or disputes the validity of, or its liability under, the Loan Documents or any thereof;

(n) The bankruptcy or insolvency of Contractor (as defined in the Loan Agreement) or the withdrawal of Contractor from proceeding with construction of the Improvements;

(o) The filing or making of any claim or lien against the Property, the Improvements or the undisbursed proceeds of the Loan, including but not



limited to receipt by Lender of any notice given or purported to be given pursuant to any Stop Notice Law (as defined in the Loan Agreement), and the continued maintenance of such claim or lien or notice for a period of 15 calendar days without discharge thereof or other provision therefor made by Borrower in a manner satisfactory to Lender or otherwise permitted by the Loan Agreement;

(p) Failure of Borrower to make any payment into any of the Accounts (as defined in the Loan Agreement), within 15 calendar days of the required under the Loan Agreement; or

(q) There shall occur any default under the Indemnity Agreement; or

(r) The occurrence of any default or event of default under the Ground Lease or any other document or agreement related thereto or any termination of the Ground Lease.

5.2 **Lender's and Trustee's Right to Perform**. After the occurrence and during the continuance of any Event of Default, Lender or Trustee, but without the obligation so to do and without notice to or demand upon Borrower and without releasing Borrower from any obligations hereunder, may: make any payments or do any acts required of Borrower hereunder in such manner and to such extent as either may deem necessary to protect the security hereof, Lender or Trustee being authorized to enter upon the Property for such purposes; commence, appear in and defend any action or proceeding purporting to affect the security hereof or the rights or powers of Lender or Trustee; pay, purchase, contest or compromise any encumbrance, charge or lien in accordance with the following paragraph; and in exercising any such powers, pay necessary expenses, employ counsel and pay a reasonable fee therefor. All sums so expended shall be payable on demand by Borrower, be secured hereby and bear interest at the Default Rate of interest specified in the Note from the date advanced or expended until repaid.

Lender or Trustee, in making any payment herein, is hereby authorized, in the place and stead of Borrower, in the case of a payment of taxes, assessments, water rates, sewer rentals and other governmental or municipal charges, fines, impositions or liens asserted against the Property, to make such payment in reliance on any bill, statement or estimate procured from the appropriate public office without inquiry into the accuracy of the bill, statement or estimate or into the validity of any tax, assessment, sale, forfeiture, tax lien or title or claim thereof; in the case of any apparent or threatened adverse claim of title, lien, statement of lien, encumbrance, deed of trust, mortgage, claim or charge Lender or Trustee, as the case may be, shall be the sole judge of the legality or validity of same; and in the case of a payment for any other purpose herein and hereby authorized, but not enumerated in this paragraph, such payment may be made whenever, in the sole judgment and discretion of Trustee or Lender, as the case may be, such advance or advances shall seem necessary or desirable to protect the full security intended to be



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created by this Security Instrument, provided further, that in connection with any such advance, Lender at its option may and is hereby authorized to obtain a continuation report of title prepared by a title insurance company, the cost and expenses of which shall be repayable by Borrower without demand and shall be secured hereby.

5.3 **Remedies on Default.** Upon the occurrence of any Event of Default all the Secured Obligations shall become immediately due and payable, without notice or demand, at the option of Lender and Lender may:

(a) Have a receiver appointed as a matter of right on an *ex parte* basis without notice to Borrower and without regard to the sufficiency of the Property or any other security for the Secured Obligations and without the necessity of posting any bond or other security. Such receiver shall take possession and control of the Property and shall collect and receive the Rents. If Lender elects to seek the appointment of a receiver for the Property, Borrower, by its execution of this Security Instrument, expressly consents to the appointment of such receiver, including the appointment of a receiver *ex parte* if permitted by applicable law. The receiver shall be entitled to receive a reasonable fee for managing the Property, which fee may be deducted from the Rents or may be paid by Lender and added to the Secured Obligations. Immediately upon appointment of a receiver, Borrower shall surrender possession of the Property to the receiver and shall deliver to the receiver all documents, records (including records on electronic or magnetic media), accounts, surveys, plans, and specifications relating to the Property and all security deposits. If the Rents are not sufficient to pay the costs of taking control of and managing the Property and collecting the Rents, any funds expended by Lender, or advanced by Lender to the receiver, for such purposes shall become an additional part of the Secured Obligations. The receiver may exclude Borrower and its representatives from the Property. Borrower acknowledges and agrees that the exercise by Lender of any of the rights conferred under this Section 5.3 shall not be construed to make Lender a mortgagee-in-possession of the Property.

