NEW ISSUE
Book-Entry Only

RATINGS:+
Moody's: Baa1
S&P: BBB

In the opinion of Bond Counsel, under existing law and assuming continuing compliance with certain covenants and the accuracy of certain representations, (i) interest on the Series 2011B Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations; however, such interest will be taken into account in determining adjusted current earnings for purposes of computing the alternative minimum tax imposed on certain corporations; (ii) interest on the Series 2011C Bonds is excluded from gross income for federal income tax purposes except interest on a Series 2011C (AMT) Bond for any period during which that Series 2011C Bond is held by a "substantial user" of the facilities refinanced by such Series 2011C Bond or by a "related person" within the meaning of Section 147(a) of the U.S. Internal Revenue Code of 1986, as amended; however, such interest is a specific preference item for purposes of the federal individual and corporate alternative minimum taxes; and (iii) interest on the Series 2011A Bonds is not excluded from gross income for federal income tax purposes. Bond Counsel is further of the opinion that the Bonds and interest thereon are exempt from state, Commonwealth of Puerto Rico, and local income taxation. For a more complete discussion of the tax aspects, including the tax aspects of the Series 2011A Bonds as they relate to holders of the Bonds that are Puerto Rico individuals and/or Puerto Rico corporations, see "Tax Matters," herein.

$669,215,000
PUERTO RICO INFRASTRUCTURE FINANCING AUTHORITY
Revenue Bonds (Ports Authority Project), Series 2011
consisting of

$340,000,000 Series 2011A (Federally Taxable) **$192,830,000 Series 2011B (Non-AMT)** **$136,385,000 Series 2011C (AMT)**

Dated: Date of Delivery **Due: As shown on the inside cover**

The Series 2011 Bonds (the "Bonds") are limited obligations of the Puerto Rico Infrastructure Financing Authority (the "Financing Authority") and are being issued pursuant to a certain Loan and Trust Agreement, dated December 1, 2011 (the "Loan and Trust Agreement"), by and among the Financing Authority, the Puerto Rico Ports Authority (the "Ports Authority"), and The Bank of New York Mellon, as trustee thereunder (the "Trustee"). The proceeds of the Bonds will be loaned to the Ports Authority, to finance and refinance certain indebtedness of the Ports Authority; a swap termination fee; certain operational and capital costs; and the costs of issuance of the Bonds. See "PLAN OF FINANCING." The Bonds are payable solely from and secured by revenues received by the Financing Authority under the Loan and Trust Agreement. The obligations of the Ports Authority under the Loan and Trust Agreement constitute a general, unsecured obligation of the Ports Authority, which ranks on parity with all other general, unsecured, and unsubordinated obligations thereof.

The Series 2011A Bonds and the Series 2011B Bonds will be issued as fixed rate bonds. The Series 2011C Bonds initially will bear interest at the Term Rate, which will be a fixed rate established separately for each Term Rate Period by Wells Fargo Securities, LLC, acting as initial Remarketing Agent. The initial Term Rate for the Series 2011C Bonds shall be in effect from the date of issuance of the Series 2011C Bonds to the end of the initial Term Rate Periods as described on the inside cover hereof (the "Initial Term Rate Periods"). The interest rates on the Series 2011C Bonds for the Initial Term Rate Periods are as set forth on the inside cover hereof.

The Bonds also are secured by two irrevocable, transferable direct pay letters of credit (collectively, the "GDB Letter of Credit") issued by

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO

a public corporation and governmental instrumentality of the Commonwealth of Puerto Rico ("Government Development Bank"). The letter of credit securing the Series 2011A Bonds and the Series 2011B Bonds will expire on the earlier of December 15, 2026 or the date when the Series 2011A Bonds and the Series 2011B Bonds are no longer outstanding under the Loan and Trust Agreement. The letter of credit securing the Series 2011C Bonds will expire on the earlier of December 16, 2013 or the date when the Series 2011C Bonds are no longer outstanding under the Loan and Trust Agreement. The GDB Letter of Credit is not subject to early termination upon a default by the Ports Authority under the Letter of Credit Disbursement and Reimbursement Agreement (the "Reimbursement Agreement") between the Ports Authority and Government Development Bank.

Interest on the Bonds will be payable on June 15 and December 15, commencing June 15, 2012. Interest on the Bonds will be calculated on the basis of a 360-day year consisting of twelve 30-day months. The Bonds are issuable as fully registered bonds and when issued, will be registered in the name of Cede & Co., as registered owner and nominee of The Depository Trust Company ("DTC"), New York, New York. Individual purchases and sales of the Bonds may be made in book-entry form only, in denominations of $5,000 and integral multiples thereof. Purchasers will not receive certificates from the Financing Authority or the Trustee representing their interest in the Bonds purchased. So long as the Bonds are held by DTC, the principal of and interest on the Bonds will be payable by wire transfer to DTC, which in turn is required to remit such principal and interest to the DTC Participants for subsequent disbursement to the Beneficial Owners of the Bonds, as more fully described herein.

The Bonds are subject to extraordinary optional redemption prior to maturity, the Series 2011B Bonds are subject to optional redemption prior to maturity, and the Series 2011C Bonds are subject to mandatory sinking fund redemption and mandatory tender for purchase, all as more fully described herein.

THE BONDS ARE BEING OFFERED SOLELY ON THE BASIS OF THE FINANCIAL STRENGTH OF GOVERNMENT DEVELOPMENT BANK AND NOT ON THE FINANCIAL STRENGTH OF THE PORTS AUTHORITY OR OTHER SECURITY. THE BONDS ARE NOT DIRECTLY SECURED BY ANY COLLATERAL OTHER THAN THE GDB LETTER OF CREDIT. See "Risk Factors."

The Bonds are not (i) a general obligation of the Financing Authority, (ii) a pledge of the faith and credit of the Financing Authority, or (iii) a debt or pledge of the good faith and credit of the Commonwealth of Puerto Rico. The obligations of the Ports Authority under the Loan and Trust Agreement constitute a general, unsecured obligation of the Ports Authority. The GDB Letter of Credit is a general, unsecured obligation of Government Development Bank. The principal of and interest on the Bonds are payable solely from, and secured by, an assignment and pledge of the Revenues to be received under the Loan and Trust Agreement, including funds payable under the GDB Letter of Credit. The Bonds are not secured by a legal or equitable pledge of, or charge, lien or encumbrance upon, any of the property or any of the income or receipts of the Financing Authority, the Ports Authority or Government Development Bank. None of the Financing Authority, the Ports Authority or Government Development Bank has any taxing power.

The Bonds are offered when, as and if issued by the Financing Authority and received by the Underwriters, subject to the approval of legality by Greenberg Traurig, LLP, Boston, Massachusetts, Bond Counsel. Certain legal matters will be passed upon on behalf of the Financing Authority, the Ports Authority, and Government Development Bank by Greenberg Traurig, LLP, Boston, Massachusetts, Special Counsel, and for Government Development Bank by its General Counsel. Certain legal matters will be passed upon for the Underwriters by their counsel, Ferraiuoli LLC. It is expected that the Bonds will be available for delivery through the facilities of DTC on or about December 28, 2011.

Wells Fargo Securities

Ramirez& Co., Inc. **RBC Capital Markets**

Barclays Capital BMO Capital Markets BofA Merrill Lynch
Citigroup Goldman, Sachs & Co. Jefferies
J.P. Morgan Morgan Stanley Raymond James UBS FS Puerto Rico

BBVAPR MSD FirstBank Puerto Rico Securities Oriental Financial Services Popular Securities Santander Securities Scotia MSD VAB FINANCIAL

December 16, 2011

$669,215,000
Revenue Bonds (Ports Authority Project) Series 2011

$340,000,000 Series 2011A (Federally Taxable)

Maturity June 15	Amount	Interest Rate	Price	CUSIP‡
2013	$340,000,000	2.990%	100%	74528UAA9

$192,830,000 Series 2011B (Non-AMT)

Maturity December 15	Amount	Interest Rate	Yield	CUSIP‡
2014	$550,000	4.000%	2.380%	74528UAB7
2015	1,650,000	5.000%	2.760%	74528UAC5
2016	2,055,000	3.000%	2.950%	74528UAD3
2017	1,125,000	5.000%	3.170%	74528UAE1
2018	1,100,000	4.000%	3.440%	74528UAF8
2021	4,290,000	4.000%	4.060%	74528UAG6
2022	640,000	4.250%	4.330%	74528UAH4
2022	25,000,000	5.000%	4.330%*	74528UAN1
2023	690,000	4.500%	4.490%*	74528UAJ0
2024	6,100,000	4.625%	4.700%	74528UAK7
2025	3,175,000	5.000%	4.860%*	74528UAL5
2026	86,455,000	5.250%	4.980%*	74528UAM3
2026	60,000,000	6.000%	4.770%*	74528UAP6

$136,385,000 Series 2011C (AMT)

Maturity December 15	Amount	Initial Term Rate	Price	End of Initial Term Rate Period	CUSIP‡
2026	$96,785,000	2.750%	100%	June 14, 2013	74528UAQ4
2026	39,600,000	3.000%	100%	December 14, 2013	74528UAR2

‡ Copyright, American Bankers Association. CUSIP data herein is provided by Standard and Poor's, CUSIP Service Bureau, a division of the McGraw-Hill Companies, Inc. This data is not intended to create a database and does nor serve in any way as a substitute of the CUSIP Services. CUSIP numbers are provided for convenience of reference only. None of the Financing Authority, the Ports Authority, Government Development Bank or the Underwriters take any responsibility for the accuracy of such numbers.

* Priced at the stated yield to the December 15, 2021 optional redemption date at a redemption price of 100%. See "Redemption" under DESCRIPTION OF THE BONDS herein.

No Offering May Be Made Except by this Official Statement. No dealer, broker, salesperson or other person has been authorized by the Financing Authority, the Ports Authority, or Government Development Bank to give any information or to make any representations other than as contained in this Official Statement, and, if given or made, such other information or representation must not be relied upon as having been given or authorized by the Financing Authority, the Ports Authority, Government Development Bank or the Underwriters.

Use of this Official Statement. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy nor shall there be any sale of the Bonds by a person in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale. This Official Statement does not constitute a contract between any Bondowner and the Financing Authority, the Ports Authority, Government Development Bank or the Underwriters.

Preparation of this Official Statement. The information contained in this Official Statement (which shall include the Appendices hereto as well as all documents incorporated herein by reference) has been obtained from the Financing Authority, the Ports Authority, Government Development Bank, and other sources deemed reliable. The information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the Financing Authority, the Ports Authority, or Government Development Bank since the date hereof. This Official Statement is submitted in connection with the sale of the Bonds referred to herein and may not be reproduced or used, in whole or in part, for any other purpose.

The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with, and as a part of, their respective responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

Estimates and Forecasts. Certain statements contained in this Official Statement do not reflect historical facts but are forecasts and "forward-looking statements." No assurance can be given that the future results discussed herein will be achieved, and actual results may differ materially from the forecasts described herein. In this respect, the words "estimate," "forecast," "project," "anticipate," "expect," "intend," "plan," "believe" and similar expressions are intended to identify forward-looking statements. All projections, forecasts, assumptions and other forward-looking statements are expressly qualified in their entirety by the cautionary statements set forth in this Official Statement. See also "GOVERNMENT DEVELOPMENT BANK – General GDB Financial Information."

The projections set forth in this Official Statement were not prepared with a view toward complying with the guidelines established by the American Institute of Certified Public Accountants with respect to prospective financial information, but in the view of management of Government Development Bank and the Commonwealth of Puerto Rico, were prepared on a reasonable basis, reflect the best currently available estimates and judgments, and present, to the best of management's knowledge and belief, the expected course of action and the expected future financial performance of Government Development Bank and the Commonwealth of Puerto Rico. However, this information is not fact and should not be relied upon as being necessarily indicative of future results, and readers of this Official Statement are cautioned not to place undue reliance on the prospective financial information. Neither Government Development Bank's nor the Commonwealth's independent auditors nor any other independent auditors have compiled, examined, or performed any procedures with respect to the prospective financial information contained herein, nor have they expressed any opinion or any other form of assurance on such information or its achievability and disclaim any association with, the prospective financial information. Neither Government Development Bank's nor the Commonwealth's independent auditors nor any other independent auditors have been consulted in connection with the preparation of the prospective financial information set forth in this Official Statement, which is solely the product of Government Development Bank and the Commonwealth of Puerto Rico, and the independent auditors assume no responsibility for its content.

Document Summaries. All summaries of documents contained in this Official Statement are made subject to the provisions of such documents and do not purport to be complete statements of any or all such provisions. Each reference in this Official Statement to a document is qualified in its entirety by reference to such document, which is on file with the Trustee. Copies of documents referred to herein are available from the Trustee at 101 Barclay Street – 7W, New York, New York, 10286.

No Registration or Qualification. The issuance and sale of the Bonds have not been registered under the U.S. Securities Act of 1933 or the U.S. Securities Exchange Act of 1934, both as amended, and the Loan and Trust Agreement has not been qualified under the U.S. Trust Indenture Act of 1939, as amended, in reliance upon exemptions provided thereunder.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICES OF THE BONDS OFFERED HEREBY AT LEVELS ABOVE THOSE WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

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INTRODUCTORY STATEMENT

This Official Statement of the Puerto Rico Infrastructure Financing Authority (the "Financing Authority"), which includes the cover page, the inside cover page, the appendices, and the information incorporated by reference as set forth below, sets forth certain information with respect to the offering and sale by the Financing Authority of its Revenue Bonds (Ports Authority Project), Series 2011 (the "Bonds"), consisting of $340,000,000 Series 2011A (Federally Taxable), $192,830,000 Series 2011B (Non-AMT), and $136,385,000 Series 2011C (AMT) (hereinafter, the "Series 2011A Bonds," the "Series 2011B Bonds," and the "Series 2011C Bonds," respectively). The Bonds are being issued pursuant to a certain Loan and Trust Agreement, dated December 1, 2011 (the "Loan and Trust Agreement"), by and among the Financing Authority, the Puerto Rico Ports Authority (the "Ports Authority"), and The Bank of New York Mellon, as trustee thereunder (the "Trustee"). The proceeds from the Bonds will be loaned to the Ports Authority, in order to (i) refinance certain obligations the proceeds of which were used by the Ports Authority to (a) finance or refinance the acquisition of land, site development, construction, renovation, or installation of airport or seaport facilities, related infrastructure or buildings, or acquisition or installation of furnishings, equipment, vehicles, or any combination of the foregoing, and (b) provide working capital to the Ports Authority, (ii) finance certain operating and capital costs, and (iii) finance the costs of issuance of the Bonds. See "PLAN OF FINANCING."

The Bonds are limited obligations of the Financing Authority payable solely from and secured by the Revenues received under the Loan and Trust Agreement. Under the Loan and Trust Agreement, the Ports Authority will agree to make loan payments sufficient to pay the principal of, premium, if any, and interest on the Bonds when due. As further security for the payment of the principal of, premium, if any, and interest on the Bonds, the Financing Authority will assign to the Trustee, for the benefit of the holders of the Bonds, certain of the Financing Authority's rights under the Loan and Trust Agreement (except for certain rights of the Financing Authority to indemnification, exemption from liabilities, notices, and payment of costs and expenses), including the right to receive the loan payments from the Ports Authority pursuant to the Loan and Trust Agreement and the Financing Authority's rights in the funds and accounts established under the Loan and Trust Agreement.

As further security for the Bonds, and pursuant to the Letter of Credit Disbursement and Reimbursement Agreement, between the Ports Authority and Government Development Bank for Puerto Rico ("Government Development Bank"), dated as of December 1, 2011 (the "Reimbursement Agreement"), Government Development Bank will issue two irrevocable, transferable direct-pay letters of credit (collectively, the "GDB Letter of Credit"), in favor of the Trustee and for the benefit of the holders of the Bonds. See APPENDIX C – "Forms of the GDB Letter of Credit." The letter of credit securing the Series 2011A Bonds and the 2011B Bonds (the "Series A/B Letter of Credit") will be in an amount sufficient to pay the aggregate principal amount of the Series 2011A Bonds and the Series 2011B Bonds, premium, if any, and up to 180 days' interest on the Series 2011A Bonds and the Series 2011B Bonds (computed based on the actual interest rates in effect on the Series 2011A Bonds and the Series 2011B Bonds in a 360-day year). The letter of credit securing the Series 2011C Bonds (the "Series C Letter of Credit") initially will be in an amount sufficient to pay the principal amount, or the portion of the Purchase Price representing principal, of the Series 2011C Bonds, premium, if any, and up to 180 days' interest, or the portion of the Purchase Price representing interest, on the Series 2011C Bonds at the actual Term Rates applicable to the Series 2011C Bonds (computed based on a 360-day year). The Series C Letter of Credit may be extended, modified or replaced by a similar letter of credit issued by Government Development Bank in connection with a change of Mode or following a mandatory tender for purchase. See "DESCRIPTION OF THE BONDS – Series 2011C Bonds – Failure to Satisfy Conditions Precedent to a Mode Change," and APPENDIX B - "Summary of Certain Provisions of the Loan and Trust Agreement" under the heading "Remarketing of the Bonds Tendered."

Government Development Bank's issuing of the GDB Letter of Credit for the account of the Ports Authority will have the effect of substituting the GDB Letter of Credit for certain outstanding obligations of Government Development Bank incurred on behalf of the Ports Authority. See "PLAN OF FINANCING."

Under the GDB Letter of Credit, Government Development Bank is obligated to pay to the Trustee, upon presentation of required documentation, the amount necessary to pay the principal of and interest on the Bonds then due and payable. The Series A/B Letter of Credit provides that it will expire on the earliest of (i) honoring of a final drawing by the Trustee under the Series A/B Letter of Credit, accompanied by the Series A/B Letter of Credit, (ii) the date on which Government Development Bank receives a certificate signed by the Trustee, accompanied by the Series A/B Letter of Credit, stating that the Series 2011A Bonds and the Series 2011B Bonds are no longer outstanding under the Loan and Trust Agreement, and (iii) December 15, 2026. The Series C Letter of Credit provides that it will expire on the earlier of (i) honoring of a final drawing by the Trustee under the Series C Letter of Credit, accompanied by the Series C Letter of Credit, (ii) the date on which Government Development Bank receives a certificate signed by the Trustee, accompanied by the Series C Letter of Credit, stating that the Series 2011C Bonds are no longer outstanding under the Loan and Trust Agreement, and (iii) December 16, 2013. The Loan and Trust Agreement also provides that the Trustee will make timely drawings under the GDB Letter of Credit in accordance with the terms thereof to pay when due (whether by maturity, redemption or acceleration) the principal or Purchase Price of and interest on the Bonds.

PROSPECTIVE PURCHASERS OF THE BONDS SHOULD LOOK TO THE GDB LETTER OF CREDIT AS THE SOLE SOURCE OF PAYMENT FOR THE BONDS. NO INFORMATION WILL BE PROVIDED REGARDING THE ABILITY OF THE PORTS AUTHORITY TO PAY DEBT SERVICE ON THE BONDS SHOULD GOVERNMENT DEVELOPMENT BANK DEFAULT IN ITS PAYMENT OBLIGATIONS UNDER THE GDB LETTER OF CREDIT. See "THE PORTS AUTHORITY."

The purchase of the Bonds involves a degree of risk. Prospective purchasers should carefully consider the material under the caption "RISK FACTORS."

THE BONDS ARE NOT A GENERAL OBLIGATION OF THE FINANCING AUTHORITY OR A PLEDGE OF THE FAITH AND CREDIT OF THE FINANCING AUTHORITY OR A DEBT OR PLEDGE OF THE GOOD FAITH AND CREDIT OF THE COMMONWEALTH OF PUERTO RICO.

THE PORTS AUTHORITY'S OBLIGATION TO MAKE PAYMENTS UNDER THE LOAN AND TRUST AGREEMENT IS A GENERAL, UNSECURED OBLIGATION OF THE PORTS AUTHORITY, AND GOVERNMENT DEVELOPMENT BANK'S OBLIGATION UNDER THE GDB LETTER OF CREDIT IS A GENERAL, UNSECURED OBLIGATION OF GOVERNMENT DEVELOPMENT BANK. THE PRINCIPAL, PURCHASE PRICE AND REDEMPTION PRICE OF AND INTEREST ON THE BONDS ARE PAYABLE SOLELY FROM THE REVENUES AND FUNDS PLEDGED FOR THEIR PAYMENT UNDER THE LOAN AND TRUST AGREEMENT AND THE GDB LETTER OF CREDIT. NONE OF THE FINANCING AUTHORITY, THE PORTS AUTHORITY OR GOVERNMENT DEVELOPMENT BANK HAS ANY TAXING POWER.

The summaries contained herein are not comprehensive or definitive. All references to the Bonds, the GDB Letter of Credit, the Reimbursement Agreement and the Loan and Trust Agreement are qualified in their entirety by the definitive forms thereof. See APPENDIX A - "Definitions of Certain Terms," APPENDIX B - "Summary of Certain Provision of the Loan and Trust Agreement," APPENDIX C – "Forms of GDB Letter of Credit, " and APPENDIX D - "Summary of Certain Provisions of the Reimbursement Agreement." Copies of the documents in definitive form will be available for inspection at the Principal Office of the Trustee.

Unless otherwise defined herein, capitalized terms used in this Official Statement shall have the meanings specified in APPENDIX A - "Definitions of Certain Terms". Terms not otherwise defined in this Official Statement have the meanings provided in the specific documents.

The agreements of the Financing Authority with the Bondowners are fully set forth in the Loan and Trust Agreement and neither any advertisement of the Bonds nor this Official Statement is to be construed as constituting an agreement with the purchasers of the Bonds. So far as any statements are made in this Official

Statement involving matters of opinion, whether or not expressly so stated, they are intended as such and not as representations of fact.

Incorporation of Commonwealth of Puerto Rico's Financial Information

Because of the role played by Government Development Bank as a lender to the Commonwealth of Puerto Rico (the "Commonwealth" or "Puerto Rico") and its instrumentalities and the effect that the financial condition of the Commonwealth and its instrumentalities may have on the financial condition and results of operations of Government Development Bank, this Official Statement includes as APPENDIX I the Commonwealth of Puerto Rico's Financial Information and Operating Data Report, dated December 6, 2011 (the "Commonwealth Report"). Deloitte & Touche LLP, independent auditors for Government Development Bank and the Commonwealth, has not been engaged to perform and has not performed any procedures on the financial information addressed in the Commonwealth Report which is incorporated by reference in this Official Statement.