(b) Foreclose this Security Instrument as a mortgage or otherwise realize upon the Property.

(c) Cause Trustee to exercise its power of sale.

(d) Sue on the Note as permitted under applicable law.

(e) To the extent permitted by law, including, without limitation, RCW 61.24.100, seek and obtain a deficiency judgment following the completion of a judicial foreclosure or a trustee's sale of all or a portion of the security for the Secured Obligations.

(f) Avail itself of any other right or remedy available to it under the terms of this Security Instrument, the other Loan Documents or applicable law.



5.4 **No Waiver.** By accepting payment of any sum secured hereby after its due date, Lender does not waive its right either to require prompt payment when due of all other sums so secured or to declare an Event of Default for failure to do so. Lender may from time to time accept and apply any one or more payments of less than the full amount then due and payable on the Secured Obligations without waiving any Default, Event of Default, acceleration or other right or remedy of any nature whatsoever.

5.5 **Waiver of Marshaling, Etc.** In connection with any trustee's sale or other foreclosure sale under this Security Instrument, Borrower hereby waives, for itself and all others claiming by, through or under Borrower, any right Borrower or such others would otherwise have to require marshaling or to require that the Property be sold in parcels or in any particular order.

5.6 **Remedies Cumulative; Subrogation.** The rights and remedies accorded by this Security Instrument shall be in addition to, and not in substitution of, any rights or remedies available under now existing or hereafter arising applicable law. All rights and remedies provided for in this Security Instrument or afforded by law or equity are distinct and cumulative and may be exercised concurrently, independently or successively. The failure on the part of Lender to promptly enforce any right hereunder shall not operate as a waiver of such right and the waiver of any Default or Event of Default shall not constitute a waiver of any subsequent or other Default or Event of Default. Lender shall be subrogated to the claims and liens of those whose claims or liens are discharged or paid with the proceeds of the Loan.

6. **CONDEMNATION, ETC.** Any and all awards of damages, whether paid as a result of judgment or prior settlement, in connection with any condemnation or other taking of any portion of the Property for public or private use, or for injury to any portion of the Property ("Awards"), are hereby assigned and shall be paid to Lender, which may apply or disburse such Awards in the same manner, on the same terms, subject to the same conditions, to the same extent, and with the same effect as provided in Section 4.4.6 above for disposition of Insurance Proceeds. Without limiting the generality of the foregoing, if the taking results in a loss of the Property to an extent that, in the reasonable opinion of Lender, renders or is likely to render the Property not economically viable or if, in Lender's reasonable judgment, Lender's security is otherwise impaired, Lender may apply the Awards to reduce the unpaid Secured Obligations in such order as Lender may determine, and without any adjustment in the amount or due dates of installments due under the Note. If so applied, any Awards in excess of the unpaid balance of the Note and other sums due to Lender shall be paid to Borrower or Borrower's assignee. Lender shall in no case be obligated to see to the proper application of any amount paid over to Borrower. Such application or release shall not cure or waive any Default or notice of default hereunder or invalidate any act done pursuant to such notice. Should the Property or any part or appurtenance thereof or right or interest therein be taken or threatened to be taken by reason of any public or private improvement,



condemnation proceeding (including change of grade), or in any other manner, Lender may, at its option, commence, appear in and prosecute, in its own name, any action or proceeding, or make any reasonable compromise or settlement in connection with such taking or damage, and obtain all Awards or other relief therefor, and Borrower agrees to pay Lender's costs and reasonable attorneys' fees incurred in connection therewith. Lender shall have no obligation to take any action in connection with any actual or threatened condemnation or other proceeding.