The Commonwealth Report includes important operating and financial information about the Commonwealth, including information about its economy, historical revenues and expenditures of its General Fund, the budget for fiscal years 2011 and 2012, and the debt of Puerto Rico's public sector. Purchasers of the Bonds should read the Commonwealth Report in its entirety. Any appendix of an Official Statement or other disclosure document of the Commonwealth or of any instrumentality of the Commonwealth containing any revision to the Commonwealth Report that is filed with the Municipal Securities Rulemaking Board ("MSRB")through the Electronic Municipal Market Access System ("EMMA") (http://emma.msrb.org), or any new or revised Commonwealth Report or other document containing information that modifies or supersedes the information contained in the Commonwealth Report that is filed with the MSRB through EMMA, in each case after the date hereof and prior to the termination of the offering of the Bonds shall be deemed to be incorporated by reference into this Official Statement and to be part of this Official Statement from the date of filing of such document. Any statement contained in the Commonwealth Report or elsewhere herein shall also be deemed to be modified or superseded to the extent that a statement contained in any such subsequently filed document modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Official Statement. Any filing with the MSRB through EMMA by Government Development Bank of a document generally containing the same information set forth in its continuing disclosure reports or financial statements, after the date hereof and prior to the termination of the offering of the Bonds, shall also be deemed to be incorporated by reference into this Official Statement and to be part of this Official Statement from the date of filing of such document. Government Development Bank will provide without charge to any person to whom this Official Statement is delivered, on the written or oral request of such person, a copy of the Commonwealth Report incorporated herein by reference. Requests should be directed to Government Development Bank for Puerto Rico, P.O. Box 42001, San Juan, Puerto Rico 00940, telephone number (787) 722-2525.

The following information supplements the information in the Commonwealth Report included as APPENDIX I, and should be read in conjunction therewith.

Preliminary General Fund Revenues for the First Four Months of Fiscal Year 2012. Preliminary General Fund revenues for the first four months of fiscal year 2012 (from July 1, 2011 to October 31, 2011) were $2.284 billion, an increase of $148.1 million, or 6.9%, from $2.136 billion of revenues for the same period in the prior fiscal year and a decrease of $32.8 million, or 1.4%, from the revised estimate of revenues of $2.317 billion. The increase in General Fund revenues for the first four months of fiscal year 2012, compared to the same period in the prior fiscal year, is mainly due to the collection of $650.2 million from the new temporary excise tax under Act No. 154, which was not in effect during the first four months of fiscal year 2011. This increase was partially offset by decreases in collections from the following: (i) income taxes from individuals of $208.3 million, (ii) corporate income taxes of $84.9 million, (iii) taxes withheld from non-residents of $81.9 million and (iv) property taxes of $108.3 million. The reduction in collections from property taxes is due to the phase out of the special property tax imposed on residential and commercial real estate in fiscal year 2009 as part of the temporary revenue raising measures included in the fiscal stabilization plan. The reduction in income taxes was expected and is largely due to the tax reform implemented in January 2011.

THE FINANCING AUTHORITY

The Financing Authority is a public corporation and instrumentality established under Act No. 44 of June 21, 1988 (the "Enabling Act"). The Financing Authority has two principal functions: (i) providing financial, administrative and other types of assistance to political subdivisions, public corporations, instrumentalities and municipalities of the Commonwealth responsible for developing and operating infrastructure facilities, and (ii) providing an alternative means for directly financing those facilities. The Enabling Act defines "infrastructure" to include public works and facilities of a substantial public interest, such as aqueduct and sewer systems including water supply systems, waste water treatment and disposal systems, improvements financed under the provisions of the Federal Clean Water Act and the Federal Safe Drinking Water Act, solid and hazardous waste disposal systems, resource recovery systems, electric power systems, highways, roads, pedestrian walkways, parking facilities, airports, convention centers, bridges, maritime ports, tunnels, transportation systems including mass transportation, communication systems including telephones, industrial facilities, land and natural resources, public housing projects, and tourist, medical and agro-industrial infrastructure facilities. The Financing Authority has all the necessary and convenient powers to accomplish and effectuate the purposes and provisions of the Enabling Act, including the power to negotiate and enter into assistance agreements with political subdivisions, public corporations, instrumentalities and municipalities of the Commonwealth authorized to provide infrastructure for the purpose of carrying out necessary financing programs for the development of infrastructure and providing consulting, technical, administrative, advisory, and other assistance in all matters related to such facilities. Any such entity receiving assistance from the Financing Authority (a "Benefited Entity") may be required to comply with all operational, administrative and budgetary requirements that the Financing Authority considers pertinent to achieve the purposes of said assistance.

The Financing Authority has signed assistance agreements with among others, the Municipality of Carolina, the Department of Health, the Department of Education, the Department of Transportation and Public Works, the Department of Environmental and Natural Resources, the Public Buildings Authority, the Highways and Transportation Authority, the Land Authority, the Courts Administration Office, the Institute of Puerto Rican Culture, the Department of Sports and Recreation, the Puerto Rico State Historic Preservation Office, the Fine Arts Center Corporation, the Public Schools Improvement Office, the Puerto Rico Science, Research and Technology Trust Fund, the Special Communities Perpetual Trust, and the University of Puerto Rico. The Financing Authority has executed an assistance agreement with the Ports Authority in connection with the issuance of the Bonds.

The Financing Authority has heretofore authorized and issued bonds under the Enabling Act for its own use and for the benefit of certain Benefited Entities. Each series of such bonds constitutes a separate obligation of the Financing Authority payable only from the revenues and other funds pledged to secure such bonds. None of the revenues or other funds pledged to secure such bonds are pledged to or available to pay the Bonds.

The executive offices of the Financing Authority are located at the Roberto Sánchez Vilella Government Center, North Tower, 8th Floor, De Diego Ave., Stop 22, Santurce, P.R. 00907. Its telephone number is (787) 763-5757.

The Enabling Act provides that the Board of Directors of the Financing Authority (the "Board") shall be composed of the Board of Directors of Government Development Bank and the Secretary of the Treasury of Puerto Rico (in the event the Secretary of the Treasury is not a member of Government Development Bank's Board of Directors). Members of the boards or officers of any Benefited Entity are specifically excluded from serving on the Board. The Secretary of the Treasury is the Chairman of the Board.

The Board appoints officers and employs agents and employees who are responsible for the general operation of the Financing Authority.

José E. Basora Fagundo serves as the Executive Director of the Financing Authority.

THE PORTS AUTHORITY

The Ports Authority is a public corporation and government instrumentality of the Commonwealth, established and existing under Act No. 125 of the Legislative Assembly of Puerto Rico, approved May 7, 1942, as amended. The Ports Authority was created to administer the public port and aviation transportation facilities in Puerto Rico and to provide other related services. The Ports Authority owns and operates Luís Muñoz Marín International Airport ("LMM Airport"), the largest (in terms of enplanements) airport in the Caribbean region and the primary aviation port of entry into Puerto Rico, as well as 11 regional airports and most governmentally owned maritime operations, including the Port of San Juan. Maritime operations consist principally of cargo and cruise ships with ports and docks throughout Puerto Rico.

The Ports Authority currently is in the process, through and with the assistance of the Puerto Rico Public Private Partnership Authority ("PPPA"), of soliciting proposals to grant a long-term concession for the operation of LMM Airport (the "LMM Concession"). The proposed concession is the second of its type undertaken by PPPA; the Commonwealth recently entered into a long-term concession agreement for certain toll roads. See "GOVERNMENT DEVELOPMENT BANK - Loans to the Commonwealth, its Public Corporations and Municipalities - Loans to Public Corporations - Highways and Transportation Authority." In September 2011, PPPA completed its review of the statements of qualifications submitted by proponents wishing to operate the LMM Airport and selected six proponents to whom it has issued a request for proposals with respect to the LMM Concession. These consortia comprise the following: (i) Flughafen Zürich AG, Public Sector Pension Investment Board (PSP), Camargo Corrêa Investimento em Infra-Estructura and Gestión e Ingeniería (IDC); (ii) Fraport AG and Goldman Sachs Infrastructure Partners; (iii) GMR Infrastructure and Incheon International Airport Corporation; (iv) Grupo Aeroportuario del Sureste (ASUR) and Highstar Capital; (v) Grupo Aeropuertos Avance (Macquarie and Ferrovial Aeropuertos); and (vi) Puerto Rico Gateway Group (GE Capital Aviation, Allegheny County Airport Authority, TIAA-CREF, OpTrust and Airmall USA). Final proposals from such consortia are expected to be due, and a final decision with respect to the awarding of the concession currently is expected to be made during the first calendar quarter of 2012.

Although the final terms of the concession agreement have not yet been established, the Ports Authority expects that the term could be up to 50 years. Under the concession agreement, it is expected that all or substantially all of LMM Airport operating revenues will inure to the benefit of the successful proponent for the term of the concession, in exchange for an upfront payment to the Ports Authority and subject to the terms and conditions of the concession agreement. At this time, it is not possible for the Ports Authority to predict the final terms of the concession agreement, including the amount of any upfront payment to the Ports Authority, or whether any such concession will be awarded. Any upfront payment that the Ports Authority may receive if it does award the LMM Concession, after the satisfaction of any indebtedness, other obligations or expenses that may be paid or payable therefrom, including any payment to LMM terminal owners for the transfer to the Ports Authority of title and/or control of their terminals, may be applied, in whole or in part, at the option of the Ports Authority, to the extraordinary optional redemption of the Bonds. The Ports Authority has covenanted in the Reimbursement Agreement to so apply such payment in an amount agreed to by Government Development Bank and the Ports Authority. See "DESCRIPTION OF THE BONDS - Redemption - Extraordinary Optional Redemption" and "- Selection of Bonds to be Redeemed - Extraordinary Optional Redemption, " and Appendix D - "Summary of Certain Provisions of the Reimbursement Agreement - Covenants of the Borrower."

As currently structured and without awarding the LMM Concession, the Ports Authority does not expect to be able to meet its current liabilities and pay debt service in full on the loan of Bond proceeds, as and when due, with its existing revenues, without the benefit of the GDB Letter of Credit. If the LMM Concession is awarded, it is not possible at this time to predict what the Ports Authority's remaining revenues and liabilities will be in order to evaluate the Ports Authority's future ability to pay its liabilities and debt service on the loan of Bond proceeds, as and when due. **ACCORDINGLY, THE BONDS ARE BEING OFFERED SOLELY ON THE FINANCIAL CAPACITY OF GOVERNMENT DEVELOPMENT BANK AND NOT ON THE FINANCIAL CAPACITY OF THE PORTS AUTHORITY OR ANY OTHER SECURITY, OTHER THAN THE GDB LETTER OF CREDIT. INVESTORS IN THE BONDS WILL NOT BE ABLE TO ASSESS THE ABILITY OF THE PORTS AUTHORITY TO PAY DEBT SERVICE ON THE BONDS OR THE PURCHASE PRICE OF THE SERIES 2011C BONDS SHOULD A GOVERNMENT DEVELOPMENT BANK DEFAULT OR FAILURE TO HONOR A DRAW ON THE GDB LETTER OF CREDIT OCCUR.**

THE BONDS, HOWEVER, ARE NOT SUBJECT TO REDEMPTION OR ACCELERATION UPON A PAYMENT DEFAULT BY THE PORTS AUTHORITY UNDER THE REIMBURSEMENT AGREEMENT.

RISK FACTORS

Prospective purchasers should consider carefully the following factors and other information in this Official Statement before deciding to invest in the Bonds. The following discussion of investment considerations involved in purchasing and owning the Bonds is not, and is not intended to be, a complete list of the considerations associated with the purchase of the Bonds and does not necessarily reflect the relative importance of the various factors. Prospective purchasers of the Bonds are advised to consider the following investment considerations, among others, and to review the other information in this Official Statement when evaluating an investment in the Bonds.

Risks related to the Bonds

The Bonds are limited obligations of the Financing Authority payable through the payments made by the Ports Authority under the Loan and Trust Agreement and by Government Development Bank under the GDB Letter of Credit. The Bonds will be limited obligations of the Financing Authority payable solely from and secured by the Revenues received under the Loan and Trust Agreement, including draws under the GDB Letter of Credit. The Bonds are not directly secured by any collateral other than the GDB Letter of Credit. No other entity will have any obligation, contingent or otherwise, to make any payments with respect to the Bonds. None of the Financing Authority, Government Development Bank or the Ports Authority has any taxing power. **THE BONDS ARE BEING OFFERED SOLELY ON THE FINANCIAL CAPACITY OF GOVERNMENT DEVELOPMENT BANK AS ISSUER OF THE GDB LETTER OF CREDIT AND NOT ON THE FINANCIAL CAPACITY OF THE PORTS AUTHORITY OR ANY OTHER SECURITY, OTHER THAN THE GDB LETTER OF CREDIT.**

Redemption and Mandatory Purchase. The Bonds are subject to redemption upon the occurrence of certain events more particularly described under "DESCRIPTION OF THE BONDS – Redemption," and the Series 2011C Bonds are subject to mandatory tender for purchase at certain times as more particularly described under "DESCRIPTION OF THE BONDS – Series 2011C Bonds – Mandatory Tender of Series 2011C Bonds for Purchase." Rights of redemption include the right of redemption at the option of the Ports Authority. Owners of the Bonds are subject to these rights of redemption and mandatory tender for purchase and will be unable to continue to hold their Bonds in the event of such a redemption or mandatory tender for purchase. In making their decision to invest, prospective purchasers should consider that the Ports Authority is in the process of obtaining proposals from proponents for the LMM Concession. A final decision regarding the award of the LMM Concession, if any, is expected during the first calendar quarter of 2012, although there can be no assurance that any such LMM Concession will be awarded. If the LMM Concession is awarded, all or a portion of the Bonds may be redeemed prior to December 15, 2014. See "DESCRIPTION OF THE BONDS - Redemption - Extraordinary Optional Redemption" and "- Selection of Bonds to be Redeemed - Extraordinary Optional Redemption, " and Appendix D - "Summary of Certain Provisions of the Reimbursement Agreement - Covenants of the Borrower."

Possible Acceleration of the Bonds. Under the terms of the Loan and Trust Agreement, upon the occurrence of certain Events of Default thereunder, including an Act of Bankruptcy of the Bank, the Trustee is required to accelerate all of the Bonds and declare the Bonds to be immediately due and payable. In such event, the principal of the Bonds, without premium, and all interest accrued thereon to the accelerated payment date shall become due and payable. The Bonds, however, are not subject to acceleration upon a payment default by the Ports Authority under the Reimbursement Agreement. See "SOURCES OF PAYMENT AND SECURITY FOR THE BONDS – Acceleration" and APPENDIX B — "Summary of Certain Provisions of the Loan and Trust Agreement" under the heading "Events of Default."

Risks related to Government Development Bank

The ability of Government Development Bank to honor its obligations under the GDB Letter of Credit depends on its financial condition. Payment of principal, Purchase Price or redemption price of and interest on the Bonds is secured by the GDB Letter of Credit. The GDB Letter of Credit is the Bondowners' primary expected source of payment of principal of and interest on the Bonds. Payment of these amounts will depend on the creditworthiness of Government Development Bank. For information on the GDB Letter of Credit and Government Development Bank see "THE GDB LETTER OF CREDIT" and "GOVERNMENT DEVELOPMENT BANK" herein, and APPENDIX E — "Basic Financial Statements and Required Supplementary Information of Government Development Bank for Puerto Rico as of and for the Year Ended June 30, 2011." There can be no assurance that Government Development Bank will maintain its present financial condition or that an adverse change in such condition will not adversely affect its ability to honor future drawings under the GDB Letter of Credit. A change in the creditworthiness of Government Development Bank could result in changes in the ratings on the Bonds.

The fiscal situation and condition of the Commonwealth, its public corporations and municipalities may negatively affect the financial condition and liquidity of Government Development Bank. One of Government Development Bank's principal functions is to provide financing to the Commonwealth and its instrumentalities, public corporations and municipalities. These financings include interim loans to finance the capital expenditures of the Commonwealth and its instrumentalities, public corporations and municipalities in anticipation of the issuance of bonds and notes, and loans to cover operational deficits of such governmental entities. The aggregate amount of these loans by Government Development Bank has generally increased in recent years as a result of (i) the deterioration of the fiscal situation and financial condition of the Commonwealth and its principal instrumentalities, as well as certain municipalities, and (ii) general market conditions as a result of the global financial crisis, which market conditions have negatively affected the ability of the Commonwealth and its instrumentalities and public corporations to permanently finance their capital expenditures and operating deficits by issuing bonds and notes. Any further deterioration of the fiscal situation and financial condition of the Commonwealth and its instrumentalities, public corporations and municipalities may have an adverse effect on the financial condition and liquidity of Government Development Bank.

The access of the Commonwealth and its instrumentalities and public corporations to funding through the bond market to finance their capital improvement programs, as well as any future operating deficits, may be adversely affected if their respective credit ratings are downgraded. If the credit ratings of the Commonwealth or any of its instrumentalities and public corporations are downgraded, Government Development Bank may be asked to provide financing for these capital improvement programs or for working capital needs. Government Development Bank is not required by law to provide such financing. Under Act No. 164 of 2001, as amended, Government Development Bank is prohibited from making loans to any governmental entity for which the source of repayment consists of appropriations from the General Fund without first obtaining the approval of the Legislative Assembly, with certain limited exceptions, including up to an aggregate amount of $100 million in loans (decreased from $200 million on June 30, 2011) without Legislative Assembly approval, and including loans needed to cover the governmental entity's debt service.

Government Development Bank generally does not provide financing to any governmental entity of Puerto Rico unless Government Development Bank reasonably believes that the borrowing governmental entity will have sufficient resources, including the ability to issue bonds or notes or otherwise borrow funds, to repay such loan. Government Development Bank, however, has provided financing in the past and may continue to provide financing to government entities that do not have sufficient independent resources to cover operating expenses, to the extent permitted by law. A material increase in the amount of loans to the public sector, coupled with continued deterioration of the public sector's fiscal situation and financial condition, may have an adverse effect on Government Development Bank's financial condition and liquidity.

Government Development Bank is not subject to single borrower limitations. Government Development Bank is not subject to limitations on loans to one borrower, and the default by one debtor or a few debtors may have a materially adverse effect on the value of its assets, its liquidity or even cause it to fail. As of June 30, 2011, loans to the Treasury Department, the Highways and Transportation Authority and Puerto Rico

Aqueduct and Sewer Authority ("PRASA") represented approximately 8.29%, 15.78%, and 12.56%, respectively, of Government Development Bank's total loan assets, and collectively represent 36.63% of its total loan assets. Moreover, Government Development Bank is not restricted from further increasing the concentration of its loans to the abovementioned entities or to any other agencies or parties. To manage the credit risk of its debtors, Government Development Bank has entered into fiscal oversight agreements ("FOAs") with certain of its debtors, including the Ports Authority, PRASA and the Highways and Transportation Authority, whereby Government Development Bank, among other things, imposes conditions on the extensions of credit to these entities and continually monitors their finances. Although Government Development Bank monitors and manages its credit risk, there is no precise method of predicting how the credit standing of a borrower may be impacted by unforeseen circumstances. The default by any such borrower on Government Development Bank's loans may have a material adverse effect on the financial condition of Government Development Bank, its liquidity or even cause it to fail.

Adverse movements in interest rates may negatively affect Government Development Bank's net interest income and value of its investments. Adverse movements in interest rates may negatively affect Government Development Bank's net interest income and the value of its investments. Interest rates are highly sensitive to many factors, such as governmental monetary policies and domestic and international economic and political conditions that are beyond the control of Government Development Bank.

Repayment of Puerto Rico's public debt has priority over repayment of loans made by Government Development Bank. The Puerto Rico Constitution provides that if the Commonwealth were to have insufficient funds to pay all approved appropriations, the available resources of the Commonwealth would have to be used to pay public debt backed by the good faith and credit of the Commonwealth before being used for any other purpose, including paying any loans due to Government Development Bank.

Failure by the Legislative Assembly to appropriate sufficient funds to cover amounts due to Government Development Bank by its public sector debtors or lack of alternate financing would adversely affect its financial condition. As of June 30, 2011, public sector loans by Government Development Bank amounting to approximately $2.3 billion were delinquent by 90 days or more or had matured. Public sector loans classified as non-accrual amounted to approximately $57 million at such date. Government Development Bank expects to incur no losses with respect to principal and interest on most of its loans to the public sector (including municipalities) and, as a result, no allowance for loan losses is generally established for such loans. However, there can be no assurance that the director of the Puerto Rico Office of Management and Budget ("OMB") will include amounts for loan repayments in the Commonwealth's budget, and that the Legislative Assembly will appropriate sufficient funds in the future to cover all amounts due to Government Development Bank by the Commonwealth or public sector debtors requiring the Commonwealth's support, or that the proceeds from any future bond issuances by the Puerto Rico Sales Tax Financing Corporation ("COFINA" by its acronym in Spanish) or certain public entities which have financed their capital improvement programs with Government Development Bank or any other potential sources of repayment that may be available will be sufficient to cover the outstanding amount of extra-constitutional or capital improvement program debt at June 30, 2011. The participation of certain public entities in the bond market has been delayed pending an improvement in the credit rating of such entities or more favorable market conditions. The timing and amount of any financial assistance and bond proceeds to be used to repay certain public sector loans cannot be reasonably estimated by Government Development Bank. Government Development Bank, however, has in the past collected the outstanding principal and interest at the contractual rate on loans repaid from Commonwealth appropriations or bond proceeds.

Risks related to the Ports Authority

Financial Condition of the Ports Authority. Without awarding the LMM Concession, the Ports Authority does not expect that it will be able to meet all of its current liabilities and satisfy its obligations under the Loan and Trust Agreement, as and when due, with its existing revenues, without the benefit of the GDB Letter of Credit. Even if the Ports Authority does award the LMM Concession, it is not possible at this time to predict what the Ports Authority's remaining revenues and liabilities will be, in order to evaluate the Ports Authority's future ability to pay its current liabilities and satisfy its obligations under the Loan and Trust Agreement, as and when due. See "THE PORTS AUTHORITY."

Other Risks Related to the Bonds

The enforceability of remedies may not be available or may be limited. The remedies available to the owners of the Bonds upon an Event of Default under the Loan and Trust Agreement may depend upon regulatory and judicial actions which are often subject to discretion and delay. Under existing constitutional and statutory law and judicial precedent, the remedies specified by the Loan and Trust Agreement may not be applicable, readily available, or may be limited, especially in the event of a bankruptcy/insolvency of Government Development Bank. The various legal opinions to be delivered concurrently with the delivery of the Bonds will be qualified as to the enforceability of the various legal instruments, by limitations imposed by bankruptcy, reorganization, insolvency or other similar laws affecting the rights of creditors generally and by general principles of equity.

The market value of the Bonds may be affected by a negative change in their ratings. The ratings initially assigned to the Bonds may be lowered or withdrawn by the rating agencies at any time. Such rating changes could adversely affect the value of and market for the Bonds.

A secondary market for the Bonds may not develop. There is currently no secondary market for the Bonds, and there can be no assurance that a secondary market will develop, or if it does develop, that it will provide owners of the Bonds with liquidity for their investment or that it will continue for the life of the Bonds. The Underwriters do not have a legal obligation to maintain a market for the Bonds.

PLAN OF FINANCING

The proceeds from the sale of the Bonds will be loaned by the Financing Authority to the Ports Authority under the Loan and Trust Agreement and applied to finance and refinance some or all of the following: (i) the repayment of certain commercial loans; (ii) the payment of a swap termination fee relating to one of the loans; (iii) the repayment to Government Development Bank of certain loans and lines of credit; (iv) the payment of certain amounts owed by the Ports Authority to the Puerto Rico Electric Power Authority and with respect to certain capital expenditures; and (v) the payment of the cost of issuing the Bonds. See also, "UNDERWRITING."