7. **TRUSTEE.**

7.1 **General Powers and Duties of Trustee.** At any time or from time to time, without liability therefor, without notice and without affecting the liability of any person for the payment of the Secured Obligations, upon written request of Lender, payment of its own fees and presentation of this Security Instrument and the Note for endorsement (in case of full reconveyance, for cancellation or retention), Trustee may: (a) consent to the making of any map or plat of the Property; (b) join in granting any easement or creating any restriction thereon; (c) join in any subordination or other agreement affecting this Security Instrument or the lien or charge thereof; or (d) reconvey, without warranty, all or any part of the Property.

7.2 **Reconveyance.** Upon written request of Lender stating that all the Secured Obligations have been paid, and upon surrender of this Security Instrument and the Note to Trustee for cancellation and retention and upon payment of its fees, Trustee shall reconvey, without warranty, the Property then held hereunder. The recitals in any reconveyance executed under this Security Instrument of any matters of fact shall be conclusive proof of the truthfulness thereof. The grantee in such reconveyance may be described as "the person or persons legally entitled thereto."

7.3 **Powers and Duties on Default.** Upon written request therefor by Lender specifying the nature of the Event of Default, or the nature of the several Events of Default, and the amount or amounts due and owing, Trustee shall execute a written notice of default and of its election to cause the Property to be sold to satisfy the Secured Obligations, and shall cause such notice to be recorded and otherwise given according to law. Thereafter, Trustee shall execute a written notice of sale, and shall cause such notice to be recorded and otherwise given as required by law. Notice of sale having been given as then required by law and not less than the time then required by law having elapsed after recordation of such notice of breach, Trustee, without demand on Borrower, shall sell the Property at the time and place of sale specified in the notice, as provided by statute, either as a whole or in separate parcels and in such order as it may determine, at public auction to the highest and best bidder for cash in lawful money of the United States, payable at time of sale. Borrower agrees that such a sale (or a sheriff's sale pursuant to judicial foreclosure) of all the Property as real estate constitutes a commercially reasonable disposition thereof, but that with respect to all or any part of the Property which may be personal property Trustee shall have and exercise, at Lender's sole election, all the rights and remedies of a secured party under the UCC. Whenever notice of such



a sale is permitted or required hereunder or under the UCC, ten days shall be deemed reasonable. Trustee may postpone sale of all or any portion of the Property, and from time to time thereafter may postpone such sale, as provided by statute. Trustee shall deliver to the purchaser its deed conveying the Property so sold, but without any covenant or warranty, express or implied. The recital in such deed of any matters or facts shall be conclusive proof of the truthfulness thereof. Any person other than Trustee, including Borrower or Lender, may purchase at such sale. After deducting all costs, fees and expenses of Trustee and of this trust, including the cost of evidence of title search and title insurance and reasonable counsel fees in connection with sale, Trustee shall apply the proceeds of sale to the Secured Obligations in such order as Lender may determine and the remainder, if any, to the clerk of the superior court of the county in which the sale took place, as provided in RCW 61.24.080 or shall otherwise pay or apply such remainder as permitted by applicable law.

7.4 **Reassignment of Security Interest.** At the request of Lender, Trustee shall reassign to Lender the security interest created hereby and after such reassignment Lender shall have the right, upon the occurrence or continuance of any Event of Default, to realize upon the personal property subject to this Security Instrument, independent of any action of Trustee, pursuant to the UCC.

7.5 **Acceptance of Trust.** Trustee accepts this trust when this Security Instrument, duly executed and acknowledged, is made a public record as provided by law. Trustee is not obligated to notify any party hereto except Lender of pending sale under any other deed of trust or of any action or proceeding in which Borrower, Lender or Trustee shall be a party unless brought by Trustee.

7.6 **Reliance.** Trustee, upon presentation to Trustee by Lender of a written statement setting forth facts showing an Event of Default, is authorized to accept as true and conclusive all facts and statements therein, and to act thereon hereunder.

7.7 **Replacement of Trustee.** Lender may, from time to time, as provided by statute, appoint another trustee in place and stead of Trustee herein named, and thereupon Trustee herein named shall be discharged and the trustee so appointed shall be substituted as Trustee hereunder, with the same effect as if originally named Trustee herein.

8. NOTICES.

8.1 **Trustee.** Any notice or demand upon Trustee may be given or made at the address set forth above for Trustee.

8.2 **Borrower and Lender.** Any notice to or demand upon Borrower (including any notice of default or notice of sale) or notice to or demand upon Lender shall be deemed to have been sufficiently made for all purposes when deposited in the United States mails, postage prepaid, registered or certified, return receipt requested, addressed to Borrower



and Lender at their addresses as set forth in the first paragraph of this Security Instrument or to such other address as the recipient may have directed by notice in accordance herewith.

8.3 **Ground Lessor.** Ground Lessor has a right to certain notices under the terms of the Ground Lessor's Estoppel Certificate, Consent and Agreement entered into among Borrower, Lender and Ground Lessor contemporaneously with the execution of this Security Instrument. Lender will not have any obligations or liabilities to Borrower with respect to such notices to Ground Lessor or with respect to any failure of Lender to give such notices.

8.4 **Waiver of Notice.** The giving of notice may be waived in writing by the person or persons entitled to receive such notice, either before or after the time established for the giving of such notice.

9. **MODIFICATIONS, ETC.** Each person or entity now or hereafter owning or holding any interest in the Property agrees, by executing this Security Instrument or taking the Property subject to it, that Lender may in its sole discretion and without notice to or consent of any such person or entity: (a) extend the time for payment of the Secured Obligations; (b) discharge or release any one or more parties from their liability for such obligations in whole or in part; (c) delay any action to collect on such obligations or to realize on any collateral therefor; (d) release or fail to perfect any security for such obligations; (e) consent to one or more transfers of the Property, in whole or in part, on any terms; (f) waive or release any of holder's rights under any of the Loan Documents; (g) agree to an increase in the amount of the Secured Obligations or to any other modification of the Secured Obligations or of the Loan Documents; or (h) proceed against such person or entity before, at the same time as, or after it proceeds against any other person or entity liable for the Secured Obligations. None of the foregoing actions by Lender will result in any loss of priority in whole or in part, of the lien of this Security Instrument.

10. **SUCCESSORS AND ASSIGNS.** All provisions herein contained shall be binding upon and inure to the benefit of the respective successors and assigns of the parties. Lender may at any time sell, assign, participate or securitize all or any portion of Lender's rights and obligations under the Loan Documents.

11. **GOVERNING LAW; SEVERABILITY.** This Security Instrument shall be governed by the law of the state of Washington. In the event that any provision or clause of this Security Instrument, the Note or the other Loan Documents conflicts with applicable law, the conflict shall not affect other provisions of this Security Instrument, the Note or the other Loan Documents that can be given effect without the conflicting provision and to this end the provisions of this Security Instrument, the Note and the other Loan Documents are declared to be severable.



12. **BORROWER'S RIGHT TO POSSESSION.** Borrower may be and remain in possession of the Property for so long as no Event of Default exists and Borrower may, while it is entitled to possession of the Property, use the same.

13. **MAXIMUM INTEREST.** No provision of this Security Instrument, the Note or the other Loan Documents shall require the payment or permit the collection of interest in excess of the maximum permitted by law. If any excess of interest in such respect is herein or in the Note provided for, neither Borrower nor its successors or assigns shall be obligated to pay that portion of such interest that is in excess of the maximum permitted by law, and the right to demand the payment of any such excess shall be and is hereby waived and this Section 13 shall control any provision of this Security Instrument or the Note that is inconsistent herewith. If, notwithstanding the foregoing, Lender receives any payment that constitutes interest in an amount in excess of the maximum amount allowed by applicable law, the excess shall be applied to reduce the principal balance of the Secured Obligations without payment of a prepayment premium.