As described above, proceeds of the Bonds will be used to prepay certain indebtedness of the Ports Authority to commercial lenders, as well as to Government Development Bank. The commercial loans being prepaid and the swap agreement that is being terminated currently are secured either by letters of credit or by guaranties of Government Development Bank. Upon the prepayment of such indebtedness and the termination of the swap agreement (the unlimited payments under which are guaranteed by Government Development Bank), the obligations of Government Development Bank under such letters of credit and guaranties will be extinguished. Below is a summary of the sources and uses of Bond proceeds and other funds, rounded to the nearest dollar.

Sources and Uses of Funds

Sources of Funds	
Principal Amount of the Series 2011 Bonds	$669,215,000
Net Original Issue Premium	9,236,920
Swap Collateral Release	11,830,000
Total	$690,281,920
Uses of Funds	
Repay Loans	$435,041,961
Operational and Capital Expenditures	79,200,000
Swap Termination Fee	61,837,000
Repay Government Development Bank Loans and Lines of Credit	100,331,250
Cost of Issuance*	8,665,311
Capitalized Interest	5,206,398
Total	$690,281,920

* Includes Underwriters' discount and initial GDB Letter of Credit fee.

DESCRIPTION OF THE BONDS

General

The Series 2011A Bonds and the Series 2011B Bonds will be issued as fixed rate bonds, will be dated their date of delivery, and will bear interest at such rates, be payable at such times, and mature on the dates and in the principal amounts set forth on the cover and inside cover of this Official Statement. Interest on the Series 2011A Bonds and Series 2011B Bonds will be payable on each June 15 and December 15, commencing June 15, 2012.

The Series 2011C Bonds will be issued initially in the Term Rate Mode and will bear interest at the initial Term Rates, as set forth on the inside cover of this Official Statement from their date of issuance to the end of the initial Term Rate Periods, as set forth on the inside cover. At the option of the Ports Authority and upon certain conditions provided for in the Loan and Trust Agreement, the Series 2011C Bonds may be (i) converted to another Term Rate Period, consisting of any multiple of six months, or (ii) converted to the Fixed Rate Mode. See "Series 2011C Bonds - Conversion of the Series 2011C Bonds" below.

The Series 2011C Bonds will be dated their date of initial delivery, and will bear interest from such date, payable on June 15, 2012, and on each December 15 and June 15 thereafter, and on the Purchase Date that follows the last day of the each Term Rate Period. The Series 2011C Bonds will mature on December 15, 2026.

The Bonds are issuable as fully registered bonds without coupons in denominations of $5,000 or integral multiples thereof. The Bonds will be registered under the DTC Book-Entry Only System described below. The principal or redemption price of and interest on the Bonds will be payable as described below under "Book-Entry Only System."

Redemption

Extraordinary Optional Redemption. The Bonds will be subject to redemption from Eligible Funds, at the option of the Ports Authority, prior to maturity, upon direction to the Financing Authority and the Trustee, in whole or in part, at any time on or prior to December 15, 2014, as a result of any available moneys that may be received by or on behalf of the Ports Authority in consideration of entering into the LMM Concession. Any upfront payment that the Ports Authority may receive, if it does award the LMM Concession, after the satisfaction of any indebtedness, obligations or other expenses that may be paid or payable therefrom, may be applied, in whole or in part, at the option of the Ports Authority, to the extraordinary optional redemption of the Bonds, and the Ports Authority has covenanted in the Reimbursement Agreement to so apply such payment in an amount agreed to by Government Development Bank and the Ports Authority. Any Bonds originally issued at par will be redeemed at a price equal to 100% of the principal amount of the Bonds to be redeemed, plus accrued and unpaid interest to the redemption date, without redemption premium. Any Bonds with an original offering price less than the stated principal amount thereof (collectively, the "Discount Bonds") will be redeemed at the original offering price of the Bonds, plus the original issue discount accrued to the redemption date, plus accrued and unpaid interest to the redemption date, without redemption premium. Any Bonds with an original offering price more than the stated principal amount thereof (collectively, the "Premium Bonds") will be redeemed at the original offering price of the Bonds, less the original issue premium amortized to the redemption date, plus accrued and unpaid interest to the redemption date, without redemption premium.

The original issue discount accrued to the redemption date when the redemption date is an interest payment date will be the amount of discount that results in a yield to the redemption date equal to the yield to maturity at which the Bond was originally sold. The original issue premium amortized to the redemption date when the redemption date is an interest payment date will be the amount of premium that results in a yield to the redemption date equal to the yield to call at which the Bond was originally sold. If the redemption date is between interest payment dates, the amount of discount or premium will be calculated based on the assumption that discount accrues and premium amortizes between interest payment dates in equal daily amounts on the basis of a 360-day year consisting of twelve 30-day months.

See Appendix H - "Table of Discount Bonds and Premium Bonds" for tables illustrating the redemption price for each Discount Bond or Premium Bond on interest payment dates from the date of original issue until the expiration of the Extraordinary Redemption period. The tables do not reflect accrued interest.

Sinking Fund Redemption. The Series 2011C Bonds will be subject to redemption from sinking fund installments at their principal amounts, without premium, plus accrued interest to the redemption date on December 15 of each of the years and in the principal amounts as follows:

$96,785,000 Term Bond Due December 15, 2026

Year (December 15)	Principal Amount
2014	$ 275,000
2015	855,000
2016	990,000
2017	590,000
2018	545,000
2021	2,045,000
2022	12,920,000
2023	330,000
2024	2,900,000
2025	1,540,000
2026*	73,795,000

* Maturity

$39,600,000 Term Bond Due December 15, 2026

Year (December 15)	**Principal Amount**
2014	$ 115,000
2015	350,000
2016	405,000
2017	240,000
2018	225,000
2021	835,000
2022	5,285,000
2023	135,000
2024	1,185,000
2025	630,000
2026*	30,195,000

* Maturity

Optional Redemption. The Series 2011B Bonds will be subject to redemption from Eligible Funds, at the option of the Ports Authority prior to maturity, upon direction to the Financing Authority and the Trustee, in whole or in part, on any date not earlier than December 15, 2021, at a redemption price equal to 100% of the principal amount of the Series 2011B Bonds to be redeemed plus accrued and unpaid interest to the redemption date, without redemption premium.

The Series 2011C Bonds in a Term Rate Mode with a Term Rate Period of less than five years (or, upon conversion to the Fixed Rate Mode, with a period to final maturity of less than five years), are not subject to optional redemption other than on their applicable Purchase Dates (but are subject to extraordinary optional redemption, as described above under "Redemption - Extraordinary Optional Redemption"). Series 2011C Bonds in the Term Rate Mode with a Term Rate Period of five years or more (or, upon conversion to the Fixed Rate Mode, with a final maturity measured from the Fixed Rate Conversion Date of at least five years) are subject to redemption from Eligible Funds, at the option of the Ports Authority, upon direction to the Financing Authority and the Trustee, in whole or in part on any date, at a redemption price equal to 100% of the principal amount of the Series 2011C Bonds to be redeemed, plus accrued and unpaid interest to the redemption date, commencing on the dates set forth below:

Length of Term Rate Period or Period to Maturity	**Commencement of Redemption Period**
Greater than or equal to 10 years	Seventh anniversary of the commencement of Term Rate Period or Fixed Rate Conversion Date
Less than 10, and greater than or equal to 5 years	Third anniversary of the commencement of Term Rate Period or Fixed Rate Conversion Date
Less than 5 years	Series 2011C Bonds not subject to optional redemption

Selection of Bonds to be Redeemed

Extraordinary Optional Redemption. If the Ports Authority elects to redeem Bonds pursuant to the Extraordinary Optional Redemption provisions described above, the Bonds will be redeemed from Eligible Funds, through the application by the Ports Authority of monies resulting from entering into the LMM Concession, in the following order and amounts, until such monies are exhausted:

First, to the redemption of the Series 2011A Bonds, in an amount up to $176,700,000;
Second, to the redemption of the Series 2011B Bonds, in an amount up to $143,285,000;
Third, to the redemption of the remaining Series 2011A Bonds;
Fourth, to the redemption of the Series 2011C Bonds; and
Fifth, to the redemption of the remaining Series 2011B Bonds.

If less than all of the Series 2011A Bonds are to be redeemed and so long as CEDE & CO., as nominee of DTC, is the Bondowner, the Trustee shall instruct DTC to instruct the DTC participants to select the specific Series 2011A Bonds to be redeemed on a *pro-rata* basis, and none of the Ports Authority, the Trustee or the Financing Authority shall have any responsibility to ensure that DTC or its participants properly select such Series 2011A Bonds for redemption. See "Book-Entry Only System" below. If less than all of the Series 2011A Bonds are to be redeemed prior to maturity and the Series 2011A Bonds are not then in book-entry form at the time of such redemption, the Trustee shall select the specific Series 2011A Bonds for redemption on a *pro-rata* basis on each redemption date. The portion of any registered Series 2011A Bond of a denomination of more than $5,000 to be redeemed, will be in the principal amount of $5,000 or any integral multiple thereof, and in selecting portions of such Series 2011A Bonds for redemption, the Trustee will treat each such Series 2011A Bond as representing that number of Series 2011A Bonds of $5,000 denominations that is obtained by dividing the principal amount of such Series 2011A Bonds by $5,000. If less than all of the Series 2011B Bonds or the Series 2011C Bonds are to be redeemed, such Bonds shall be redeemed in such order of maturity or sinking fund installment, as directed by the Ports Authority so long as no Event of Default exists, and otherwise by the Trustee. The selection for redemption of Series 2011B Bonds and Series 2011C Bonds or portions thereof within a maturity or sinking fund installment shall be by lot by the Trustee or in any other customary manner determined by the Trustee. So long as CEDE & CO., as nominee of DTC, is the Bondowner, the particular Bonds or portions thereof to be redeemed within a maturity or sinking fund installment shall be selected by lot by DTC, in such manner as DTC may determine. See "Book-Entry Only System" below.

Optional Redemption. The Series 2011B Bonds and the Series 2011C Bonds to be redeemed at the option of the Ports Authority as described above shall be redeemed in such order of maturity or sinking fund installment, as directed by the Ports Authority so long as no Event of Default exists, and otherwise by the Trustee. The selection for redemption of Series 2011B Bonds and Series 2011C Bonds or portions thereof within a maturity or sinking fund installment shall be by lot by the Trustee or in any other customary manner determined by the Trustee. So long as CEDE & CO., as nominee of DTC, is the Bondowner, the particular Bonds or portions thereof to be redeemed within a maturity or sinking fund installment shall be selected by lot by DTC, in such manner as DTC may determine. See "Book-Entry Only System" below.

Notice of Redemption; Effect

When Bonds are to be redeemed, the Trustee shall give notice to the Bondowners in the name of the Financing Authority, which notice shall identify the Bonds to be redeemed, state the date fixed for redemption and specify the office of the Trustee at which such Bonds will be redeemed. The notice shall further state that on such date there shall become due and payable upon each Bond to be redeemed the redemption price thereof, together with interest accrued to the redemption date, and that monies therefor having been deposited with the Trustee, from and after such date, interest thereon shall cease to accrue and that the Bonds or portions thereof called for redemption shall cease to be entitled to any benefit under the Loan and Trust Agreement except the right to receive payment of the redemption price. The Trustee shall mail the redemption notice not less than 30 days prior to the date fixed for redemption to the registered owners of any Bonds which are to be redeemed, at their addresses shown on the registration books maintained by the Trustee. Any notice of extraordinary optional redemption or optional redemption may state that the redemption is conditional and, if so, the notice shall state what the conditions are. In addition, if at the time of mailing a notice of redemption there shall not have been deposited with the Trustee Eligible Funds sufficient to redeem the Bonds called for redemption, such notice may state that it is conditional upon the deposit of the Eligible Funds with the Trustee on the redemption date, and such notice shall be of no effect unless such Eligible Funds are so deposited. Any notice of extraordinary optional redemption or optional redemption may be rescinded by notice given by the Trustee by mail, or by such other means as may be acceptable to DTC so long as the Bonds are in the Book-Entry Only System, no later than two Business Days prior to the date specified for redemption. Failure to give notice to a particular Bondowner, or any defect in the notice to such Bondowner, shall not affect the redemption of any other Bond.

Purchase for Cancelation

The Ports Authority may purchase Bonds of a series and credit them against any corresponding principal coming due on or sinking fund installment for the Bonds of such series at the principal amount or applicable redemption price, as the case may be, by delivering them to the Trustee for cancellation at least 45 days before the principal due date or sinking fund installment date.

Series 2011C Bonds

General. The initial Term Rates for the Series 2011C Bonds shall be as set forth on the inside cover of this Official Statement and shall be effective as of the date of issuance of the Series 2011C Bonds through and including the last day of the initial Term Rate Periods, as set forth on the inside cover. Thereafter, while the Series 2011C Bonds are in the Term Rate Mode, a new Term Rate shall take effect on the first day of each Term Rate Period.

While the Series 2011C Bonds are in the Term Rate Mode, the Term Rate in effect for each Term Rate Period after the initial Term Rate Periods shall be determined on the Rate Determination Date (defined below) and shall be the rate of interest determined by Wells Fargo Securities, LLC, as the initial remarketing agent for the Series 2011C Bonds (the "Remarketing Agent"), for each Term Rate Period to be the lowest rate which in its judgment, on the basis of then existing market conditions, would permit the sale of the Series 2011C Bonds bearing interest at the Term Rate, at par plus accrued interest, if any, on and as of the applicable Rate Determination Date. The Rate Determination Date shall be a Business Day no earlier than 15 Business Days and no later than one Business Day next preceding the first day of the Term Rate Period, as determined by the Remarketing Agent.

If for any reason the interest rate on the Series 2011C Bonds cannot be established for any Term Rate Period, or is held invalid or unenforceable by a court of law, the interest rate on the Series 2011C Bonds during such Term Rate Period will equal the Term Rate Index, as determined by the Remarketing Agent. If for any reason the Remarketing Agent fails to announce the Term Rate, the Term Rate for that Term Rate Period shall be the same as the Term Rate for the immediately preceding Term Rate Period.

Conversion of the Series 2011C Bonds.

Change in Term Rate Period. The Term Rate Period applicable to particular Series 2011C Bonds may be changed by the Ports Authority, upon notice to the Financing Authority, the Trustee, Government Development Bank and the Remarketing Agent (the "Notice Parties"), stating its intention to effect a change in the Term Rate Period from the Term Rate Period then in effect (the "Current Period") to another Term Rate Period (the "New Period"). The New Period shall commence on the first day following the last day of the Current Period (the "Mode Change Date") applicable to such Series 2011C Bonds. Notice of the proposed change in the Term Rate Period is required to be given by the Trustee to the Owners of the affected Series 2011C Bonds not less than the 15th day next preceding the Mode Change Date. Such notice is required to state: (i) the Mode Change Date; (ii) that such Series 2011C Bonds will be subject to mandatory tender for purchase on the Mode Change Date and the Purchase Price to be paid on the Mode Change Date; and (iii) if the Book-Entry System is no longer in effect, information with respect to required delivery of Series 2011C Bond certificates and payment of Purchase Price.

The New Period applicable to the affected Series 2011C Bonds shall commence on the Mode Change Date and the Term Rate to be in effect for such New Period shall be determined by the Remarketing Agent as described above. The affected Series 2011C Bonds are required to be mandatorily tendered for purchase on the Mode Change Date at a Purchase Price equal to 100% of the principal amount thereof.

Change to Fixed Rate Mode. At the option of the Ports Authority, all or a portion of the Series 2011C Bonds may be converted to the Fixed Rate Mode upon written notice to the Notice Parties stating that the Series 2011C Bonds will be converted to the Fixed Rate Mode and setting forth the proposed Mode Change Date. In the event of a change to the Fixed Rate Mode, the Mode Change Date may be either any Interest Payment Date on which the Series 2011C Bonds are subject to optional redemption, or the next Purchase Date for the applicable Series 2011C Bonds. Such Series 2011C Bonds shall be purchased on such Mode Change Date at a Purchase Price equal to 100% of the principal amount thereof.

Not later than the 15th day next preceding the Mode Change Date, the Trustee is required to give notice, in the name of the Ports Authority, of such proposed change to the Owners of the affected Series 2011C Bonds stating that (i) the Mode will be changed to the Fixed Rate Mode, (ii) the proposed Mode Change Date, and (iii) that the Owners of the affected Series 2011C Bonds are required to tender their Series 2011C Bonds for purchase on such proposed Mode Change Date.

The Fixed Rate (or rates) for the Series 2011C Bonds to be converted to the Fixed Rate Mode shall be established by the Remarketing Agent not later than the second Business Day prior to the Mode Change Date. Such Fixed Rate (or rates) shall remain in effect for the remainder of the terms of the Series 2011C Bonds.

Failure to Satisfy Conditions Precedent to a Mode Change. In addition to the requirement described in the immediately following paragraph, no conversion shall occur unless (i) the Series 2011C Bonds remarketed in connection with the conversion are remarketed at a price of par, unless otherwise consented to by Government Development Bank, and (ii) the Purchase Price of all Series 2011C Bonds on such Mode Change Date is paid to the tendering Bondowners. In the event the conditions precedent to a Mode Change (including a change from the Current Period to a New Period) have not been satisfied by the applicable Mode Change Date (a "Failed Conversion"), then the Fixed Rate Mode or New Period will not take effect and the applicable Series 2011C Bonds will remain in the Term Rate Mode for the same length as the Current Period, but the mandatory tender of such Series 2011C Bonds shall occur on the proposed Mode Change Date.

No Series 2011C Bonds may be converted to a New Period or to the Fixed Rate Mode unless the Ports Authority has provided for the delivery to the Trustee, not later than the Mode Change Date, of an extension, or amendment to the Series C Letter of Credit in effect prior to the Mode Change Date, or a new letter of credit, substantially in the same form and substance as the Series C Letter of Credit then in effect, issued by Government Development Bank, in the Required Stated Amount, with a Stated Expiration Date not earlier than, in the case of Series 2011C Bonds to be remarketed in the Term Rate Mode, the Business Day following the next Purchase Date, and in the case of Series 2011C Bonds to be remarketed in the Fixed Rate Mode, the final maturity date of the Series 2011C Bonds. The failure of the Ports Authority to cause such extension, or amendment to the Series C Letter of Credit, or issuance of a new letter of credit as described above to be delivered to the Trustee not later than the Mode Change Date shall result in a Failed Conversion.

Rescission of Election. The Ports Authority may rescind any election by it to change a Mode (including a change to a New Period) prior to the Mode Change Date (a "Canceled Conversion") by giving written notice thereof to the Notice Parties prior to such Mode Change Date. If the Trustee receives notice of such Canceled Conversion prior to the time the Trustee has given notice to the Owners of the affected Series 2011C Bonds, then the Ports Authority's Mode Change notice shall be of no force and effect. If the Trustee receives notice from the Ports Authority of such Canceled Conversion after the Trustee has given notice thereof to the Owners of the affected Series 2011C Bonds, the Trustee shall promptly give notice to such Owners of such Canceled Conversion not later than the second Business Day prior to the Mode Change Date. In either event, the mandatory tender of such Series 2011C Bonds shall nonetheless occur on the proposed Mode Change Date.

Mandatory Tender of Series 2011C Bonds for Purchase. The Series 2011C Bonds are subject to mandatory tender for purchase at the Purchase Price on the first Business Day following the last day of each Term Rate Period, including the initial Term Rate Periods. **Owners of the Series 2011C Bonds agree to sell and surrender the Series 2011C Bonds at such Purchase Price to any purchaser determined in accordance with the provisions of the Loan and Trust Agreement in the event of such mandatory tender and, on the**

applicable Purchase Date, to surrender the Series 2011C Bonds to the Trustee for payment of the Purchase Price by 10:00 A.M. (New York City time). From and after the Purchase Date, no further interest on the Series 2011C Bonds required to be tendered for purchase shall be payable to the Owners thereof, provided that there are sufficient funds available on the Purchase Date to pay the Purchase Price.

The Purchase Price of any Series 2011C Bonds required to be tendered for purchase and not remarketed shall be paid through a drawing by the Trustee on the Series C Letter of Credit. No Series 2011C Bonds shall be remarketed unless there has been delivered to the Trustee, not later than the applicable Purchase Date for the particular Series 2011C Bonds, a Series C Letter of Credit in the Required Stated Amount with a Stated Expiration Date not earlier than, in the case of Series 2011C Bonds to be remarketed in the Term Rate Mode, the Business Day following the next Purchase Date, and in the case of Series 2011C Bonds to be remarketed in the Fixed Rate Mode, the final maturity date of the Series 2011C Bonds.

This paragraph is applicable only if the book-entry system has been discontinued and replacement bonds have been issued or if DTC has exercised its option to surrender and exchange its Bonds. If a Series 2011C Bond to be purchased is not delivered by the Owner to the Trustee by 12:00 noon (New York City time) on the Purchase Date, the Trustee shall hold any funds received for the purchase of those Series 2011C Bonds in trust in a separate account and shall pay the Purchase Price to the former Owners of the Series 2011C Bonds upon presentation and surrender of the Series 2011C Bonds from such account. Such undelivered Series 2011C Bonds shall cease to accrue interest as to the former Owners on such Purchase Date and moneys representing the Purchase Price shall be available against delivery of those Series 2011C Bonds at the Principal Office of the Trustee; provided, however, that any funds which shall be so held by the Trustee shall be applied in accordance with the Loan and Trust Agreement. The Trustee shall authenticate a replacement Series 2011C Bond for any undelivered Series 2011C Bond which may then be remarketed by the Remarketing Agent.

Remarketing of Series 2011C Bonds. The Remarketing Agent shall use its best efforts to offer for sale at par:

(i) all Series 2011C Bonds required to be purchased on a Purchase Date;

(ii) any Bank Bonds; and

(iii) any Borrower Bonds;

provided that in no event shall the Remarketing Agent remarket any Series 2011C Bonds to the Ports Authority, the Financing Authority or any Affiliate of either.

The Remarketing Agent shall notify by Electronic Means the Trustee, Government Development Bank and the Ports Authority by 2:00 P.M. (New York City time) on the Business Day preceding the Purchase Date if it has been unable to remarket any of the Series 2011C Bonds, and shall include in such notice the principal amount of Series 2011C Bonds it has been unable to remarket. The Trustee shall draw on the Series C Letter of Credit to pay the Purchase Price of any Series 2011C Bonds that have not been remarketed.

By 2:00 P.M. (New York City time) on the Purchase Date, and except as set forth in the Loan and Trust Agreement with respect to certain book-entry procedures, the Trustee shall purchase tendered Series 2011C Bonds from the tendering Owners at the applicable Purchase Price by wire transfer in immediately available funds. Funds for the payment of such Purchase Price shall be derived solely from the following sources and in the order of priority indicated, and neither the Trustee nor the Remarketing Agent shall be obligated to provide funds from any other source:

(a) immediately available funds on deposit in the Bond Purchase Fund;

(b) immediately available funds on deposit in the Series C Account of the Credit Facility Fund; and

(c) immediately available funds provided by the Ports Authority.

On each Purchase Date, such Series 2011C Bonds shall be delivered as follows:

(i) Series 2011C Bonds sold by the Remarketing Agent and purchased with funds described in clause (a) above shall be delivered by the Remarketing Agent to the purchasers of such Series 2011C Bonds by 2:30 P.M. (New York City time);

(ii) Series 2011C Bonds purchased with moneys described in clause (b) above shall be registered in the name of Government Development Bank, or its nominee; and

(iii) Series 2011C Bonds purchased by the Ports Authority with moneys described in clause (c) above shall be registered in the name of the Ports Authority or its nominee.