14. **ATTORNEYS' FEES AND LEGAL EXPENSES.** In the event of any Default under this Security Instrument, or in the event that any dispute arises relating to the interpretation, enforcement or performance of any Secured Obligation, Lender shall be entitled to collect from Borrower on demand all fees and expenses incurred in connection therewith, including but not limited to fees of attorneys, accountants, appraisers, environmental inspectors, consultants, expert witnesses, arbitrators, mediators and court reporters. Without limiting the generality of the foregoing, Borrower shall pay all such costs and expenses incurred in connection with: (a) arbitration or other alternative dispute resolution proceedings, trial court actions and appeals; (b) bankruptcy or other insolvency proceedings of Borrower, any guarantor or other party liable for any of the Secured Obligations or any party having any interest in any security for any of those obligations; (c) judicial or nonjudicial foreclosure on, or appointment of a receiver for, any of the Property; (d) post-judgment collection proceedings; (e) all claims, counterclaims, cross-claims and defenses asserted in any of the foregoing whether or not they arise out of or are related to this Security Instrument; (f) all preparation for any of the foregoing; and (g) all settlement negotiations with respect to any of the foregoing.

15. **PREPAYMENT PROVISIONS.** If at any time after an Event of Default and acceleration of the Secured Obligations there shall be a tender of payment of the amount necessary to satisfy such indebtedness by or on behalf of Borrower, its successors or assigns, the same shall be deemed to be a voluntary prepayment such that the sum required to satisfy such indebtedness in full shall include, to the extent permitted by law, the additional payment, if any, required under the prepayment provisions of the Loan Agreement or the Note.

16. **TIME IS OF THE ESSENCE.** Time is of the essence under this Security Instrument and in the performance of every term, covenant and obligation contained herein.



17. **FIXTURE FILING.** This Security Instrument constitutes a financing statement, filed as a fixture filing in the real estate records of the county of the state in which the real property described in Exhibit A is located, with respect to any and all fixtures included within the list of improvements and fixtures described in Section 1.2 of this Security Instrument and to any goods or other personal property that are now or hereafter will become a part of the Property as fixtures.

18. **MISCELLANEOUS.**

18.1 **Number and Gender.** Whenever the context so requires, as used in this Security Instrument, the singular number includes the plural, the impersonal includes the personal and pronouns of one gender include either or both other genders.

18.2 **Captions.** The headings to the various sections have been inserted for convenient reference only and shall not modify, define, limit or expand the express provisions of this Security Instrument.

18.3 **Entire Agreement; No Oral Agreements.** This Security Instrument, the Note and the other Loan Documents constitute the final expression of the entire agreement of the parties with respect to the transactions set forth therein. No party is relying upon any oral agreement or other understanding not expressly set forth in the Loan Documents. The Loan Documents may not be amended or modified except by means of a written document executed by the party sought to be charged with such amendment or modification.

18.4 **Release; No Partial Release.** Within a reasonable time after payment and performance of all of the Secured Obligations and termination of any further commitment by Lender to extend further credit secured by this Security Instrument, Lender shall release or obtain the release of the lien of this Security Instrument. Borrower shall prepay all costs and expenses incurred by Lender in connection with such release. Borrower will not be entitled to a partial release of any portion of the Property so long as any of the Secured Obligations remain outstanding.

18.5 **Incorporation of Terms of Note.** All terms and conditions of the Note are incorporated herein as if set forth in full in this Security Instrument.