Series 2011C Bonds described in clauses (ii) and (iii) above shall continue to be outstanding under and be subject to all of the terms and conditions of the Loan and Trust Agreement and shall be subject to remarketing by the Remarketing Agent.

Book-Entry Only System

The following information regarding The Depository Trust Company ("DTC") and DTC's book-entry system has been extracted from information provided by DTC. Neither the Financing Authority nor the Ports Authority makes any representation as to the accuracy or the completeness of such information or as to the absence of material adverse changes in such information. Additionally, neither the Financing Authority nor the Ports Authority undertakes any responsibility for and makes any representations as to the accuracy or the completeness of the content of any material contained on DTC's website as described herein including, but not limited to, updates of such information or links to other Internet sites accessed through such website.

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

DTC, the world's largest securities depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 3.5 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments (from over 100 countries) that DTC's participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities, through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has Standard & Poor's rating of "AA+." The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com and www.dtc.org; nothing contained in such websites is incorporated into this Official Statement.

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

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

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

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

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

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

A Beneficial Owner required to tender its Series 2011C Bonds shall effect delivery of such Bonds by causing its Participant to transfer its interest in such Bonds on DTC's records to the Remarketing Agent. The requirement for physical delivery of Series 2011C Bonds in connection with a mandatory purchase will be deemed satisfied when the ownership rights in such Bonds are transferred by Direct Participants on DTC's records and followed by a book-entry credit of tendered Series 2011C Bonds to the Remarketing Agent's DTC account.

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

None of the Financing Authority, the Ports Authority, Government Development Bank, the Underwriters, or the Trustee can give any assurances that DTC, DTC Participants, Indirect Participants or others will distribute payments of principal of, premium, if any, and interest on the Bonds paid to DTC or its nominee, as the registered owner, or any redemption or other notice, to the Beneficial Owners or that they will do so on a timely basis or that DTC will serve and act in a manner described in this Official Statement.

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

If the Financing Authority is unable to retain a qualified successor to DTC or the Financing Authority has determined that DTC or its successor is no longer able to carry out its functions as a depository or that it is no longer desirable to use a depository, the Financing Authority will be required to deliver a written request to the Trustee, together with a supply of definitive Bonds in certificated form, to issue Bonds in any authorized denomination. Thereafter, the principal of the Bonds shall be paid in lawful money of the United States upon due presentment and surrender thereof at the principal office of the Trustee, interest on the Bonds will be payable by check mailed to the persons in whose names such Bonds are registered, at the address appearing upon the registration books on the first day of the month in which an interest payment date occurs, and the transfer of Bonds will be registrable as provided in the Loan and Trust Agreement.

SOURCES OF PAYMENT AND SECURITY FOR THE BONDS

The Financing Authority, the Ports Authority and the Trustee shall execute the Loan and Trust Agreement, which provides that the obligation of the Ports Authority to make payments under the Loan and Trust Agreement shall be absolute and unconditional, shall be binding and enforceable in all circumstances whatsoever, shall not be subject to a setoff, recoupment or counterclaim and shall be a general obligation of the Ports Authority to which the full faith and credit of the Ports Authority are pledged. The Loan and Trust Agreement also provides, among other things, that the Ports Authority shall make payments to the Trustee equal to the principal of or sinking fund installments, as the case may be, and interest due on the Bonds and certain other payments required by the Loan and Trust Agreement. In certain circumstances described above (see "DESCRIPTION OF THE BONDS – Series 2011C Bonds – Remarketing of Series 2011C Bonds"), the Ports Authority also is obligated to pay the Purchase Price of tendered Series 2011C Bonds that have not been remarketed. The Loan and Trust Agreement shall remain in full force and effect until such time as all of the Bonds and the interest thereon have been fully paid or until adequate provision for such payments has been made.

The Bonds are limited obligations of the Financing Authority, payable from the loan repayments of the Ports Authority pledged for such payment, and are secured by a pledge and assignment of amounts held in the funds and accounts established pursuant to the Loan and Trust Agreement. Loan repayments are required to be made by the Ports Authority pursuant to the Loan and Trust Agreement in amounts sufficient in the aggregate to pay the principal (and in certain circumstances the Purchase Price) of and premium, if any, and interest on the Bonds when such payments become due.

The Financing Authority will assign its right, title and interest in the Loan and Trust Agreement (except for the right to receive any notices and its administrative fees and expenses to the extent payable to the Financing Authority and the right of the Financing Authority to be indemnified pursuant thereto) to the Trustee.

In addition, the Trustee shall draw upon the GDB Letter of Credit for the payment of the principal and Purchase Price of and interest on the Bonds as the same shall become due whether at maturity, redemption or acceleration or upon mandatory tender.

THE BONDS ARE BEING OFFERED SOLELY ON THE BASIS OF THE FINANCIAL STRENGTH OF GOVERNMENT DEVELOPMENT BANK AND NOT ON THE FINANCIAL STRENGTH OF THE PORTS AUTHORITY OR OTHER SECURITY. THE BONDS ARE NOT DIRECTLY SECURED BY ANY COLLATERAL OTHER THAN THE GDB LETTER OF CREDIT. See "RISK FACTORS" herein.

Acceleration

Under the Loan and Trust Agreement, the Trustee is required to declare the Bonds immediately due and payable at par prior to maturity upon the occurrence of an Event of Default, including an Act of Bankruptcy of the Bank. Events of Default under the Loan and Trust Agreement include the failure to make any payment of principal or interest on the Bonds when due, the failure of Government Development Bank to honor a properly presented draw under the GDB Letter of Credit, an Act of Bankruptcy of the Bank, and if the interest on the Series 2011B Bonds or the Series 2011C Bonds ceases to be excluded from gross income of the owners thereof for federal income tax purposes; provided, however, that in such event only those Series 2011B Bonds or Series 2011C Bonds that cease to be excluded from gross income for federal income tax purposes shall be subject to acceleration. See APPENDIX B -- "Summary of Certain Provisions of the Loan and Trust Agreement" under the heading "Events of Default." A default by the Ports Authority under the Reimbursement Agreement, however, does not constitute an Event of Default under the Loan and Trust Agreement.

THE LOAN AND TRUST AGREEMENT

The Bonds will be issued under and secured by the Loan and Trust Agreement. Reference is made to the Loan and Trust Agreement for the complete details of the terms thereof. Attached as APPENDIX B is a summary of certain provisions of the Loan and Trust Agreement, which should not be considered a full statement thereof. APPENDIX A contains certain definitions used in this Official Statement.

THE REIMBURSEMENT AGREEMENT

Government Development Bank will agree to issue the GDB Letter of Credit pursuant to the terms of the Reimbursement Agreement. Reference is made to the Reimbursement Agreement for complete details of the terms thereof. Attached as APPENDIX D is a summary of certain provisions of the Reimbursement Agreement, which should not be considered a full statement thereof.

THE GDB LETTER OF CREDIT

Concurrently with the delivery of the Bonds, the GDB Letter of Credit will be issued by Government Development Bank. The GDB Letter of Credit irrevocably authorizes draws in accordance with its terms. Forms of the GDB Letter of Credit are attached as APPENDIX C.

The Series A/B Letter of Credit shall be issued in an aggregate amount not exceeding $543,076,007 (as reduced or reinstated from time to time in accordance with the terms of the Series A/B Letter of Credit), of which an amount not exceeding $532,830,000 (as reduced from time to time in accordance with the terms of the Series A/B Letter of Credit) may be drawn upon with respect to payment of the unpaid principal amount of the Series 2011A Bonds and the Series 2011B Bonds, and an amount not exceeding $10,246,007 (as reduced or reinstated from time to time in accordance with the terms of the Series A/B Letter of Credit) may be drawn upon with respect to payment of up to 180 days' interest accrued on the Series 2011A Bonds and the Series 2011B Bonds (computed at the actual rates of interest in effect on the Outstanding Series 2011A Bonds and Series 2011B Bonds on the basis of a 360-day year).

The Series C Letter of Credit initially shall be issued in an aggregate amount not exceeding $138,309,794 (as reduced or reinstated from time to time in accordance with the terms of the Series C Letter of Credit), of which an amount not exceeding $136,385,000 (as reduced from time to time in accordance with the terms of the Series C Letter of Credit) may be drawn upon with respect to payment of the unpaid principal amount or a portion of the Purchase Price corresponding to principal of the Series 2011C Bonds, and an amount not exceeding $1,924,794 (as reduced or reinstated from time to time in accordance with the terms of the Series C Letter of Credit) may be drawn upon with respect to payment of up to 180 days' interest or the portion of the Purchase Price corresponding to interest accrued on the Series 2011C Bonds (computed at the actual Term Rates in effect on the Series C Bonds during the initial Term Rate Periods, on the basis of a 360-day year).

Subject to the provisions described in the next succeeding paragraph, after a drawing for interest (an "Interest Drawing"), the portion of a GDB Letter of Credit available to pay interest (the "Interest Component") will be automatically reinstated in an amount equal to 180 days' accrued interest (computed as described above for the applicable GDB Letter of Credit) on the portion of the applicable GDB Letter of Credit then available to pay principal of the Bonds (the "Principal Component").

Each drawing for principal on the Bonds shall *pro tanto* reduce the Principal Component and the Interest Component, and any such reduction shall result in a corresponding reduction in the amount available to be drawn under the applicable GDB Letter of Credit.

The Series A/B Letter of Credit provides that it will expire on the earliest of (i) honoring of a final drawing by the Trustee under the Series A/B Letter of Credit, accompanied by the Series A/B Letter of Credit, (ii) the date on which Government Development Bank receives a certificate signed by the Trustee, accompanied by the Series A/B Letter of Credit, stating that the Series 2011A Bonds and the Series 2011B Bonds are no longer outstanding under the Loan and Trust Agreement, and (iii) December 15, 2026. The Series C Letter of Credit provides that it will expire on the earliest of (i) the honoring of a final drawing by the Trustee under the Series C Letter of Credit, accompanied by the Series C Letter of Credit, (ii) the date on which Government Development Bank receives a certificate signed by the Trustee, accompanied by the Series C Letter of Credit, stating that the Series 2011C Bonds are no longer outstanding under the Loan and Trust Agreement, and (iii) December 16, 2013.

GOVERNMENT DEVELOPMENT BANK

Organization and Powers

Government Development Bank is a public corporation and governmental instrumentality of the Commonwealth, created by Act No. 17 of the Legislative Assembly of Puerto Rico, approved September 23, 1948, as amended (the "GDB Act"), to aid the Commonwealth in the performance of its fiscal duties and more effectively carry out its governmental responsibility to develop the economy of Puerto Rico, particularly with respect to its industrialization. The GDB Act establishes Government Development Bank's charter (the "Charter"), which provides that its existence is perpetual. Pursuant to the GDB Act, no amendment to the GDB Act, or to any other law of the Commonwealth, may impair any outstanding obligation or commitment of Government Development Bank.

Under the Charter, Government Development Bank has the power, among other things, to borrow money; to issue bonds, notes, debentures, and other obligations; to lend money to and purchase obligations issued by the Commonwealth, its instrumentalities, public corporations and municipalities; to lend money to any other person when such monies are to be used to develop the economy of Puerto Rico; and to sue and be sued. It also has the power to acquire property for its own corporate purposes; to acquire any property in the settlement or reduction of debts previously contracted, where such acquisition is necessary to minimize or avoid loss in connection therewith; to establish branches, offices or agencies for the transaction of its business; to purchase, hold, lease, mortgage and convey real property; and to create subsidiary or affiliate corporations. See "General GDB Financial Information" below.

Government Development Bank is generally exempt from Commonwealth taxation. It is required to have an annual examination and audit by certified public accountants of national reputation selected by its Board of Directors. Government Development Bank is subject to examination and supervision by the Commissioner of Financial Institutions of the Commonwealth. The Comptroller of the Commonwealth, who is responsible to the

Legislative Assembly of Puerto Rico, also reviews the operations of Government Development Bank every two to three years.

Principal Functions

The principal functions of Government Development Bank are to act as fiscal agent, paying agent and financial advisor to the Commonwealth and its instrumentalities, public corporations and municipalities, and to the Governor, the Council of Secretaries, and the Secretary of Treasury; to provide interim and long-term financing to the Commonwealth and its instrumentalities, public corporations and municipalities, and to private parties for economic development; and to act as depositary or trustee of funds for the Commonwealth and its instrumentalities, public corporations and municipalities.

In its role as fiscal agent and financial advisor, it acts as advisor to the Commonwealth and its instrumentalities, public corporations and municipalities in connection with all their borrowings and all such borrowings are subject to prior approval by Government Development Bank. Government Development Bank receives fees for rendering such services. In its role as financial advisor, Government Development Bank will approve the issuance of the Bonds by the Financing Authority and the loan of the proceeds to the Ports Authority.

Government Development Bank lends to, and purchases and guarantees certain obligations of, the Commonwealth and its instrumentalities, public corporations and municipalities. It provides interim financing to these entities in anticipation of their refinancing such indebtedness in the public finance markets and also provides long-term financing to such entities. In fiscal years 2011, 2010, and 2009, Government Development Bank disbursed individual lines of credit and other financing facilities to the public sector in aggregate amounts of approximately \$4.6 billion, \$3.3 billion, and \$3.8 billion, respectively. For a breakdown of the outstanding principal amount of certain of Government Development Bank's loans to the public sector, see the table under "Loans to the Commonwealth, its Public Corporations and Municipalities" below.

The Ports Authority has had the benefit of letters of credit and guarantees issued for its account by Government Development Bank and has received lines of credit and loans from Government Development Bank. A portion of proceeds of the Bonds, as secured by the GDB Letter of Credit, are being used to refinance existing debt of the Ports Authority to Government Development Bank, as well as to extinguish certain letters of credit and guarantees that Government Development Bank has issued for the account of the Ports Authority. See "PLAN OF FINANCING."

Government Development Bank also lends and provides guarantees to the private sector, mainly through its subsidiaries, the Puerto Rico Tourism Development Fund and the Puerto Rico Housing Finance Authority. For a description of Government Development Bank's loans to the private sector, see "Loans to Private Enterprises" below. From time to time, Government Development Bank also issues letters of credit to guarantee obligations of private lenders with respect to financing arrangements that promote the development of the Commonwealth's economy.

Fiscal Oversight Agreements

As part of its risk management activities and as a condition to provide financing support to certain public corporations and agencies, Government Development Bank has entered into FOAs with the Highways and Transportation Authority, PRASA, the Electric Power Authority, the Ports Authority, the Puerto Rico Medical Services Administration and the Puerto Rico Health Insurance Administration and may enter into FOAs with other public corporations and agencies. The FOAs require such public corporations and agencies to implement a comprehensive expense reduction program, including certain fiscal oversight controls designed to minimize future tariff increases to households and the private sector, and to protect and improve their credit ratings. Such public corporations and agencies are also required to furnish to Government Development Bank monthly reports concerning their financial condition.

Government Development Bank has also entered into a Cooperation and Financial Reporting Agreement ("COFRA") with the University of Puerto Rico, which provides practically the same mechanism as any of the FOAs. Government Development Bank does not anticipate entering into any other COFRA.

Government Development Bank's approval of any current and future financing is expressly conditioned upon the compliance by the public corporation or agency with the covenants established in its FOA or COFRA. Each FOA or COFRA will remain in effect until the parties mutually agree that the public corporation or agency has regained a level of financial stability and is able to secure long-term financing that will result in the continued stability of its operations and financial condition.

As of November 30, 2011, all public corporations and agencies have complied with the material terms and conditions of their respective FOA or COFRA.

Board of Directors and Management

Government Development Bank is governed by a seven member Board of Directors appointed by the Governor of Puerto Rico with the approval of the Council of Secretaries. The Board of Directors consists of the following seven members serving terms as indicated:

Member	Commencement of Term	Expiration Date
Marcos Rodríguez-Ema, Chairman	January 15, 2009	September 23, 2015
Juan Carlos Batlle, Vice Chairman	March 2, 2011	September 23, 2012
Manuel H. Dubón, Esq.	February 2, 2009	September 23, 2012
Juan E. Rodríguez Díaz, Esq.	February 20, 2009	September 23, 2012
Eduardo R. Emanuelli	May 11, 2011	September 23, 2015
Jesús F. Méndez	May 18, 2011	September 23, 2014
Eugenio L. Torres	July 5, 2011	September 23, 2014

The Board of Directors appoints a President who is the chief executive officer of Government Development Bank and is responsible for its day-to-day operations. Government Development Bank also has three executive vice presidents who are in charge of its principal operational and business units. The following are Government Development Bank's principal officers:

Juan Carlos Batlle was appointed President of Government Development Bank effective as of March 2, 2011. Before entering public service, Mr. Batlle served 14 years with distinction as a top executive for Santander Group in Puerto Rico. He initially joined Santander in 1997 and soon began to move up the corporate ranks. As part of the Investment Banking Group of Santander Securities Corporation, he served consecutively as Assistant Vice President in 1999, Vice President in 2001, and Senior Vice President and Director in 2003. Then, in 2005, Mr. Batlle moved on to serve as First Senior Vice President of Banco Santander Puerto Rico and President and Chief Executive Officer of Santander Asset Management Corporation. Most recently, he went on to serve as Managing Director of Santander Securities Corporation in 2008. Prior to Santander, Mr. Batlle worked for Popular Securities. Mr. Batlle has also been a member of the Board of Directors of Santander Securities Corporation, Santander Asset Management Corporation and the First Puerto Rico Family of Funds. In addition, he has been a member of the Board of Directors of the Puerto Rico Tourism Company, the Convention Center District Authority and the Hotel Development Corporation. He holds a degree in Economics from the College of Literature, Science and the Arts of the University of Michigan.

José R. Otero-Freiría was appointed Executive Vice President of Government Development Bank and Director of Financing effective as of March 2, 2011. Throughout his professional career, Mr. Otero-Freiría has held various top positions in the financial field, including Manager of Procter & Gamble's Finance Department in San Juan, Finance Manager for Guidant Corporation (later Boston Scientific) in Santa Clara, California, and Director of Institutional Investment Consulting Services at UBS Financial Services in San Juan, Puerto Rico. Most recently, he served in the Office of the Governor as Advisor for Economic Development and Finance, and as Deputy Chief of Staff for Public Policy. Mr. Otero-Freiría earned his bachelor's degree in Economics with a major in Finance and Accounting from the Wharton School of Business at the University of Pennsylvania. He later earned his Master's in Business Administration from Stanford University. He is a Certified Public Accountant.

Rubén Méndez-Benabe, Executive Vice President, became Chief Operating Officer on July 13, 2011, after serving as General Counsel and Secretary of the Board of Directors of Government Development Bank and as Advisor to the President of Government Development Bank. He has also served as Executive Advisor and Legal Counsel to the Commissioner of Financial Institutions. Mr. Méndez-Benabe has extensive experience in regulation of financial institutions and holds a *Juris Doctor* degree from the University of Puerto Rico School of Law and a bachelor's degree from the University of Puerto Rico.

Juan M. Román Rivera was appointed Executive Vice President and Fiscal Agent of Government Development Bank effective March 16, 2011. Before being named Executive Vice President of Government Development Bank, he served as Chief Advisor to the Governor on Government Management Performance and Executive Director of the Government's Reorganization Committee of the Executive Branch. In this role, Mr. Román oversaw the Government's efforts to streamline government's agencies, and internal processes to enhance government services as well as reduce government expenditures. Before entering public service, Mr. Roman was the Commercial Director for ConAgra Foods Puerto Rico where he led several corporate reorganization efforts during his tenure from July 2004 to January 2009. Prior to ConAgra Foods, Mr. Román held several positions at Procter & Gamble Puerto Rico in sales, marketing, and operations roles. Mr. Roman has a Master's of Science in Information Networking, which is a dual degree program (MBA/MSE) from Carnegie Mellon University, and a Bachelor of Science in Electrical Engineering from the University of Pennsylvania.

Javier Ramos Luiña, Senior Vice President, has 21 years of experience in the capital markets and banking industry of which the last 15 years have been at Government Development Bank. Throughout his tenure with Government Development Bank, Mr. Ramos has also directed several of its affiliates and subsidiaries. He is the Assistant Executive Director of the Puerto Rico Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority, and for 9 years, he was also the Executive Director for the Puerto Rico Tourism Development Fund, two public corporations that assist in financing capital investments that promote economic development in Puerto Rico. Mr. Ramos obtained his Master's in Business Administration degree from Atlanta University in 1990 and Bachelor of Science degree in Business Administration from Bryant College in 1988.

Ignacio Canto is the Executive Vice President and Treasurer of Government Development Bank, where he commenced working in September 2010. Prior to his tenure as Executive Vice President and Treasurer of Government Development Bank, Mr. Canto worked at Santander Asset Management Corporation, where he began as a portfolio analyst and later on became portfolio manager. At Santander Asset Management Corporation, he garnered experience trading interest rate derivatives, agency debentures, structured products, municipal bonds, equities and equity derivatives in the context of a geared portfolio. Prior to joining Santander Asset Management Corporation, he worked at Santander Securities Corporation as part of the Investment Banking Group where he participated in financings of the Commonwealth, its agencies, corporations and instrumentalities, including Government Development Bank, the Puerto Rico Housing Finance Authority and the Puerto Rico Convention Center District Authority. In addition, Mr. Canto has performed financial analysis and valuations for corporate clients with a particular emphasis on mergers and acquisitions. Mr. Canto holds a Bachelor of Business Administration in Finance from Boston University's School of Management, as well as the Chartered Financial Analyst designation (CFA) and the Financial Risk Manager designation (FRM).

Zulema Martínez-Álvarez has been Senior Vice President, General Counsel and Secretary of the Board of Directors since July 13, 2011. Before being named General Counsel, Mrs. Martínez-Álvarez served as Legal Counsel of Government Development Bank, the Energy Affairs Administration and the Solid Waste Management Authority. She also served as an Assistant Solicitor General for the Solicitor General's Office at the Department of Justice and as a Law Clerk for the Puerto Rico Court of Appeals. Mrs. Martínez-Álvarez holds a Juris Doctor from the University of Puerto Rico School of Law, a Master's of Public Health from the University of Puerto Rico Public Health Graduate School and a bachelor's degree from the University of Puerto Rico.

As of June 30, 2011, Government Development Bank, its subsidiaries and affiliates had approximately 406 employees, 137 of which were members of the Employee Union of Government Development Bank and the Puerto Rico Housing Finance Authority (the "Housing Finance Authority").

The main offices of Government Development Bank are located at Roberto Sanchez Vilella Government Center, De Diego Avenue, P.O. Box 42001, San Juan, Puerto Rico 00940, and its telephone number is (787) 722-

2525. Government Development Bank also maintains an office at 135 West 50th Street, 22nd Floor, New York, NY, telephone (212) 422-6420.

Government Development Bank Subsidiaries.

Government Development Bank has several subsidiaries which perform various functions. The principal subsidiaries and their functions are listed below.

Housing Finance Authority. Housing Finance Authority (formerly known as Puerto Rico Housing Finance Corporation) was created in 1977 to provide needed rental housing units and stimulate the construction industry under federally subsidized programs. Effective February 8, 2002, the Housing Finance Corporation became the Housing Finance Authority and the Housing Bank and Finance Agency was dissolved and its powers transferred to the Housing Finance Authority. The Housing Finance Authority provides financing for rental housing units, stimulates the construction industry under federally subsidized programs and provides interim financing for low-income housing projects and single-family homeownership programs. It is also engaged in insuring and servicing mortgages originated by the former Housing Bank and Finance Agency. As of June 30, 2011, the Housing Finance Authority's total outstanding principal balance of loans to the private sector for development of housing projects targeted to low and moderate income families was $154.9 million. The Housing Finance Authority's mortgage loans to low and moderate income homeowners represented an additional outstanding principal balance of $147.5 million as of the same date.

The Housing Finance Authority has outstanding tax-exempt revenue bonds the proceeds of which were loaned to the Puerto Rico Public Housing Administration and to a limited liability company to finance improvements to various housing projects in the Commonwealth. Such bonds are limited obligations of the Housing Finance Authority, payable solely from revenues collected from such housing projects, with certain exceptions. As of June 30, 2011, $623.8 million of these bonds were outstanding.

As of June 30, 2011, the Housing Finance Authority had total notes and bonds outstanding of $952.2 million (including $106.8 million under loan agreements and other financings with Government Development Bank and $823.3 million in bonds issued to fund certain payments under its mortgage subsidy programs for low and moderate income families). As of June 30, 2011, the Housing Finance Authority had total unrestricted net assets of $243.8 million.

Tourism Development Fund. The Puerto Rico Tourism Development Fund (the "Tourism Development Fund") was created in September 1993 to facilitate the development of Puerto Rico's hotel and tourism industry. The Tourism Development Fund works with private sector financial institutions to structure financings for new hotel projects. The Tourism Development Fund is also authorized to make capital investments in tourism related projects. As of June 30, 2011, the Tourism Development Fund had outstanding direct loans in an aggregate outstanding amount of $432.3 million, and guarantees and letters of credit issued in the outstanding amount of $328.5 million (with a maximum commitment amount of guarantees and letters of credit of $446.4 million). In addition, the Tourism Development Fund had a $50 million preferred equity investment in a tourism-related project. Total assets as of June 30, 2011 increased to $611.3 million.

Since 1993, the Tourism Development Fund has made payments under its guarantees and letters of credit in the aggregate amount of approximately $221.3 million with respect to several projects. Of the total amount disbursed, the Tourism Development Fund has been able to recover approximately $172.3 million. As of December 1, 2011, the Tourism Development Fund has made or is going to make principal and interest payments on two tourism projects with total guarantees of approximately $50.6 million. For calendar year 2012, the Tourism Development Fund estimates that it will make approximately $2.7 million in principal and interest payments related to these two guarantees. As of June 30, 2011, the unrestricted net assets of the Tourism Development Fund were approximately $154.1 million, and its allowances for losses on loans and guarantees and letters of credit were approximately $110.5 million.

Capital Fund. Government Development Bank for Puerto Rico's Capital Fund (the "Capital Fund") was created in November 1992 for the purpose of investing and trading in debt obligations and publicly traded shares of domestic and foreign corporations separate from Government Development Bank's general investment operations. On June 30, 2010, the Capital Fund transferred to the Tourism Development Fund $72 million representing most of its investments at such date. As of June 30, 2011, the Capital Fund had total assets of approximately $243,000 consisting principally of money market investments.

Development Fund. The Puerto Rico Development Fund (the "Development Fund") was established in April 1977 to provide an alternate source of financing to private enterprises. The Development Fund is also authorized to guarantee obligations of those enterprises and invest in their equity securities. On December 31, 2010, the Development Fund acquired for $8.5 million a commercial loan from a private commercial bank, secured by a first mortgage over a 2.34 acre parcel of land in the Convention Center District. As of June 30, 2011, the Development Fund had total assets of $22.9 million, including investments of $8.1 million in loans to private entities, $11.2 million in an interest bearing account, and $3.6 million in preferred shares of various private entities.

Public Finance Corporation. The Puerto Rico Public Finance Corporation (the "Public Finance Corporation") was established in November 1984 to provide agencies and instrumentalities of the Commonwealth with alternate means of meeting their financing requirements. The trustees of certain no-commitment bonds issued by the Public Finance Corporation currently hold notes payable by the Commonwealth, the Maritime Shipping Authority, the Office for the Improvement of Public Schools, the Department of Health, and PRASA, among others. All such bonds are limited non-recourse obligations of the Public Finance Corporation payable solely from the Commonwealth's appropriations made to pay the notes held by the trustees. As of June 30, 2011, the Public Finance Corporation had $1.6 billion aggregate principal amount of no-commitment bonds outstanding.

General GDB Financial Information

The tables that follow provide financial information of Government Development Bank. Except as otherwise specified, such financial information is presented on a consolidated basis. The financial information is presented in accordance with the requirements of the Governmental Accounting Standards Board Statement No. 34 ("GASB 34"). Financial information as of and for the fiscal years ended June 30, 2011, 2010, and 2009 was derived from Government Development Bank's audited financial statements. Financial information as of September 30, 2011 was derived from Government Development Bank's accounting records. This information should be read together with Government Development Bank's financial statements as of and for the year ended June 30, 2011, attached as APPENDIX E to this Official Statement.

Government Development Bank issued and filed with the MSRB through EMMA its audited financial statements for fiscal year 2011 on December 5, 2011.

Government Development Bank's activities consist of governmental and business-type activities. Governmental activities are generally financed through taxes, intergovernmental revenues, and governmental appropriations. Business-type activities are financed in whole or in part by fees charged to third parties for goods or services. The Housing Finance Authority accounts for all of Government Development Bank's governmental activities. Except where otherwise noted, the following tables include both governmental and business-type activities.

Consolidated Schedule of Net Assets. Set forth below is the consolidated Schedule of Net Assets of Government Development Bank and its subsidiaries as of June 30, 2011, 2010 and 2009, which has been derived from Government Development Bank's audited financial statements. The consolidated Schedule of Net Assets provides information on the assets and liabilities of Government Development Bank and its subsidiaries, and includes both governmental and business-type activities.

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	As of June 30,		
	2011	2010	2009
ASSETS			
Cash and due from banks	$ 341,790,505	$ 6,121,959	$ 5,848,209
Federal funds sold	88,850,000	331,000,000	1,364,000,000
Deposits placed with banks	219,315,862	32,639,067	1,085,257,933
Investments and investment contracts	3,775,241,121	4,585,470,934	2,580,994,163
Loans receivable, net	8,360,977,041	6,949,596,082	6,677,450,043
Interest and other receivables	231,027,713	127,051,217	191,390,695
Restricted Assets:			
Cash and due from banks	5,616,995	9,206,571	20,132,629
Deposits placed with banks	521,147,529	12,263,911	27,470,438
Due from federal government	21,251,149	24,109,197	-
Due from Commonwealth	-	5,000,000	-
Investments and investment contracts	1,573,352,454	1,633,127,774	1,792,596,262
Loans receivable, net	34,981,843	16,787,580	7,953,901
Interest and other receivables	4,304,764	2,679,245	5,414,582
Real estate available for sale	1,926,940	1,339,669	1,810,718
Other assets	5,469,294	6,357,650	7,372,112
Real estate available for sale	126,641,380	206,452,231	203,396,509
Capital assets	71,049,725	15,749,737	17,452,258
Other assets	126,864,718	83,614,606	50,614,763
Total assets	15,509,809,033	14,048,567,430	14,039,155,215
LIABILITIES			
Deposits, principally from the Commonwealth of Puerto Rico and its public entities:			
Demand	3,782,554,519	3,253,713,190	3,187,494,544
Certificates of deposit	1,771,132,735	2,895,484,554	4,367,312,924
Securities sold under agreements to repurchase	970,818,550	1,058,834,752	859,053,110
Certificates of indebtedness	4,300,000	11,800,000	11,800,000
Bonds and notes payable, due within one year	91,138,136	158,614,189	72,659,611
Accrued interest payable	29,123,864	27,141,348	22,579,090
Accounts payable and accrued liabilities	58,304,402	51,442,456	48,162,048
Allowance for losses on guarantees and letters of credit	25,155,198	24,775,404	11,370,874
Participation agreement payable	26,000,000	26,000,000	26,000,000
Bonds and notes payable due in more than one year	5,391,934,330	3,203,953,441	2,004,876,929
Liabilities payable from restricted assets:			
Accrued interest payable	1,598,477	1,440,545	2,609,213
Accounts payable and accrued liabilities	89,170,767	68,957,066	15,421,420
Allowance for losses on mortgage loan insurance	3,672,007	-	-
Bonds and mortgage-backed certificates payable:			
Due in one year	68,559,063	67,605,173	64,019,136
Due in more than one year	612,204,963	654,844,231	895,114,148
Total liabilities	12,925,667,011	11,504,606,349	11,588,473,047
NET ASSETS			
Invested in capital assets	71,049,725	15,749,737	17,452,258
Restricted for:			
Debt service	-	-	29,079,599
Affordable housing programs	298,363,430	283,828,699	177,745,445
Mortgage loan insurance	61,118,599	61,898,797	58,599,573
Other housing programs	2,566,860	4,182,693	-
Unrestricted net assets	2,151,043,408	2,178,301,155	2,167,805,293
Total net assets	$ 2,584,142,022	$ 2,543,961,081	$ 2,450,682,168

Schedule of Balance Sheet Information – Government Development Bank Operating Fund. Set forth below is the Schedule of Balance Sheet Information of Government Development Bank as of June 30, 2011, 2010 and 2009, excluding its subsidiaries. The information for fiscal years 2011, 2010 and 2009 is derived from the column titled "GDB Operating Fund" included in the balance sheet for the Enterprise Funds set forth in Government Development Bank's audited financial statements.

	As of June 30,		
	2011	**2010**	**2009**
ASSETS			
Current assets:			
Cash and due from banks	$ 341,723,688	$ 5,452,348	$ 5,770,346
Federal funds sold	88,850,000	331,000,000	1,364,000,000
Deposits placed with banks	156,016,947	7,626,549	1,060,597,756
Investments and investment contracts	800,067,569	4,034,443,465	2,281,415,520
Loans receivable–net	986,320,212	563,592,459	801,029,454
Accrued interest receivable	233,855,096	128,314,302	120,307,996
Other current receivables	13,733,864	8,934,462	66,513,619
Other current assets	368,638	7,241,448	976,268
Due from governmental funds	105,612,612	100,735,356	109,840,613
Restricted:			
Deposits placed with banks	400,000,000	-	-
Investments and investment contracts	564,326,372	794,047,624	365,539,760
Total current assets	3,690,874,998	5,981,388,013	6,175,991,332
Noncurrent assets:			
Restricted:			
Investments and investment contracts	435,792,149	342,142,751	576,258,797
Investments and investment contracts	2,913,550,162	371,709,200	326,106,666
Loans receivable–net	7,211,520,610	6,239,187,440	5,675,735,320
Real estate available for sale	125,679,219	205,026,337	200,959,644
Capital assets	67,905,041	12,148,383	13,293,463
Other assets	101,684,839	56,914,482	41,734,759
Total noncurrent assets	10,856,132,020	7,227,128,593	6,834,088,649
Total assets	$ 14,547,007,018	$ 13,208,516,606	$ 13,010,079,981
LIABILITIES			
Current Liabilities:			
Deposits, principally from the Commonwealth of Puerto Rico and its public entities:			
Demand	$ 3,829,716,026	$ 3,331,074,874	$ 3,250,161,806
Certificates of deposit	2,139,888,284	3,011,667,815	4,852,867,272
Certificates of indebtedness	4,300,000	7,500,000	-
Securities sold under agreements to repurchase	970,818,550	1,058,834,752	419,053,110
Accrued interest payable	29,270,930	38,566,132	34,464,747
Accounts payable and accrued liabilities	36,874,760	32,805,812	27,869,426
Due to governmental funds	21,133,946	22,560,287	34,042,141
Notes payable	91,138,136	158,614,189	72,659,611
Total current liabilities	7,123,140,632	7,661,623,861	8,691,118,113
Noncurrent liabilities:			
Certificates of deposit, principally from the Commonwealth of Puerto Rico and its public entities	230,816,210	633,270,717	223,045,529
Certificates of indebtedness	-	4,300,000	11,800,000
Securities sold under agreements to repurchase	-	-	440,000,000
Allowance for losses on guarantees and letters of credit	-	1,000,000	1,000,000
Accounts payable and accrued liabilities	5,173,292	4,904,689	3,186,855
Bonds and notes payable	5,391,934,330	3,199,142,204	2,000,065,693
Total noncurrent liabilities	5,627,923,832	3,842,617,610	2,679,098,077
Total liabilities	12,751,064,464	11,504,241,471	11,370,216,190
NET ASSETS			
Invested in capital assets	67,905,041	12,148,383	13,293,463
Unrestricted	1,728,037,513	1,692,126,752	1,626,570,328
Total net assets	1,795,942,554	1,704,275,135	1,639,863,791
Total liabilities and net assets	$ 14,547,007,018	$ 13,208,516,606	$ 13,010,079,981

Consolidated Schedule of Revenues, Expenses and Changes in Net Assets – Enterprise Funds. Set forth below is the consolidated Schedule of Revenues, Expenses and Changes in Net Assets – Enterprise Funds for Government Development Bank and its subsidiaries for each of the fiscal years ended June 30, 2011, 2010 and 2009. Information regarding fiscal years 2011, 2010 and 2009 was derived from Government Development Bank's audited financial statements. The consolidated Schedule of Revenues, Expenses and Changes in Net Assets for the Enterprise Funds provides in more detail the information provided in the Statement of Activities (which is included in Government Development Bank's basic financial statements attached as APPENDIX E to this Official Statement) with respect to the business-type activities of Government Development Bank and its subsidiaries.

	For the year ended June 30,		
	2011	**2010**	**2009**
OPERATING REVENUES			
Investment income			
Interest income on federal funds sold	$ 1,355,702	$ 1,662,078	$ 2,902,988
Interest income on deposits placed with banks	25,268,438	26,731,021	37,059,275
Interest and dividend income on investments and investment contracts	90,704,754	83,971,825	137,025,547
Net increase (decrease) in fair value of investments	53,183,163	42,938,170	(4,260,072)
Total investment income	170,512,057	155,303,094	172,727,738
Interest income on loans receivable			
Public sector	405,528,470	331,115,998	239,211,316
Private sector	26,760,068	21,558,890	20,637,474
Total interest income on loans receivable	432,288,538	352,674,888	259,848,790
Total investment income and interest income on loans receivable	602,800,595	507,977,982	432,576,528
Noninterest income			
Fiscal agency fees	5,861,528	17,324,977	11,408,424
Commitment, guarantee and other service fees	20,922,023	15,110,856	13,579,385
Mortgage loan insurance premiums	3,774,823	3,156,393	3,000,213
Gain on sale of foreclosed real estate available for sale	-	-	483,266
Gain on sale of loans	-	-	335,030
Other income	4,454,325	1,012,304	944,142
Total noninterest income	35,012,699	36,604,530	29,750,460
Total operating revenues	637,813,294	544,582,512	462,326,988
OPERATING EXPENSES			
Provision for loan losses	42,368,229	13,340,143	46,461,481
Interest expense:			
Deposits	94,023,109	110,980,998	165,773,611
Securities sold under agreements to repurchase	15,602,648	25,000,086	30,635,161
Commercial paper	18,000	24,001	21,757
Certificates of indebtedness	20,181	27,030	240,556
Bonds and notes payable	326,359,091	228,518,310	163,907,386
Total interest expense	436,023,029	364,550,425	360,578,471
Noninterest expenses			
Salaries and fringe benefits	35,753,634	35,893,380	34,926,256
Depreciation and amortization	2,533,158	2,861,946	2,833,236
Occupancy and equipment costs	5,938,618	6,219,760	6,263,120
Legal and professional fees	8,444,110	6,263,191	6,132,182
Office and administrative	1,414,125	976,603	801,605
Subsidy and trustee fees	420,507	4,263,014	266,554
Provision for losses on guarantees and letters of credit	2,866,664	17,461,052	8,902,995
Other	12,363,240	19,686,953	6,353,101
Total noninterest expenses	69,734,056	93,625,899	66,479,049
Total operating expenses	548,125,314	471,516,467	473,519,001
OPERATING INCOME (LOSS)	89,687,980	73,066,045	(11,192,013)
NONOPERATING REVENUES (EXPENSES)			
Contributions from Commonwealth of Puerto Rico	-	49,000,000	-
Contributions to Cooperative Development Investment Fund and others	(16,254,851)	(4,344,129)	(3,458,004)
Total nonoperating revenues (expenses)	(16,254,851)	44,655,871	(3,458,004)
INCOME (LOSS) BEFORE TRANSFERS AND SPECIAL ITEM	73,433,129	117,721,916	(14,650,017)
TRANSFERS IN	1,139,032	109,358,048	8,819,402
TRANSFER OUT	(919,042)	(104,455,886)	(2,210,392)
SPECIAL ITEM			
Contributions from Puerto Rico Infrastructure Financing Authority	554,707	1,109,641	154,221,814
CHANGE IN NET ASSETS	74,207,826	123,733,719	146,180,807
NET ASSETS – Beginning of year	2,545,540,359	2,421,806,640	2,275,625,833
NET ASSETS – End of year	$ 2,619,748,185	$ 2,545,540,359	$ 2,421,806,640

Schedule of Revenues, Expenses and Changes in Net Assets – Government Development Bank Operating Fund. Set forth below is the Schedule of Revenues, Expenses and Changes in Net Assets–Government Development Bank Operating Fund for each of the fiscal years ended June 30, 2011, 2010 and 2009, excluding its subsidiaries. The Schedule of Revenues, Expenses and Changes in Net Assets for Government Development Bank's Operating Fund provides in more detail information with respect to the business-type activities of Government Development Bank as a standalone entity (excluding its subsidiaries). The information set forth in the table below for fiscal years 2011, 2010 and 2009 is derived from the column titled "GDB Operating Fund" included in the Statement of Revenues, Expenses and Changes in Net Assets – Enterprise Funds set forth in Government Development Bank's fiscal year 2011, 2010 and 2009 audited financial statements.

	For the year ended June 30,		
	2011	2010	2009
OPERATING REVENUES			
Investment income			
Interest income on federal funds sold	$ 1,355,702	$ 1,662,078	$ 2,902,988
Interest income on deposits placed with banks	351,276	933,844	9,284,246
Interest and dividend income on investments and investment contracts	45,566,123	36,873,050	85,829,640
Net increase (decrease) in fair value of investments	33,805,166	16,828,350	(938,833)
Total investment income	81,078,267	56,297,322	97,078,041
Interest income on loans receivable			
Public sector	405,528,470	326,438,248	235,481,248
Private sector	253,445	1,596	-
Total interest income on loans receivable	405,781,915	326,439,844	235,481,248
Total investment income and interest income on loans receivable	486,860,182	382,737,166	332,559,289
Noninterest income			
Fiscal agency fees	5,690,900	17,226,656	10,949,657
Commitment, guarantee and other service fees	7,860,072	5,565,924	3,707,979
Other income	532,604	725,580	303,745
Total noninterest income	14,083,576	23,518,160	14,961,381
Total operating revenues	500,943,758	406,255,326	347,520,670
OPERATING EXPENSES			
Credit for loan losses	(5,550,286)	-	-
Interest expense:			
Deposits	94,023,109	110,980,998	165,773,611
Securities sold under agreements to repurchase	15,602,648	25,000,086	30,635,161
Commercial paper	18,000	24,001	21,757
Certificates of indebtedness	20,181	27,030	240,556
Bonds and notes payable	255,033,613	151,017,060	79,528,858
Total interest expense	364,697,551	287,049,175	276,199,943
Noninterest expenses			
Salaries and fringe benefits	23,270,179	25,322,708	24,270,730
Depreciation and amortization	1,406,622	1,692,837	1,801,865
Occupancy and equipment costs	3,724,235	3,828,115	4,074,422
Legal and professional fees	3,292,270	3,459,935	2,559,363
Office and administrative	326,621	320,602	372,036
Credit for losses on guarantees and letters of credit	(1,000,000)		
Other	3,639,338	17,031,948	6,055,267
Total noninterest expenses	34,659,265	51,656,145	39,133,683
Total operating expenses	393,806,530	338,705,320	315,333,626
OPERATING INCOME	107,137,228	67,550,006	32,187,044
NONOPERATING EXPENSES - Contributions to Cooperative Development Investment Fund and others	(15,846,516)	(4,148,303)	(3,458,004)
SPECIAL ITEM - Contributions from Puerto Rico Infrastructure Financing Authority	554,707	1,109,641	154,221,814
TRANSFER OUT	(178,000)	(100,000)	(100,000)
CHANGE IN NET ASSETS	91,667,419	64,411,344	182,850,854
NET ASSETS – Beginning of year	1,704,275,135	1,639,863,791	1,457,012,937
NET ASSETS – End of year	$ 1,795,942,554	$ 1,704,275,135	$ 1,639,863,791

Capitalization. The following table sets forth the Notes, bonds and net assets of Government Development Bank (excluding its subsidiaries) as of June 30, 2011 and as adjusted to reflect the subsequent issuance by Government Development Bank of various series of its Senior Notes and the subsequent maturity or redemption of certain outstanding Senior Notes.

	June 30, 2011	As Adjusted
	(In thousands)	
Notes and Bonds		
Bonds and Notes	$ 5,483,072	$ 4,804,756
Subsequently Issued Senior Notes	-	1,295,000
Total Notes and Bonds	$ 5,483,072	$ 6,099,756*
Net Assets		
Invested in capital assets	$ 67,905	$ 67,905
Unrestricted	1,728,038	1,728,038
Total net assets	$ 1,795,943	$ 1,795,943

Subsequent to the issuance of the Bonds, Government Development Bank expects to issue additional series of its Senior Notes the proceeds of which are expected to be used for general corporate purposes, including, but not limited to, increasing Government Development Bank's investment portfolio, making loans to, and purchasing obligations of, the Commonwealth and its public corporations, instrumentalities and municipalities, and redeeming a portion of its outstanding Notes. The issuance of the Bonds is not contingent upon the issuance of these additional series of Senior Notes.

Interest Rate Spread. The following table sets forth, for each of the three fiscal years in the period ended June 30, 2011, the average interest rate earned by Government Development Bank (excluding its subsidiaries) on its interest-earning assets and the average interest rate paid by Government Development Bank (excluding its subsidiaries) for its interest-bearing liabilities and the corresponding spread.

	For the year ended June 30,		
	2011	2010	2009
Average interest rate earned	3.57%	3.13%	3.28%
Average interest rate paid	3.10	2.66	2.98
Spread	0.47%	0.47%	0.30%

Liquidity and Sources of Funding. As of June 30, 2011, approximately $5.7 billion, or 39.2%, of Government Development Bank's assets (excluding its subsidiaries) consisted of cash and due from banks, money market instruments and investment securities. At June 30, 2011, $4.5 billion, or 95.5%, of the investment securities were classified among the three highest rating categories. Based on contractual maturities, approximately $815 million, or 15%, of the investment portfolio matures in 180 days or less. Of the $5.4 billion in the investment portfolio, approximately $1.4 billion was pledged to secure or repay borrowings of Government Development Bank.