19. **WAIVER OF JURY TRIAL. EACH OF BORROWER AND LENDER (FOR ITSELF AND ITS SUCCESSORS, ASSIGNS AND PARTICIPANTS) WAIVES ITS RIGHT TO A TRIAL BY JURY OF ANY CLAIM OR CAUSE OF ACTION BASED UPON, ARISING OUT OF OR RELATED TO THIS SECURITY INSTRUMENT, THE OTHER LOAN DOCUMENTS OR THE TRANSACTIONS PROVIDED FOR HEREIN OR THEREIN, IN ANY LEGAL ACTION OR PROCEEDING OF ANY TYPE BROUGHT BY ANY PARTY TO ANY OF THE FOREGOING AGAINST ANY OTHER SUCH PARTY, WHETHER SOUNDING IN**



CONTRACT, TORT OR OTHERWISE. ANY SUCH CLAIM OR CAUSE OF ACTION SHALL BE TRIED BY A COURT SITTING WITHOUT A JURY.

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Skagit County Auditor

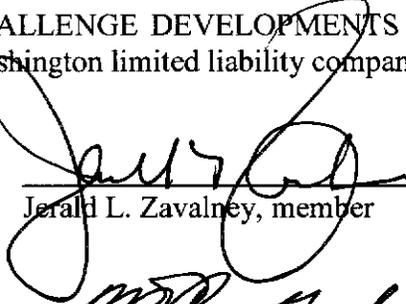
DATED as of the day and year first above written.

ORAL AGREEMENTS OR ORAL COMMITMENTS TO LOAN MONEY, EXTEND CREDIT, OR TO FORBEAR FROM ENFORCING REPAYMENT OF A DEBT ARE NOT ENFORCEABLE UNDER WASHINGTON LAW.

BORROWER:

CHALLENGE DEVELOPMENTS II, L.L.C., a
Washington limited liability company

By


Jerald L. Zavalney, member

By


Michael E. Ruthford, member



STATE OF WASHINGTON

SS.

COUNTY OF SKAGIT

I certify that I know or have satisfactory evidence that JERALD L. ZAVALNEY is the person who appeared before me, and said person acknowledged that said person signed this instrument, on oath stated that said person was authorized to execute the instrument and acknowledged it as a member of CHALLENGE DEVELOPMENTS II, L.L.C., a limited liability company, to be the free and voluntary act of such limited liability company for the uses and purposes mentioned in the instrument.

Dated this 13th day of March, 2006.



Rhonda McNett

(Signature of Notary)

Rhonda McNett

(Legibly Print or Stamp Name of Notary)

Notary public in and for the state of Washington,
residing at Anacortes, WA

My appointment expires 11/29/09



STATE OF WASHINGTON

SS.

COUNTY OF SKAGIT

I certify that I know or have satisfactory evidence that MICHAEL E. RUTHFORD is the person who appeared before me, and said person acknowledged that said person signed this instrument, on oath stated that said person was authorized to execute the instrument and acknowledged it as a member of CHALLENGE DEVELOPMENTS II, L.L.C., a limited liability company, to be the free and voluntary act of such limited liability company for the uses and purposes mentioned in the instrument.

Dated this 13th day of March, 2006.

Rhonda McNett
(Signature of Notary)



Rhonda McNett

(Legibly Print or Stamp Name of Notary)

Notary public in and for the state of Washington,
residing at Anacortes, WA

My appointment expires 11/29/09



EXHIBIT A

LEGAL DESCRIPTION

PARCEL 1 (GROUND LEASE PARCEL)

That portion of the Southeast Quarter of Section 24, Township 35 North, Range 1 East of the Willamette Meridian, described as follows:

Commencing at the East Quarter corner of said Section 24;
thence South 0°59'30" East, along the East line of said Section 24, 1,223.17 feet to an intersection with the South line of 24th Street;
thence South 89°58'48" West, along the South line of 24th Street, 396.27 feet to the true point of beginning;
thence South 0°01'35" East, 264.46 feet;
thence South 89°58'25" West, 358.50 feet to the East line of "M" Avenue;
thence North 0°01'35" West, along the East line of "M" Avenue, 264.50 feet to the South line of 24th Street;
thence North 89°58'48" East along the South line of 24th Street, 358.50 feet to the true point of beginning;

Situate in Skagit County, Washington.