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* Amount outstanding as of December 16, 2011. Government Development Bank expects to issue up to $1,796,980,000 in additional Senior Notes during calendar year 2011.

The following table sets forth a breakdown of Government Development Bank's (excluding its subsidiaries) total funding by source.

	As of June 30,					
	2011		2010		2009	
			(amounts in millions)			
Funding Source	**Amount**	**%**	**Amount**	**%**	**Amount**	**%**
Public Funds:						
Demand Deposits	$ 3,830	30.26	$ 3,331	29.21	$ 3,250	28.84
Certificates of Deposit	2,154	17.02	3,263	28.61	4,596	40.78
Private Deposits	221	1.74	393	3.45	492	4.36
Bonds and Notes	5,483	43.31	3,358	29.47	2,073	18.40
Repurchase Agreements	971	7. 67	1,059	9.29	859	7.62
Total	$12,659	100.00	$ 11,404	100.00	$ 11,270	100.00

Special Capital and Income Contributions. Act No. 82 of June 16, 2002 ("Act No. 82") amended Government Development Bank's Charter to authorize Government Development Bank to transfer annually to the Commonwealth's General Fund, beginning with fiscal year 2001, the greater of up to 10% of its audited net income or $10 million. Government Development Bank is not required by Act No. 82 to transfer any funds. Government Development Bank made payments to the General Fund of $11.6 million for fiscal year 2003 and $18.4 million for fiscal year 2004. Government Development Bank has not made any additional payment to the General Fund under Act No. 82 since fiscal year 2004 and does not expect to make a payment during fiscal year 2012.

Investment Portfolio

General. The following tables set forth Government Development Bank's investment portfolio (excluding its subsidiaries) at June 30, 2011, 2010 and 2009 and September 30, 2011, by instrument and contractual maturity. As of June 30, 2011 the expected average life of its investment portfolio was 3.60 years and approximately 37.49% of the investment portfolio had an average life of less than one year. As of September 30, 2011 the expected average life of its investment portfolio was 3.25 years and approximately 25.12% of the investment portfolio had an average life of less than one year. At June 30, 2011, 2010 and 2009, Government Development Bank's investment portfolio (excluding its subsidiaries) was $5.4 billion $5.9 billion and $6.0 billion, respectively. At September 30, 2011, Government Development Bank's investment portfolio (excluding its subsidiaries) was $4.3 billion.

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The following table shows Government Development Bank's investment portfolio (excluding its subsidiaries) by type of instrument:

	As of June 30,					
	2011		2010		2009	
			(amounts in millions)			
Instrument	**Amount**	**%**	**Amount**	**%**	**Amount**	**%**
U.S. Government and Sponsored Agency Securities[1]	$ 3,925	73.24	$ 1,672	28.43	$ 962	16.10
Money Market[2]	762	14.22	3,677	62.53	4,574	76.56
Non-Participating Investment Contracts	198	3.69	182	3.09	170	2.85
Other[3]	474	8.85	350	5.95	268	4.49
Total	$ 5,359	100.00	$ 5,881	100.00	$ 5,974	100.00

	As of September 30, 2011	
	(amounts in millions)	
Instrument	**Amount**	**%**
U.S. Government and Sponsored Agency Securities[1]	$ 2,989	69.71
Money Market[2]	733	17.09
Non-Participating Investment Contracts	197	4.60
Other[3]	369	8.60
Total	$ 4,288	100.00

(1) Includes U.S. Treasury Bonds and Notes, U.S. agencies and collateralized obligations.

(2) Includes Federal Funds, certificates of deposit and time deposits.

(3) Includes U.S. municipal notes, asset-backed securities, corporate bonds and bonds of the Commonwealth, its municipalities and instrumentalities.

The following tables show Government Development Bank's investment portfolio (excluding its subsidiaries) by maturity:

	As of June 30,					
	2011		2010		2009	
			(amounts in millions)			
Maturity[1]	**Amount**	**%**	**Amount**	**%**	**Amount**	**%**
Less than one year	$ 2,009	37.49	$ 5,167	87.86	$ 5,072	84.90
More than one but less than 5 years	1,341	25.02	106	1.80	306	5.12
More than 5 years	2,009	37.49	608	10.34	596	9.98
Total	$ 5,359	100.00	$ 5,881	100.00	$ 5,974	100.00

	As of September 30, 2011	
	(amounts in millions)	
Maturity[1]	**Amount**	**%**
Less than one year	$1,077	25.12
More than one but less than 5 years	1,546	36.06
More than 5 years	1,665	38.82
Total	$ 4,288	100.00

(1) The information presented is based on contractual maturities. Actual or expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without penalty.

Hedging and Derivatives. Subject to certain limited exceptions, Government Development Bank's policy does not allow the use of derivatives for speculative trading purposes or for off-balance sheet leveraged transactions. Government Development Bank uses derivatives in its asset and liability management activities, which include hedging activities. Government Development Bank may take, from time to time, Eurodollars futures exposure to hedge basis risk or to reflect short-term interest rate views.

Loans to the Commonwealth, its Public Corporations and Municipalities

The table below shows, for each of Government Development Bank's public sector borrowers with outstanding principal balance greater than $20 million as of June 30, 2011 (including loans to Government Development Bank's subsidiaries and excluding municipalities), the name of the borrower, the aggregate outstanding principal amount borrowed and the source or sources of repayment:

Name of Borrower	Outstanding Principal Amount (in thousands)	Sources of Repayment
Departments and Agencies		
Department of the Treasury	$ 679,816	Legislative appropriations; Dedicated Sales Tax Fund; and proceeds of Commonwealth general obligation bonds and proceeds of other bond issues
Medical Services Administration	193,252	Legislative appropriations – General Fund
Municipal Revenues Collection Center	180,374	General Fund subsidy to the Municipalities and Operational Fund; Income from Municipalities
Emergency Fund (OMB)	117,524	Legislative appropriations – General Fund
Department of Education	113,524	Legislative appropriations; proceeds of Commonwealth general obligation bonds; and Dedicated Sales Tax Fund
Agricultural Business Development Administration	99,482	Legislative appropriations; Dedicated Sales Tax Fund and operating revenues
Department of Transportation and Public Works	80,754	Legislative appropriations; and proceeds of Commonwealth general obligation bonds
Department of Agriculture	65,439	Legislative appropriations; and proceeds of Commonwealth general obligation bonds
Department of Justice	52,976	Legislative appropriations; and proceeds of Commonwealth general obligation bonds
Puerto Rico Police Department	51,805	Legislative appropriations – General Fund
Department of Health	40,739	Legislative appropriations; proceeds of Commonwealth general obligation bonds; Dedicated Sales Tax Fund; and Fondo Especial de la Salud, Act No. 249 of November 17, 2006 (State Insurance Fund – General Fund)
Housing Department	34,414	Operating revenues and sales of properties
Puerto Rico Court Administration	21,584	Operating revenues
Public Corporations		
Highways and Transportation Authority	1,294,307	Proceeds of bond issues and operating revenues
Aqueduct and Sewer Authority	1,030,041	Proceeds of bond issues and operating revenues
Public Buildings Authority	400,315	Legislative appropriations; Dedicated Sales Tax Fund; proceeds of bond issues and operating revenues
Tourism Development Fund	399,516	Operating revenues and proceeds of bond issues
Special Communities Perpetual Fund Trust	367,902	Legislative appropriations; and proceeds of Commonwealth general obligation bonds
Port of the Americas Authority	214,525 (1)	Proceeds of bond issues
Health Insurance Administration	171,080	Legislative appropriations – General Fund
Ports Authority	155,264	Operating revenues and property sales
Convention Center District Authority	147,600	Legislative appropriations; and proceeds of Commonwealth general obligation bonds
University of Puerto Rico	93,706	Legislative appropriations; and proceeds of bond issues and proceeds of Commonwealth general obligations bonds
Industrial Development Company	88,532	Legislative appropriations; Dedicated Sales Tax Fund and operating revenues
Solid Waste Authority	68,948	Legislative appropriations; and proceeds of Commonwealth general obligation bonds
Housing Finance Authority	67,498	Legislative appropriations; proceeds of Commonwealth general obligation bonds; FEMA and operating revenues
Puerto Rico Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority	59,314	Operating revenues
Industrial Fund for Agricultural Development	41,834	Operating revenues
Cantera Development Company	20,175	Legislative appropriations; and proceeds of Commonwealth general obligation bonds
TOTAL	$ 6,352,240	

(1) The entire amount of debt is the outstanding principal amount of bonds held by Government Development Bank.

The table below shows the principal amounts owed to Government Development Bank (excluding loans to Government Development Bank's subsidiaries) from public sector loans by source of repayment:

Source of Repayment	Outstanding Principal Amount as of June 30, 2011	
	(in millions)	
Public Improvements Fund, Dedicated Sales Tax Fund, Legislative Appropriations and/or Proceeds of Commonwealth Bond Issues	$	2,736
Proceeds of Bond Issues (other than proceeds of Commonwealth general obligation bonds)		1,646
Operating Revenues of the respective borrowers (including proceeds generated through the sale of assets and/or operations)		1,621
Municipalities		1,792
Total	$	7,795

Act No. 164 of 2001, as amended ("Act No. 164"), prohibits Government Development Bank from making loans to any governmental entity for which the source of repayment consists of appropriations from the General Fund without first obtaining the approval of the Legislative Assembly, except for (i) loans up to an aggregate amount of $100 million (decreased from $200 million on June 30, 2011) as long as, among other things, Government Development Bank obtains the written approval of the Governor and the Director of OMB, (ii) loans to any financially troubled governmental entity to enable it to honor its debt obligations, and (iii) loans to the Secretary of the Treasury under legislation authorizing the Secretary to borrow funds in anticipation of tax revenues.

Loans to Departments and Agencies of the Commonwealth and Other Agencies and Instrumentalities. The Secretary of the Treasury and other agencies and instrumentalities of the Commonwealth may borrow from Government Development Bank for capital improvements and operating needs. As of June 30, 2011, the outstanding principal balance of Government Development Bank loans to the Commonwealth was $680 million and of other loans to agencies and instrumentalities of the Commonwealth was $5.7 billion, for a total of $6.4 billion.

The following are summary descriptions of some of the departments and agencies of the Commonwealth that have loans outstanding from Government Development Bank and the respective amounts of their outstanding indebtedness.

Treasury Department. The Commonwealth, through the Treasury Department, is authorized to borrow funds from Government Development Bank. As of June 30, 2011, the aggregate outstanding principal amount of all Government Development Bank loans made to the Treasury Department was $679.8 million. Additionally, Government Development Bank extended a $449.9 million and an $87.8 million financing to the Treasury Department to refinance general obligation bond interest and principal payments, respectively, for fiscal year 2012. Also, a $160 million financing was approved to OMB and the Treasury as per Joint Resolution 62 of July 2011.

Medical Services Administration. The Medical Services Administration was created by Act No. 66 of June 22, 1978 and is ascribed to the Department of Health of the Commonwealth. The Medical Services Administration plans, organizes, operates and administers the centralized health services provided in support of the member institutions of the hospital system known as the "Puerto Rico Medical Center." As of June 30, 2011, the aggregate outstanding principal amount of all Government Development Bank loans made to the Medical Services Administration was $193.3 million.

Municipal Revenues Collection Center. The Municipal Revenues Collection Center ("CRIM") is a government instrumentality of the Commonwealth that assesses, determines and collects for the benefit of the municipalities real and personal property taxes (including intangible property) in each municipality. All property taxes collected by CRIM are deposited with Government Development Bank. As of June 30, 2011, the aggregate outstanding principal amount of all Government Development Bank loans made to the CRIM was $180.4 million.

Emergency Fund. An Emergency Fund (the "Emergency Fund") was created by Act No. 91 of June 21, 1966, as amended,("Act No. 91) to cover unexpected public needs caused by calamities, such as wars, hurricanes, earthquakes, droughts, floods and plagues, and to protect people's lives and property and the public sector credit. The Emergency Fund is capitalized annually with an amount totaling no less than one percent of the General Fund net revenues of the preceding fiscal year. Act No. 91 was amended in 2003 to set an upper limit to the Emergency Fund of $150 million at the beginning of the fiscal year and was further amended in 2005 to authorize the disbursement of funds from the Emergency Fund to cover certain General Fund expenditures and operational costs of the State Emergency Management Agency. The 2005 amendment also authorizes Government Development Bank to lend to the Commonwealth up to $150 million to replenish the Emergency Fund to provide funding for emergency and disaster needs. As of December 6, 2011, the balance in the Emergency Fund was approximately $656,963, and as of June 30, 2011, Government Development Bank had an outstanding loan to the Emergency Fund of $117.5 million.

Department of Education. The Department of Education of Puerto Rico is responsible for the planning, structuring and administration of Puerto Rico's public school system, including its school facilities and curriculums. The Secretary of Education of Puerto Rico (the "Secretary of Education") is also responsible for the implementation of fiscal controls on a system-wide and individual school basis, system-wide budget planning, and the evaluation of scholastic performance and achievement. As of June 30, 2011, outstanding indebtedness to Government Development Bank was approximately $113.5 million.

Agricultural Business Development Administration. The Agricultural Business Development Administration (the "Administration") is a separate legal entity attached to the Department of Agriculture. The Administration is authorized to provide agricultural services to promote the development of farming and of agriculture in general. As of June 30, 2011, the Administration had $99.5 million of indebtedness outstanding with Government Development Bank.

Department of Transportation and Public Works. The Department of Transportation and Public Works is responsible for all public works carried out in Puerto Rico, including all roads and highways, and all public property of the Commonwealth. As of June 30, 2011, outstanding indebtedness to Government Development Bank was approximately $80.8 million.

Department of Agriculture. The Department of Agriculture is engaged in providing loans to farmers and in building and leasing commercial buildings. As of June 30, 2011, outstanding indebtedness to Government Development Bank was approximately $65.4 million.

The outstanding debt of other agencies and instrumentalities of the Commonwealth not described above is also included in the total outstanding principal balance of loans of $6.4 billion as of June 30, 2011. Such agencies include, but are not limited to the following: Department of Justice, Sports and Recreational Department, Puerto Rico Police Department, Puerto Rico Court Administration, Corrections and Rehabilitation Department and Housing Department.

Loans to Public Corporations. Government Development Bank lends funds to the public corporations of the Commonwealth for capital improvements and operating needs. The loans to public corporations for capital improvements generally are construction loans and are repaid from the proceeds of future bond issues of the respective public corporations. Such loans may, however, also be repaid from the revenues of such public corporations, from accreting certificates of deposit held by Government Development Bank, from loans provided by sources other than Government Development Bank, from federal grants, and from the sale of assets of such public corporations. The amount of outstanding loans from Government Development Bank to the public corporations fluctuates annually, depending upon the capital program needs of the public corporations, the timing and level of their capital expenditures, and their ability to gain access to the long term capital markets. As of June 30, 2011, the principal amount of loans outstanding to public corporations (including loans to Government Development Bank's subsidiaries) was approximately $4.5 billion. As of June 30, 2011, none of the outstanding loans to public corporations exceeded 10% of Government Development Bank total assets. However, as of September 2011, Highway and Transportation Authority financings surpass 10% of total assets.

The following are summary descriptions of some of the public corporations that have loans outstanding from Government Development Bank and the respective amounts of their outstanding indebtedness.

Highways and Transportation Authority. The Highways and Transportation Authority is responsible for highway construction in Puerto Rico. Such construction is financed by debt (interim notes and revenue bonds), revenues of the Highways and Transportation Authority, and federal and Puerto Rico grants.

The Highways and Transportation Authority reported a net operating loss of $523.6 million for fiscal year 2011, compared to net operating losses of $445.3 million and $493.9 million for fiscal years 2010 and 2009, respectively. As of June 30, 2011, the Highways and Transportation Authority's total debt was $7.4 billion, including $1.3 billion from Government Development Bank financings. On September 21, 2011, two additional lines of credit were approved in the aggregate amount of $471 million for the operating expenses and capital improvements program of the Highways and Transportation Authority. As of September 30, 2011, Highways and Transportation Authority's total debt was $6.7 billion, consisting of $5.1 billion of bonds and $1.6 billion of Government Development Bank financings. It is expected that the Highways and Transportation Authority will request loans to cover operational expenses for fiscal year 2012.

In July 2010, the Highways and Transportation Authority remarketed its $253,670,000 Puerto Rico Highways Revenue Funding Bonds, Series AA and its $44,275,000 Transportation Revenue Refunding Bonds, Series H, as authorized under Resolution No. 68-18 and Resolution No. 98-06, respectively, and certain supplemental resolution adopted in April 2003. These bonds were reoffered at par. Additionally during the calendar year 2010, Government Development Bank approved four lines of credit, including a revolving line, and an increase to one of the lines of credit to the Highways and Transportation Authority in the aggregate amount of $312.8 million to (i) refund existing debt, (ii) finance its capital improvement program and collateral postings on swap transactions, and (iii) pay operational expenses and settlement agreements with private contractors, which lines had an aggregate outstanding principal balance of $177.5 million as of December 31, 2010. One of these lines of credit was increased after December 2010.

The Highways and Transportation Authority's Highway Revenue Bonds are rated "A3" and "BBB+" by Moody's Investors Service (“Moody’s”) and S&P, respectively. Its Senior Transportation Revenue Bonds are rated Baa1 and BBB by Moody's and S&P, respectively.

Debt service on the Highways and Transportation Authority's revenue bonds constitutes a first lien on its gross revenues, which consist currently of all the proceeds of the tax on gasoline; one-half of the proceeds of the tax on gas oil and diesel oil; all the proceeds of the excise taxes on crude oil, unfinished oil and derivative products, up to $120 million per fiscal year; highway toll revenues; and the gross receipts of $15.00 per vehicle per year from certain motor vehicle license fees. Such revenues (except for toll revenues) may be applied first to the payment of debt service on general obligation bonds and notes of the Commonwealth and to payments required to be made by the Commonwealth under its guarantees of bonds and notes, to the extent that no other revenues are available for such purpose. The Commonwealth has never applied such revenues for such payment.

The Highways and Transportation Authority has a mass transit system, known as Tren Urbano (Urban Train), serving a portion of metropolitan San Juan. It was constructed under several design/build contracts and is being privately operated under a five-year contract with an additional five-year option at the Highways and Transportation Authority's election. The cost of the Tren Urbano was $2.4 billion, which cost was financed by federal Transit Administration grants, other federal funding sources and the Highways and Transportation Authority's own resources, including revenue bonds. Tren Urbano commenced operations in June 2005. The operation of Tren Urbano has generated losses of $51.7 million, $64.5 million and $62.5 million in fiscal years 2010, 2009, and 2008, respectively.

The Highways and Transportation Authority is a party to a concession agreement under which a private company designed, constructed and currently is operating a toll bridge spanning the San José Lagoon. The toll bridge was financed with special facility revenue bonds of the Highways and Transportation Authority, payable by the private operator of the bridge principally from toll revenues. The concession is for a term of 35 years, subject to earlier termination or extension. The bridge opened for traffic in February 1994. In certain circumstances described in the concession agreement, including where toll revenues are insufficient to generate certain rates of return to the private operator, the private operator may require the Highways and Transportation Authority, among other things, to assume the operator's obligations with respect to the special facility revenue bonds. Some of those circumstances, including low toll revenues, exist at this time, but the Highways and Transportation Authority does not currently anticipate that the operator will exercise its remedy against the Highways and Transportation Authority.

Government Development Bank has extended the terms of the financings provided to the Highways and Transportation Authority until January 2013 and will capitalize accrued interest until maturity.

As part of the government of Puerto Rico’s public-private partnership initiative, the Public-Private Partnerships Authority and the Highways and Transportation Authority (collectively, the "Owners") recently completed the procurement for a concession of toll roads PR-22 and PR-5 (the "Toll Roads"). On June 10, 2011, the Owners selected Autopistas Metropolitanas de Puerto Rico, LLC ("Metropistas"), a consortium comprised of Goldman Sachs Infrastructure Partners and Abertis Infraestructuras, as the winning proponent based on a bid of $1.080 billion. On June 27, 2011, Metropistas and the Highways and Transportation Authority executed the concession agreement for the Toll Roads (the "HTA Concession Agreement") and on September 22, 2011, the parties successfully completed the financial closing. As a result of this transaction, the Highways and Transportation Authority received a lump-sum payment of $1.136 billion and a commitment to invest $56 million in immediate improvements and to comply with world-class operating standards.

In connection with the closing of the concession of the Toll Roads, on September 22, 2011, Government Development Bank executed a payment guarantee in favor of Metropistas (the "HTA Guaranty") pursuant to which it acts as guarantor of any Termination Damages due and payable in cash by the Highways and Transportation Authority under the HTA Concession Agreement. For purposes of the HTA Concession Agreement, "Termination Damages" refers to a payment that would arise if Metropistas elects to terminate the HTA Concession Agreement as a result of: (i) an action that appropriates or sequesters all or a material part of the Toll Roads, the revenues derived therefrom and Metropistas' interest therein (or any of them) or materially impedes, substantially frustrates or renders impossible Metropistas' ability to perform its obligations for 90 consecutive days; and (ii) a material default by the Highways and Transportation Authority that is not remedied within the allowed grace periods. In both cases, the amount of Termination Damages would consist of: (a) the fair market value of Metropistas' interest in the Toll Roads, plus (b) any compensation payable under the terms of the HTA Concession Agreement for the period between the date of the occurrence of the event that gives rise to the Termination Damages and the termination date, such as loss of revenues and other documented losses; plus (c) out-of-pocket costs and expenses incurred by Metropistas as a result of the termination; less (d) insurance proceeds paid or payable to Metropistas (or which would have been payable to Metropistas but for a breach by Metropistas of the insurance policy or a requirement under the HTA Concession Agreement to maintain insurance or the insolvency of the insurer). Termination Damages covered under the HTA Guaranty also include the Highways and Transportation Authority's obligation to pay Metropistas the lesser of the fair market value of the concession or the unamortized concession fee if (i) the HTA Concession Agreement is rescinded or terminated as a result of a conviction or guilty plea by Metropistas, its subsidiaries or its executives of a crime referred to in Puerto Rico’s applicable anti-corruption statutes, to the extent such crime was not committed in connection with the procurement of the HTA Concession Agreement.

In connection with the execution of the HTA Guaranty, on September 22, 2011, Government Development Bank and the Highways and Transportation Authority entered into a Reimbursement Agreement (the "HTA Reimbursement Agreement") whereby the Highways and Transportation Authority agreed to reimburse Government Development Bank any amounts paid under the HTA Guaranty. Under the HTA Reimbursement Agreement, in order to reimburse Government Development Bank fully for any payments made under the HTA Guaranty, the Highways and Transportation Authority is required to issue bonds secured by the revenues generated by the Toll Roads (which will be returned to the Highways and Transportation Authority in the event the HTA Concession Agreement is terminated) within one year from the effective date of a termination of the HTA Concession Agreement requiring the payment of Termination Damages. On September 22, 2011, the Highways and Transportation Authority approved the bond resolution under which such bond issue would be authorized. Pending such bond issue, the reimbursement obligation will be secured by the revenues of the Toll Roads.

The Highways and Transportation Authority anticipates that future procurement processes will lead to the establishment of concession agreements for the principal toll roads in Puerto Rico.

Aqueduct and Sewer Authority. PRASA owns and operates the island's public water supply and sanitary sewer facilities systems (the "Water and Sewer Systems"). The Water and Sewer Systems provide water and wastewater services to 97% and 58% of Puerto Rico's population, respectively.

PRASA reported an operating loss of $39.6 million for fiscal year 2011, compared to operating losses of $58.3 million and $63.7 million for fiscal years 2010 and 2009, respectively. As of June 30, 2011, PRASA's total debt was $3.6 billion, including approximately $1.0 billion of outstanding indebtedness with Government Development Bank. Additionally, Government Development Bank is in the process of extending the maturity of several loans to PRASA totaling approximately $1.2 billion (including undisbursed amounts) from December 2011 to January 2013.

PRASA's senior debt is rated Baa1, "BBB-", and "BBB" by Moody's, S&P, and Fitch, respectively. On August 8, 2011, Moody's downgraded PRASA's rating and maintained its negative outlook as part of its downgrade of the Commonwealth's general obligation debt.

The Commonwealth guarantees the principal and interest payments on the outstanding Revenue Refunding Bonds, 2008 Series A and 2008 Series B, on any bonds issued on or before June 30, 2015 to the Rural Utilities Service of the United States Department of Agriculture, and on the loans granted on or before June 30, 2015 by the Puerto Rico Water Pollution Control Revolving Fund and the Puerto Rico Safe Drinking Water Revolving Fund to PRASA. In the event that PRASA is unable to make all or any portion of the future debt service payments on these guaranteed debts, the Commonwealth will be responsible for covering such payments.

During fiscal year 2011, PRASA received a $105 million assignment from the OMB in Commonwealth appropriations and other Commonwealth available funds. According to the provisions of PRASA's trust agreement, these funds are taken into account for purposes of determining its revenues and its compliance with certain covenants therein.

PRASA also pays from its net revenues, when available, the debt service on a note it issued, which is held by a trustee under certain Commonwealth Appropriation Bonds (no-commitment debt) issued by the Public Finance Corporation in the principal amount of $341.6 million, which note financed the cost of the north coast super-aqueduct. In the event PRASA is unable to make any portion of the future debt service payments on its guaranteed bonds, the Commonwealth would be required to make such payments under its guarantee from the General Fund.

PRASA needs to make a substantial investment in infrastructure and a major overhaul of its operations to maintain the viability of the Systems, to finance its expansion for new users and to implement remedial measures required by a consent decree between PRASA and the U.S. Environmental Protection Agency (the "EPA") and a settlement agreement with the Puerto Rico Department of Health. Funds for this investment will be provided through a combination of revenues from PRASA, financing transactions, federal grants and other sources. PRASA has established a 15-year capital improvement program with a total investment of $2.2 billion in order to comply with the consent decree and the settlement agreement. PRASA has committed an investment of $1.2 billion to comply with the EPA consent decree and $1.0 billion to comply with the Puerto Rico Department of Health settlement agreement.

Public Buildings Authority. The Puerto Rico Public Buildings Authority ("PBA") is authorized to construct, purchase or lease office, school, health, correctional and other facilities for lease to departments, public corporations and instrumentalities of the Commonwealth. Bonds that have been issued by PBA to finance such facilities (through retirement of interim notes or otherwise) are payable from lease payments, which are largely derived from legislative appropriations and are secured by the Commonwealth's guaranty. PBA is authorized by law to have outstanding at any one time up to $4.325 billion of bonds guaranteed by the Commonwealth. As of

June 30, 2011, $3.1 billion aggregate principal amount of such bonds were outstanding (not including accretion of interest from the respective issuance dates on capital appreciation bonds). As of June 30, 2011, PBA's line of credit with Government Development Bank had an outstanding balance of $400.3 million. A portion of this line of credit was refinanced with the proceeds of PBA's $303,945,000 Government Facilities Revenue Bonds, Series S, issued on August 24, 2011.

PBA debt is rated Baa1, "BBB" and "BBB+" by Moody's, S&P and Fitch, respectively.

Special Communities Perpetual Trust. The Special Communities Perpetual Trust (the "Trust"), a public corporation, is an irrevocable and permanent trust. The Trust's principal purpose is to fund development projects which address the infrastructure and housing needs of underprivileged communities. Government Development Bank made a special capital contribution to the Trust of $500 million and provided it with a $500 million non-revolving line of credit. The amounts transferred by Government Development Bank were deposited in two investment accounts held by Government Development Bank for the benefit of the Trust, of which $918.7 million had been disbursed to the Trust as of June 30, 2011. As of June 30, 2011, the Trust's line of credit with Government Development Bank had an outstanding balance of $367.9 million. The line of credit is payable from legislative appropriations.

Electric Power Authority. The Puerto Rico Electric Power Authority (the "Electric Power Authority") owns and operates Puerto Rico's electric power system. The Electric Power Authority reported net operating income of $328.9 million and $359.5 million during fiscal years 2011 and 2010 respectively. The total debt of the Electric Power Authority was $8.0 billion as of June 30, 2011. The Electric Power Authority's debt is rated "A3", "BBB+" and "A-" by Moody's, S&P and Fitch, respectively. As of June 30, 2011, loans to the Electric Power Authority did not exceed $20 million. However, in October 2011, Government Development Bank extended a financing of up to $244 million to the Electric Power Authority to partially cover the payment of principal and interest on its outstanding bonds during fiscal year 2012.

Port of the Americas Authority. The Port of the Americas Authority is responsible for the development and operation of the Port of the Americas, a deep draft port on the south coast of Puerto Rico. The Port of the Americas Authority is authorized to issue bonds guaranteed by the Commonwealth in a maximum aggregate principal amount of $250 million. The proceeds from these bonds will be used to continue the development of the Port of the Americas. Currently, Government Development Bank is authorized to purchase bonds of the Port of the Americas Authority in an aggregate principal amount not to exceed $250 million. As of June 30, 2011, Government Development Bank held approximately $214.5 million of the Port of the Americas Authority's outstanding bonds, which are guaranteed by the Commonwealth.

The first phase of the Port of the Americas was completed in fiscal year 2004. This initial phase included the improvement of piers 4, 5 and 6 of the Port of the Americas and the acquisition of heavy equipment at a cost of $40 million. The second phase of the Port of the Americas was completed during the first quarter of calendar year 2009. This phase, which was designed to provide capacity to handle up to 250,000 Twenty-Foot Equivalent Units ("TEU") per year, included (i) dredging the entrance channel and adjacent areas of the Port of the Americas to a depth of 50 feet, (ii) reconstructing the container terminals, (iii) commencing certain required environmental risk mitigation procedures, and (iv) preparing final construction schematics.

A third phase, which provides for the expansion of the Port of the Americas' capacity, was initiated in August 2008. This phase includes, among other improvements, (i) infrastructure improvements related to access roads; (ii) relocation of the storm sewer channel; (iii) relocation of the sewer, water and power distribution systems; (iv) additional dredging at certain pier locations; (v) the expansion of the container terminal; and (vi) additional mitigation at Coffin Island. The first expansion under this phase will provide sufficient capacity to process 500,000 TEU annually. This phase is expected to be finished in 2012.

Health Insurance Administration. The Health Insurance Administration was created in 1993 to negotiate and contract for the provision of comprehensive health insurance coverage for qualifying (generally low income) Puerto Rico residents. Under this system, the Government selected, through a bidding system, one private health insurance company in each of eight designated regions of the Island and paid such insurance company the insurance premium for each eligible beneficiary within such region. The health insurance system covers the entire Island. Approximately 1.5 million persons were covered by the system during fiscal year 2011.

The total cost of the health insurance program was $2.013 billion for fiscal year 2011, $1.962 billion for fiscal year 2010 and $1.861 billion for fiscal year 2009. During fiscal year 2011, the General Fund covered $1.225 billion of the total cost of the health insurance program and $75 million was covered from proceeds of the Puerto Rico Sales Tax Financing Corporation bonds. The remaining $713 million was paid from federal, municipal, internal and other sources. On March 14, 2011, the Health Insurance Administration borrowed approximately $186 million from Government Development Bank in order to pay amounts owed to its suppliers, including premiums owed to certain insurance companies for services rendered under this program. As of June 30, 2011, the Health Insurance Administration had outstanding indebtedness to Government Development Bank of approximately $171.1 million. On November 29, 2011, Government Development Bank granted a $250 million revolving line of credit to the Health Insurance Administration.

Ports Authority. The Ports Authority owns and operates the major airport and seaport facilities in Puerto Rico. The Ports Authority derives revenues from a variety of sources, including charges on airplane fuel sales, air terminal space rentals, landing fees, wharfage, dockage and harbor fees, and rentals for the lease of property and seaport equipment. Ports Authority reported operating losses of $38.7 million and $46.7 million during fiscal years 2010 and 2009, respectively. As of June 30, 2011, the Ports Authority had $737.8 million in debt, including approximately $155.3 million in loans outstanding from Government Development Bank. As of December 1, 2011, the Ports Authority's total maximum indebtedness (excluding the Series E Bonds described below) was approximately $775.1 million, of which approximately $67.3 million remained to be disbursed. Of the total amount of indebtedness, approximately $506.5 million is secured by letters of credit issued by Government Development Bank, and approximately $267 million represents direct loans from Government Development Bank. In addition in June 2010, the Ports Authority issued its $46,326,069 Revenue Refunding Bonds, Series E (the "Series E Bonds") to refund, together with other available monies, the $55,580,000 outstanding amount of its Revenue Bonds Series D. The Series E Bonds have a final maturity of June 15, 2028 and were purchased by Government Development Bank. Government Development Bank also has guaranteed the obligations of the Ports Authority under an interest swap agreement, with a notional amount outstanding as of December 1, 2011 of approximately $390 million (the "Guaranteed Swap").

The Series E Bonds are expected to remain outstanding after the issuance of the Bonds. However, approximately $535.4 million of the Ports Authority's other indebtedness, which indebtedness is secured by Government Development Bank, is expected to be repaid with the proceeds of the Bonds. Also, the Guaranteed Swap is expected to be terminated upon the issuance of the Bonds; if terminated, the termination fee will be paid with the proceeds of the Bonds. See "PLAN OF FINANCING."

Convention Center District Authority. The Convention Center District Authority was created to own, develop, finance, plan, design, build, operate, maintain, administrate and promote a new convention center (the "Convention Center") and designated private parcels located within the Convention Center District in San Juan. The Convention Center opened on November 17, 2005.

The Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority ("AFICA") financed the construction of a multi-purpose coliseum in San Juan, known as the Jose Miguel Agrelot Coliseum, with a line of credit provided by Government Development Bank. The Coliseum was transferred to the Convention Center District Authority along with the associated line of credit. The Convention Center District Authority's debt as of June 30, 2011 was $447.2 million in outstanding bonds issued in March 2006 to finance the Convention Center and payable from a portion of the Hotel Room Tax. In addition, as of June 30, 2011, its outstanding indebtedness to Government Development Bank was approximately $147.6 million from the financing for the Coliseum.

University of Puerto Rico. The University of Puerto Rico (the "University"), with approximately 62,342 students in the first semester of the academic year 2010-2011, is by far the largest institution of higher education on the Island. Government appropriations are the principal source of University revenues, but additional revenues are derived from tuition, student fees, auxiliary enterprises, interest income, federal grants and other sources.

University capital improvements have been financed mainly by revenue bonds. As of June 30, 2011, the University's total debt was $626 million, including $93.7 million from Government Development Bank financing. In addition, the loans to the University's Medical Services Hospital in Carolina, Puerto Rico, had an outstanding principal balance of $18.9 million as of June 30, 2011. The University's debt is rated "Baa3" and "BBB-" by Moody's S&P, respectively. It is expected that the University will request additional loans to cover operational expenses for fiscal year 2012.

In 2000, AFICA issued its $86,735,000 Educational Facilities Revenues Bonds, 2000 Series A (University Plaza Project) for the purpose of financing the construction of additional student housing and parking and office space for the University. The project was built, is being operated by Desarrollos Universitarios, Inc., a Puerto Rico not-for-profit corporation, and is leased to the University for a term equal to the term of the bonds with University lease payments being sufficient to pay debt service on said bonds as they become due. These bonds are not included in the University's total debt or outstanding revenue bonds set forth in the prior paragraph.

In June 2007, the Board of Trustees of the University approved Certification No. 60 establishing a new policy and methodology for tuition fees structure. This new structure covers the tuition fees to be charged to new students until academic year 2012-2013. This policy was adopted to pursue continued development and financial stability of the University.

In June 2010, the Board of Trustees of the University approved Certification No. 146 establishing a $400 stabilization fee to be charged each semester to all students in addition to tuition charges and other fees already in place at the University. This stabilization fee was imposed to address the University's fiscal difficulties and is expected to increase annual revenues by approximately $40 million.

On June 26, 2010, the Middle States Commission on Higher Education (the "Commission"), the regional accreditation entity of the eleven units that comprise the University system, placed on probation ten of the University's units for lack of evidence of compliance with two of fourteen accreditation standards. This action was prompted by a student stoppage that interrupted the operations of these units for up to 62 days, but less in most cases. After a Monitoring Report submitted by the ten affected units in September 2010 and a subsequent evaluation visit, the Commission lifted probation over one of the questioned standards and added an additional standard, thereby continuing the review over two of the fourteen accreditation standards.

A second Monitoring Report was submitted to the Commission by the ten affected units on March 1, 2011 to further substantiate compliance with these two standards. Evaluation visits to the eleven units of the University were conducted between March and April 2011 as a follow up to the probationary process as well as the regular decennial re-accreditation review for some of the units. Following these visits, the evaluation teams reported that they intend to inform the Commission that 95% of all accreditation standards evaluated throughout the system were found in compliance, and significant progress was evidenced in the remaining 5%. On June 23, 2011, the Commission lifted the probation and reaffirmed the accreditation of seven units, but maintained the probation on three units.

Evaluation visits to the three units of the University on probation were conducted in September 2011. Following these visits, the evaluation teams reported that they intend to inform the Commission that these units are in full compliance with the standards under review. On November 17, 2011, the Commission lifted the probation and reaffirmed the accreditation for the three remaining units. All of the affected units remained accredited while on probation.

Industrial Development Company. The Puerto Rico Industrial Development Company ("PRIDCO") participates in the government-sponsored economic development program by providing physical facilities, general assistance, and special incentive grants to manufacturers. PRIDCO was merged with the Puerto Rico Economic Development Administration in January 1998. PRIDCO reported consolidated change in net assets of $8.4 million for fiscal year 2011, compared to consolidated change in net assets of $10.3 million for fiscal year 2010, and consolidated change in net assets of $6.0 million for fiscal year 2009. Rentals derived from the leasing of specified facilities of PRIDCO are pledged to the payment of PRIDCO's revenue bonds. As of June 30, 2011, PRIDCO's total debt was $423.1 million, including approximately $88.5 million from Government Development Bank financings and the outstanding debt of Industrial Investment Corporation, a subsidiary of PRIDCO.

The outstanding debt of other public corporations and instrumentalities not described above is also included in the total principal amount of loans of $4.5 billion. Such corporations and instrumentalities include, but are not limited to the following: Infrastructure Finance Authority, Industrial Fund for Agricultural Development, Public Private Partnership Authority, Cancer Center, National Parks Company, Economic Development Bank, Solid Waste Authority and Tourism Development Fund.

Loans to Municipalities. Government Development Bank also purchases general obligation and other bonds and notes of the municipalities of Puerto Rico, which obligations are issued by said municipalities to finance their public works projects and operational needs. The bonds and notes relating to public works projects are generally sold by Government Development Bank to the Puerto Rico Municipal Finance Agency, which issues its bonds to acquire such bonds and notes. As of June 30, 2011, approximately $1.8 billion aggregate outstanding principal amount of bonds and notes issued by the municipalities were held by Government Development Bank.

Financial Instruments with Off-Balance-Sheet Risk. In the normal course of business, Government Development Bank is party to transactions involving financial instruments with off-balance-sheet risk to meet the financing needs of its customers. These financial instruments include commitments to extend credit, letters of credit, and financial guarantees and involve, to varying degrees, elements of credit risk in excess of amounts recognized in Government Development Bank's statement of net assets and fund balance sheets. These off-balance sheet risks are managed and monitored in a manner similar to those used for on-balance-sheet risks. Government Development Bank's exposures to credit loss for lending commitments, financial guarantees, and letters of credit are represented by the contractual amount of those transactions. As of June 30, 2011, the total consolidated balance of outstanding letters of credit and financial guarantees of Government Development Bank was $1.1 billion.

Loans to Private Enterprises

Government Development Bank's loans to the private sector (excluding the lending activities of its subsidiaries, the Housing Finance Authority, the Tourism Development Fund and the Development Fund) are done solely for strategic commercial and industrial ventures. Government Development Bank also provides working capital loans to the private sector. As of June 30, 2011, Government Development Bank had approximately $5 million of outstanding loans to the private sector.

LITIGATION

As of the date hereof, to the knowledge of the officers of the Financing Authority, there is no litigation of any nature pending or threatened against the Financing Authority to restrain or enjoin the issuance, sale, execution or delivery of the Bonds or the application of the proceeds thereof as described in this Official Statement, or in any way contesting or affecting the validity of the Bonds or any proceedings of the Financing Authority taken with respect to the issuance or sale thereof, or the pledge or application of any monies or security for the Bonds or the existence or powers of the Financing Authority.

As of the date hereof, there is no litigation pending or threatened against the Ports Authority, wherein an unfavorable decision would adversely affect the ability of the Ports Authority to enter into the Loan and Trust Agreement or the Reimbursement Agreement or to fulfill the Ports Authority's obligations thereunder.

As of the date hereof, there is no litigation pending or threatened against Government Development Bank, wherein an unfavorable decision would adversely affect the ability of Government Development Bank to enter into the Reimbursement Agreement or to issue the GDB Letter of Credit in favor of the Trustee, or to fulfill Government Development Bank's obligations thereunder, or that would otherwise have a material adverse effect on Government Development Bank's financial condition.

TAX MATTERS

Series 2011B Bonds and Series 2011C Bonds -- Tax Exempt Bonds

The U.S. Internal Revenue Code of 1986, as amended (the "Code"), includes requirements which the Financing Authority and the Ports Authority must continue to meet after the issuance of the Series 2011B Bonds and Series 2011C Bonds (collectively, the "Tax-Exempt Bonds") in order that interest on the Tax-Exempt Bonds not be included in gross income for federal income tax purposes. The failure to meet these requirements may cause interest on the Tax-Exempt Bonds to be included in gross income for federal income tax purposes retroactive to their date of issuance. The Financing Authority and the Ports Authority have covenanted to comply, to the extent permitted by the Constitution and the laws of the Commonwealth, with the requirements of the Code in order to maintain the exclusion from gross income for federal income tax purposes of interest on the Tax-Exempt Bonds. Bond Counsel is not aware of any provision of the Constitution or laws of the Commonwealth which would prevent the Financing Authority and the Ports Authority from complying with the requirements of the Code.

In the opinion of Bond Counsel, subject to continuing compliance by the Financing Authority and the Ports Authority with the tax covenant referred to above, under the provisions of the Acts of Congress now in force and under existing regulations, rulings and court decisions, interest on the Tax-Exempt Bonds will not be included in gross income for federal income tax purposes, except interest on a Series 2011C Bond for any period during which that Bond is held by a "substantial user" or a "related person" as those terms are used in Section 147(a) of the Code. Interest on the Series 2011B Bonds will not be an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations; however, such interest will be taken into account in determining adjusted current earnings for purposes of computing the alternative minimum tax imposed on certain corporations. Interest on the Series 2011C Bonds will be an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations. Bond Counsel is further of the opinion that the Tax-Exempt Bonds and the interest thereon are exempt from state, Commonwealth, and local income taxation.

Ownership of tax-exempt obligations such as the Tax-Exempt Bonds may result in collateral federal income tax consequences to certain taxpayers, including, without limitation, financial institutions, property and casualty insurance companies, certain foreign corporations, certain S Corporations with excess passive income, individual recipients of Social Security or Railroad Retirement benefits, taxpayers who may be deemed to have incurred or continued indebtedness to purchase or carry tax-exempt obligations, and taxpayers who may be eligible for the earned income tax credit.

Ownership of the Tax-Exempt Bonds may also result in collateral income tax consequences under Puerto Rico law.

Prospective purchasers of the Tax-Exempt Bonds should consult their tax advisors as to their specific taxation circumstances and the applicability and impact of any collateral consequences.

Legislation affecting municipal securities is constantly being considered by the United States Congress. There can be no assurance that legislation enacted after the date of issuance of the Bonds will not have an adverse effect on the tax-exempt status of the Tax-Exempt Bonds. Legislative or regulatory actions and proposals may also affect the economic value of tax exemption or the market price of the Tax-Exempt Bonds.

Tax-Exempt Discount Bonds

Certain of the Tax-Exempt Bonds as indicated on the inside cover of this Official Statement ("Tax-Exempt Discount Bonds") were offered and sold to the public at an original issue discount ("OID"). OID is the excess of the stated redemption price at maturity (the principal amount) over the "issue price" of a Tax-Exempt Discount Bond. The issue price of a Tax-Exempt Discount Bond is the initial offering price to the public (other than to bond houses, brokers or similar persons acting in the capacity of underwriters or wholesalers) at which a substantial amount of the Tax-Exempt Discount Bonds of the same maturity is sold pursuant to that offering. For federal income tax purposes, OID accrues to the owner of a Tax-Exempt Discount Bond over the period to maturity based on the constant yield method, compounded semiannually (or over a shorter permitted compounding interval selected by the owner). The portion of OID that accrues during the period of ownership of a Tax-Exempt Discount Bond (i) is interest excludable from the owner's gross income for federal income tax purposes to the same extent, and subject to the same considerations discussed above, as other interest on the Tax-Exempt Bonds, and (ii) is added to the owner's tax basis for purposes of determining gain or loss on the maturity, redemption, prior sale or other disposition of that Tax-Exempt Discount Bond. A purchaser of a Tax-Exempt Discount Bond in the initial public offering at the price for that Tax-Exempt Discount Bond stated on the inside cover of this Official Statement who holds that Tax-Exempt Discount Bond to maturity will realize no gain or loss upon the retirement of that Tax-Exempt Discount Bond.