PARCEL 2 (CONDOMINIUM UNITS)

Unit 101 and Unit 102, Island Medical Center, a condominium, according to the Declaration Establishing the Island Medical Center Condominium recorded under recording no. 200603140(3), in Volume of Condominiums, pages through , inclusive, in Skagit County, Washington.

PARCEL 3 (RECIPROCAL EASEMENT PARCEL)

That portion of the East Half of the Southeast Quarter of Section 24, Township 35 North, Range 1 East of the Willamette Meridian, described as follows:

Commencing at the East Quarter corner of said Section 24, Township 35 North, Range 1 East of the Willamette Meridian;
thence South 0°59'30" East along the East line of said Section, 1183.99 feet to an intersection with the center line of 24th Street produced West to the true point-of-beginning;
thence continue South 0°59'30" East along the East line of said section 592.21 feet to an intersection with the centerline of 26th Street produced West;



thence West along the center line of 26th Street produced 764.27 feet to the East line of M Avenue as conveyed to the City of Anacortes for street purposes by deed recorded May 9, 1960, under Auditor's File No. 591164;

thence North 0°01' West along the East line of M Avenue 632.12 feet to the North line of 24th Street produced West;

(said point being the Southwest corner of that certain tract conveyed to the City of Anacortes by deed dated April 28, 1960, and recorded September 12, 1960, under Auditor's File No. 598656);

thence East along the North line of 24th Street and the South line of said City of Anacortes tract produced, 519.84 feet to the East line of that certain tract acquired by the United States of America under that certain Declaration of Taking filed September 8, 1944, in the District Court of the United States for the Western District of Washington, Northern Division. Cause No. 687 (said point also being on the West line of a tract of land owned by Gunnar V. Jelmsberg and Minnie Jelmsberg, his wife),

thence South 0°01'00" East along the West line of said Jelmsberg tract to the center line of 24th Street produced West;

thence East along the center line of 24th Street produced, 226.14 feet, more or less, to the point-of-beginning;

EXCEPT the East 330 feet of the South 40 feet as conveyed to the City of Anacortes by deed recorded under Auditor's File No. 715573, records of Skagit County, Washington;

ALSO EXCEPT all that portion contained in Ground Lease recorded under Auditor's File 798039, records of Skagit County, Washington; described as follows:

That portion of the Southeast Quarter of Section 24, Township 35 North, Range 1 East of the Willamette Meridian, described as follows:

Beginning at the East Quarter corner of said Section 24;

thence South 0°59'30" East, along the East line of said Section 24, 1223.17 feet to an intersection with the South line of 24th Street;

thence South 89°58'48" West along the South line of 24th Street, 396.27 feet to the true point of beginning;

thence South 0°01'35" East 264.46 feet;

thence South 89°58'25" West 358.50 feet to the East line of "M" Avenue;

thence North 0°01'35" West along the East line of "M" Avenue 264.50 feet to the South line of 24th Street;

thence North 89°58'48" East along the South line of 24th Street 358.50 feet to the true point of beginning.

Situated in Skagit County, Washington.

EXHIBIT A – Page 2 of 2



200603140135
Skagit County Auditor

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EXHIBIT B

DESCRIPTION OF GROUND LEASE

The leasehold estate created by that certain Amended and Restated Ground Lease (the "Original Ground Lease") executed by and between the lessor and lessee named below and otherwise described as follows:

DATED: As of March 13, 2006

LESSOR: Skagit County Public Hospital District No. 2., a Washington state public hospital district, d/b/a Island Hospital

LESSEE: Challenge Developments II, L.L.C., a Washington limited liability company

RECORDED: MARCH 14, 2006

IN SKAGIT COUNTY, WASHINGTON

RECORDING NO.: 200603140129

which leasehold estate covers, without limitation, the real property described in Exhibit A attached hereto. The Original Ground Lease, together with all amendments, modifications, extensions and assignments previously, currently or hereafter entered into are referred to collectively as the "Ground Lease."

EXHIBIT B



200603140135
Skagit County Auditor

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