Tax-Exempt Premium Bonds

Certain of the Tax-Exempt Bonds as indicated on the inside cover of this Official Statement ("Tax-Exempt Premium Bonds") were offered and sold to the public at a price in excess of their stated redemption price (the principal amount) at maturity. That excess constitutes bond premium. For federal income tax purposes, bond premium is amortized over the period to maturity of a Tax-Exempt Premium Bond, based on the yield to maturity of that Tax-Exempt Premium Bond (or, in the case of a Tax-Exempt Premium Bond callable prior to its stated maturity, the amortization period and yield may be required to be determined on the basis of an earlier call date that results in the lowest yield on that Tax-Exempt Premium Bond), compounded semiannually (or over a shorter permitted compounding interval selected by the owner). No portion of that bond premium is deductible by the owner of a Tax-Exempt Premium Bond. For purposes of determining the owner's gain or loss on the sale, redemption (including redemption at maturity) or other disposition of a Tax-Exempt Premium Bond, the owner's tax basis in the Tax-Exempt Premium Bond is reduced by the amount of bond premium that accrues during the period of ownership. As a result, an owner may realize taxable gain for federal income tax purposes from the sale or other disposition of a Tax-Exempt Premium Bond for an amount equal to or less than the amount paid by the owner for that Tax-Exempt Premium Bond. A purchaser of a Tax-Exempt Premium Bond in the initial public offering at the price for that Tax-Exempt Premium Bond stated on the inside cover of this Official Statement who holds that Tax-Exempt Premium Bond to maturity (or, in the case of a callable Tax-Exempt Premium Bond, to its earlier call date that results in the lowest yield on that Tax-Exempt Premium Bond) will realize no gain or loss upon the retirement of that Tax-Exempt Premium Bond.

Owners of Tax-Exempt Discount and Premium Bonds should consult their own tax advisers as to the determination for federal income tax purposes of the amount of OID or bond premium properly accruable in any period with respect to the Tax-Exempt Discount or Premium Bonds and as to other federal tax consequences and the treatment of OID and bond premium for purposes of Commonwealth, state and local taxes on, or based on, income.

Information Reporting and Backup Withholding

Interest paid on tax-exempt bonds such as the Tax-Exempt Bonds is subject to information reporting to the Internal Revenue Service in a manner similar to interest paid on taxable obligations. This reporting requirement does not affect the excludability of interest on the Tax-Exempt Bonds from gross income for federal income tax purposes. However, in conjunction with that information reporting requirement, the Code subjects certain non-corporate owners of Tax-Exempt Bonds, under certain circumstances, to "backup withholding" at (i) the fourth lowest rate of tax applicable under Section 1(c) of the Code (i.e., a rate applicable to unmarried individuals) for taxable years beginning on or before December 31, 2012; and (ii) the rate of 31% for taxable years beginning after December 31, 2012, with respect to payments on the Tax-Exempt Bonds and proceeds from the sale of Tax-Exempt Bonds. Any amount so withheld would be refunded or allowed as a credit against the federal income tax of such owner of Tax-Exempt Bonds. This withholding generally applies if the owner of Tax-Exempt Bonds (i) fails to furnish the payor such owner's social security number or other taxpayer identification number ("TIN"), (ii) furnished the payor an incorrect TIN, (iii) fails to properly report interest, dividends, or other "reportable payments" as defined in the Code, or (iv) under certain circumstances, fails to provide the payor or such owner's securities broker with a certified statement, signed under penalty of perjury, that the TIN provided is correct and that such owner is not subject to backup withholding. Prospective purchasers of the Tax-Exempt Bonds may also wish to consult with their tax advisors with respect to the need to furnish certain taxpayer information in order to avoid backup withholding.

Series 2011A Bonds – Taxable Bonds

Generally, Bond Counsel expresses no opinion with respect to the Series 2011A Bonds (the "Taxable Bonds") under federal income tax law other than that the interest on the Taxable Bonds is not excludable from gross income for federal income tax purposes. Bond Counsel is further of the opinion that the Taxable Bonds and the interest thereon are exempt from state, Commonwealth and local income taxation.

The following is a summary of certain anticipated United States federal income tax consequences of the purchase, ownership and disposition of the Taxable Bonds. The summary is based upon provisions of the Code, the regulations promulgated thereunder and rulings and court decisions now in effect, all of which are subject to change. This summary is intended as a general explanatory discussion of the consequences of holding the Taxable Bonds. This summary generally addresses Taxable Bonds held as capital assets and does not purport to address all aspects of federal income taxation that may affect particular investors in light of their individual circumstances or certain types of investors subject to special treatment under the federal income tax laws, including but not limited to financial institutions, insurance companies, dealers in securities or currencies, persons holding such Taxable Bonds as a hedge against currency risks or as a position in a straddle for tax purposes, foreign investors or persons whose functional currency is not the U.S. dollar. Potential purchasers of the Taxable Bonds should consult their own tax advisors in determining the federal, state or local tax consequences to them of the purchase, holding and disposition of the Taxable Bonds.

Interest on the Taxable Bonds is not excluded from gross income for federal income tax purposes. Purchasers other than those who purchase the Taxable Bonds in the initial offering at their principal amounts will be subject to federal income tax accounting rules affecting the timing and/or characterization of payments received with respect to such Bonds. Generally, interest paid on the Taxable Bonds and recovery of accrued original issue and market discount, if any, will be treated as ordinary income to the Bondowner, and, after adjustment for the foregoing, principal payments will be treated as a return of capital.

Taxable Discount Bonds

The following summary is a general discussion of certain federal income tax consequences of the purchase, ownership and disposition of Taxable Bonds issued with original issue discount ("Taxable Discount Bonds"). A Taxable Bond will be treated as having been issued at an original issue discount if the excess of its "stated redemption price at maturity" (defined below) over its issue price (defined as the initial offering price to the public at which a substantial amount of the Taxable Bonds of the same maturity have first been sold to the public, excluding bond houses and brokers) equals or exceeds one quarter of one percent of such Taxable Bond's stated redemption price at maturity multiplied by the number of complete years to its maturity.

Generally, a Taxable Discount Bond's "stated redemption price at maturity" is the total of all payments provided by the Taxable Discount Bond that are not payments of "qualified stated interest." Generally, "qualified stated interest" includes stated interest that is unconditionally payable in cash or property (other than debt instruments of the issuer) at least annually at a single fixed rate.

In general, the amount of original issue discount includible in income by the initial holder of a Taxable Discount Bond is the sum of the "daily portions" of original issue discount with respect to such Taxable Discount Bond for each day during the taxable year in which such holder held such Taxable Discount Bond. The daily portion of original issue discount is determined by allocating to each day in any accrual period a ratable portion of the original issue discount allocable to that accrual period.

An accrual period may be of any length, and may vary in length over the term of a Taxable Discount Bond, provided that each accrual period is not longer than one year and each scheduled payment of principal or interest occurs at the end of an accrual period. The amount of original issue discount allocable to each accrual period is equal to the difference between (i) the product of the Taxable Discount Bond's adjusted issue price at the beginning of such accrual period and its yield to maturity (determined on the basis of compounding at the close of each accrual period and appropriately adjusted to take into account the length of the particular accrual period) and (ii) the amount of any qualified stated interest payments allocable to such accrual period. The "adjusted issue price" of a Taxable Discount Bond at the beginning of any accrual period is the sum of the issue price of the Taxable Discount Bond plus the amount of original issue discount allocable to all prior accrual periods minus the amount of any prior payments on the Taxable Discount Bond that were not qualified stated interest payments. Under these rules, owners will have to include in income increasingly greater amounts of original issue discount in successive accrual periods.

Certain owners may elect to include all interest (including stated interest, acquisition discount, original issue discount, *de minimis* original issue discount, market discount, *de minimis* market discount, and unstated interest, as adjusted by any amortizable bond premium or acquisition premium) on the Taxable Discount Bond by using the constant yield method applicable to original issue discount, subject to certain limitations and exceptions. Such owners should consult their own tax advisors with respect to whether or not they should so elect.

Owners of Taxable Discount Bonds should consult their own tax advisors as to the determination for federal income tax purposes of the amount of original issue discount properly accruable in any period and as to other federal tax consequences and the treatment of original issue discount for purposes of Commonwealth, state and local taxes on, or based on, income.

Market Discount

If a Bondowner purchases a Taxable Bond for an amount that is less than the adjusted issue price of the Taxable Bond, and such difference is not considered to be *de minimis*, then such discount will represent market discount. Absent an election to accrue market discount currently, upon a sale, exchange or other disposition of a Taxable Bond, a portion of any gain will be ordinary income to the extent it represents the amount of any such market discount that was accrued through the date of sale. In addition, absent an election to accrue market discount currently, the portion of any interest expense incurred to carry a market discount bond is limited. Such Bondowners should consult their own tax advisors with respect to whether or not they should elect to accrue market discount currently, the determination and treatment of market discount for federal income tax purposes and the Commonwealth, state and local tax consequences of owning such Taxable Bonds.

Bond Premium

If a Bondowner purchases a Taxable Bond at a cost greater than its then principal amount, generally the excess is amortizable bond premium. The tax accounting treatment of bond premium is complex. Such Bondowners should consult their own tax advisors with respect to whether or not they should elect to amortize such premium under Section 171 of the Code, the determination and treatment of such premium for federal income tax purposes and the Commonwealth, state and local tax consequences of owning such Taxable Bonds.

Sale or Redemption of Taxable Bonds

A Bondowner's tax basis for a Taxable Bond is the price such owner pays for the Taxable Bond plus the amount of any original issue discount and market discount previously included in income, reduced on account of any payments received (other than "qualified periodic interest" payments) and any amortized bond premium. Gain or loss recognized on a sale, exchange or redemption of a Taxable Bond, measured by the difference between the amount realized and the Taxable Bond basis as so adjusted, will generally give rise to capital gain or loss if the Taxable Bond is held as a capital asset (except as discussed above under "Market Discount"). The legal defeasance of Taxable Bonds may result in a deemed sale or exchange of such Bonds under certain circumstances; owners of such Taxable Bonds should consult their tax advisors as to the federal income tax consequences of such an event.

Information Reporting and Backup Withholding

Interest paid on bonds such as the Taxable Bonds is subject to information reporting to the Internal Revenue Service. In conjunction with the information reporting requirement, the Code subjects certain non-corporate owners of Taxable Bonds, under certain circumstances, to "backup withholding" at (i) the fourth lowest rate of tax applicable under Section 1(c) of the Code (i.e., a rate applicable to unmarried individuals) for taxable years beginning on or before December 31, 2012; and (ii) the rate of 31% for taxable years beginning after December 31, 2012, with respect to payments on the Taxable Bonds and proceeds from the sale of Taxable Bonds. This withholding generally applies if the owner of Taxable Bonds (i) fails to furnish the payor such owner's social security number or other taxpayer identification number ("TIN"), (ii) furnished the payor an incorrect TIN, (iii) fails to properly report interest, dividends, or other "reportable payments" as defined in the Code, or (iv) under certain circumstances, fails to provide the payor or such owner's securities broker with a certified statement, signed under penalty of perjury, that the TIN provided is correct and that such owner is not subject to backup withholding. Backup withholding will not apply, however, with respect to certain payments made to Bondowners, including payments to certain exempt recipients and to certain Nonresidents (defined below). Prospective purchasers of the Taxable Bonds may also wish to consult with their tax advisors as to their qualification for an exemption from backup withholding and the procedure for obtaining the exemption.

Nonresidents

Under the Code, interest and original issue discount income with respect to Taxable Bonds held by nonresident alien individuals, foreign corporations and other non-United States persons ("Nonresidents") may not be subject to withholding. Generally, payments on the Taxable Bonds to a Nonresident that has no connection with the United States other than holding the Taxable Bond will be made free of withholding tax, as long as such holder has complied with certain tax identification and certification requirements. Nonresidents should consult their own tax advisors in determining the federal, Commonwealth, state or local tax consequences to them of the purchase, holding and disposition of the Taxable Bonds.

Circular 230 Disclosure. The above discussion was written to support the promotion and marketing of the Taxable Bonds and was not intended or written to be used, and cannot be used, by a taxpayer for purposes of avoiding United States federal income tax penalties that may be imposed. Each taxpayer should seek advice based on the taxpayer's particular circumstances from an independent tax advisor.

Puerto Rico Income and Other Tax Considerations and certain United States Federal Income Tax Considerations related to the Series 2011A Bonds for Puerto Rico Investors.

The following is a summary of the opinion of Ferraiuoli LLC, Special Puerto Rico Tax Counsel, regarding certain Puerto Rico income and other and United States federal income tax consequences of the ownership of the Series 2011A Bonds by Puerto Rico residents.

This section does not purport to cover all of the Puerto Rico income and other and United States federal income tax consequences arising from the purchase and ownership of the Series 2011A Bonds. The following is based upon laws, regulations, judicial decisions and administrative pronouncements now in effect and subject to change, and any change may apply retroactively and affect the accuracy of the opinions, statements and conclusions set forth in this discussion. You should consult your independent tax advisor as to the application to your particular situation of the tax discussion described below, as well as the effect of any foreign, state or other laws.

Puerto Rico Tax Considerations

In the opinion of Ferraiuoli LLC, based on the laws of Puerto Rico now in force:

1. In accordance with Section 1031.02(a)(3)(B) of the Internal Revenue Code for a New Puerto Rico, Act No. 1 of the Legislature of Puerto Rico, approved January 31, 2011, as amended by Act 232 of December 11, 2011 (the "PR Code"), and Article 20(b) of the Act, interest on the Series 2011A Bonds and any gain realized from the sale or exchange thereof is exempt from the income tax imposed by Sections 1021.02, 1022.01 and 1022.02 of the PR Code.

2. In accordance with Section 1022.04(b)(2) of the PR Code, interest on the Series 2011A Bonds is excluded from the "adjusted net book income" of a corporation for purposes of computing the alternative minimum tax imposed by Section 1022.03(a) of the PR Code.

3. In accordance with Section 1021.02(a)(2)(A)(i) of the PR Code, the "alternative basic tax taxable income" of an individual does not include interest on the Series 2011A Bonds for purposes of determining the Puerto Rico alternative basic tax imposed by Section 1021.02(a)(1) of the PR Code.

4. The Series 2011A Bonds will be considered an obligation of an instrumentality of the Government of Puerto Rico for purposes of: (i) the non-recognition of gain rules of Section 1034.04(f)(2)(A) of the PR Code applicable to certain involuntary conversions; and (ii) Section 1022.05(g) of the PR Code, which provides an exemption from the surtax imposed by Section 1022.05(a) of the PR Code for corporations that have a certain percentage of their net income invested in obligations of instrumentalities of the Government of Puerto Rico and certain other investments.

5. Interest on the Series 2011A Bonds is exempt from Puerto Rico municipal license taxes under Section 9(25) of the Puerto Rico Municipal License Tax Act of 1974, as amended.

6. The Series 2011A Bonds are exempt from Puerto Rico personal property tax pursuant to Act No. 44 of the Legislature of Puerto Rico, approved June 21, 1988, as amended, Section 3.11 of the Puerto Rico Municipal Property Tax Act of 1991, as amended, and Section 3 of the Puerto Rican Federal Relations Act.

7. The Series 2011A Bonds are exempt from Puerto Rico (i) gift tax with respect to donors who are residents of Puerto Rico at the time the gift is made and (ii) estate tax with respect to estates of decedents who are residents of Puerto Rico at the time of death and who acquired their United States citizenship solely by reason of birth or residence in Puerto Rico.

8. Interest on the Series 2011A Bonds constitutes "industrial development income" under Section 2(j) of the Puerto Rico Industrial Incentives Act of 1963, as amended, the Puerto Rico Industrial Incentives Act of 1978, as amended, the Puerto Rico Tax Incentives Act of 1987, as amended, and the Puerto Rico Tax Incentives Act of 1998 , as amended (collectively, the "Incentives Acts"), when received by a holder of a grant of tax exemption issued under any of the Acts that acquired the Series 2011A Bonds with "eligible funds," as such term is defined in the Incentives Acts.

The PR Code provides rules for "amortizable bond premium" that an owner of a Bond should refer to in the event that the amount payable at maturity or earliest redemption of the Series 2011A Bonds is less than such owner's basis in the Series 2011A Bonds.

The PR Code does not contain any provisions regarding the treatment of the excess of a Bond's redemption price at maturity over its initial issue price (original issue discount). Under the administrative practice followed by the Puerto Rico Treasury Department with respect to the repealed Puerto Rico Internal Revenue Code of 1994, as amended, original issue discount was treated as interest.

Prospective owners of the Series 2011A Bonds should be aware that, pursuant to Sections 1033.17(a)(5), 1033.17 (a)(10) and 1033.17(f) of the PR Code, ownership of the Series 2011A Bonds may, under certain circumstances, result in a disallowance, for Puerto Rico income tax purposes, of interest expense and other expenses related to an investment in the Series 2011A Bonds.

United States Federal Income Tax Considerations for Puerto Rico Investors

IRS Circular 230 Disclosure: The following tax discussion is not intended or written to be used, and cannot be used by any taxpayer, for purposes of avoiding penalties that may be imposed on a taxpayer by the Internal Revenue Service. This tax discussion was written in connection with the promotion or

marketing of the Series 2011A Bonds. Each prospective purchaser of the Series 2011A Bonds should seek tax advice from an independent tax advisor based on its particular circumstances.

Based upon the provisions of the Code, now in force and the rules and regulations thereunder, it is the opinion of Ferraiuoli LLC that:

1. Interest or original issue discount on the Series 2011A Bonds owned by an individual is excludable from the gross income of the individual thereof for United States federal income tax purposes under Section 933 of the Code if (a) the individual is a bona fide resident of Puerto Rico during the entire taxable year in which such interest or original discount is to be recognized for purposes of the Code and (b) such interest or original issue discount is not, and is not treated as, income effectively connected with, or attributable to, the conduct of a trade or business within the United States by such individual under the Code.

2. Interest or original issue discount on the Series 2011A Bonds derived by a corporation organized under the laws of Puerto Rico is not subject to United States federal income tax under the Code if: (a) such interest or original issue discount is not, and is not treated as, income effectively connected with, or attributable to, the conduct of a trade or business in the United States by such corporation under the Code; (b) such corporation is not a controlled foreign corporation or a passive foreign investment company under the Code; and (c) such corporation is not treated as a domestic corporation for purposes of the Code.

3. United States taxpayers, other than individuals who comply with the requirements set forth below, may be subject to federal income tax on any gain realized upon sale of the Series 2011A Bonds. Pursuant to Notice 89-40, issued by the United States Internal Revenue Service on March 27, 1989, and the regulations issued under Section 937 of the Code, the gain from the sale of the Series 2011A Bonds by an individual that is not a resident of the United States under Section 865(g) of the Code and who is a bona fide resident of Puerto Rico will constitute Puerto Rico source income, and therefore will qualify for exclusion from gross income under Section 933 of the Code, provided (i) said Series 2011A Bonds do not constitute inventory in the hands of such seller, (ii) such gain is not attributable to an office or fixed place of business of the individual located outside Puerto Rico, and (iii) the individual has been a bona fide resident of Puerto Rico for the shorter of (1) the full period during which the individual has owned the Series 2011A Bonds or (2) each of the ten years preceding the year of the sale. In the case the individual is a bona fide resident of Puerto Rico for the tax year for which the source of income must be determined and the individual was a United States citizen or resident (other than a bona fide resident of Puerto Rico) for any of the ten years preceding said year, the individual may elect to treat as gain from sources within Puerto Rico the portion of the gain attributable to the individual's holding period in Puerto Rico.

Prospective owners of the Series 2011A Bonds should consult their tax advisors with respect to the precise determination of the Puerto Rico and United States federal tax consequences arising from ownership or disposition of the Series 2011A Bonds.

LEGAL INVESTMENT

The Bonds will be eligible for deposit by banks in Puerto Rico to secure public funds and will be approved investments for insurance companies to qualify them to do business in Puerto Rico as required by law.

REMARKETING AGENT

Wells Fargo Securities, LLC will serve as the initial Remarketing Agent for the Series 2011C Bonds. The Remarketing Agent will set the interest rate on and remarket the Series 2011C Bonds and perform the other duties as provided for in the Loan and Trust Agreement, subject to the provisions of the Remarketing Agreement (the "Remarketing Agreement"). The Remarketing Agent may for its own account or as broker or agent for others deal in Series 2011C Bonds and may do anything any other Bondowner may do to the same extent as if the Remarketing Agent were not serving as such. The Remarketing Agreement provides that the Ports Authority will indemnify the Remarketing Agent against certain liabilities, including certain liabilities under applicable securities laws.

CERTAIN CONSIDERATIONS RELATING TO REMARKETING OF SERIES 2011C BONDS

The Remarketing Agent is Paid by the Ports Authority. The Remarketing Agent's responsibilities include determining the interest rate from time to time and remarketing Series 2011C Bonds that are mandatorily tendered by the Owners thereof (subject to the terms of the Remarketing Agreement, dated as of December 28, 2011, between the Ports Authority and the Remarketing Agent). The Remarketing Agent is appointed by the Ports Authority and is paid by the Ports Authority for its services. As a result, the interests of the Remarketing Agent may differ from those of existing Owners and potential purchasers of the Series 2011C Bonds.

The Remarketing Agent May Purchase Tendered Series 2011C Bonds for Its Own Account. The Remarketing Agent acts as remarketing agent for a variety of obligations and, in its sole discretion, routinely purchases such obligations for its own account in order to achieve a successful remarketing of the obligations (*i.e.,* because there are otherwise not enough buyers to purchase the obligations) or for other reasons. The Remarketing Agent is permitted, but not obligated, to purchase tendered Series 2011C Bonds for its own account and, if it does so, it may cease doing so at any time without notice. The Remarketing Agent may also make a market in the Series 2011C Bonds by routinely purchasing and selling Series 2011C Bonds other than in connection with a mandatory tender and remarketing. Such purchases and sales may be at or below par. However, the Remarketing Agent is not required to make a market in Series 2011C Bonds. The Remarketing Agent also may sell any Series 2011C Bonds it has purchased to one or more affiliated investment vehicles for collective ownership or enter into derivative arrangements with affiliates or others in order to reduce its exposure to the Series 2011C Bonds. The purchase of Series 2011C Bonds by the Remarketing Agent may create the appearance that there is greater third party demand for the Series 2011C Bonds in the market than is actually the case.

Series 2011C Bonds May be Offered at Different Prices on Any Date Including a Purchase Date. Pursuant to the Remarketing Agreement, the Remarketing Agent is required to determine the applicable rate of interest that, in its judgment, is the lowest rate that would permit the sale of the Series 2011C Bonds bearing interest in the then applicable Mode at par plus accrued interest, if any, on and as of the Rate Determination Date. The interest rate will reflect, among other factors, the level of market demand for the Series 2011C Bonds (including whether the Remarketing Agent is willing to purchase Series 2011C Bonds for its own account). The Remarketing Agent may or may not be able to remarket any Series 2011C Bonds tendered for purchase on any Purchase Date at par. The Remarketing Agent is not obligated to advise purchasers in a remarketing if it does not have third party buyers for all of the Series 2011C Bonds at the remarketing price. In the event the Remarketing Agent owns any Series 2011C Bonds for its own account, it may, in its sole discretion in a secondary market transaction outside the tender process, offer such Series 2011C Bonds on any date, including the Purchase Date, at a discount to par to some investors.

The Ability to Sell the Series 2011C Bonds other than through Tender Process May Be Limited. The Remarketing Agent may buy and sell Series 2011C Bonds other than through the tender process. However, it is not obligated to do so and may cease doing so at any time without notice. Thus, investors who purchase the Series 2011C Bonds, whether in a remarketing or otherwise, should not assume that they will be able to sell their Series 2011C Bonds other than by tendering the Series 2011C Bonds in accordance with the mandatory tender process.

UNDERWRITING

The Underwriters have jointly and severally agreed, subject to certain conditions, to purchase the Bonds from the Financing Authority at an aggregate discount of $3,215,318.21 from the initial offering prices of the Bonds set forth or derived from information set forth on the inside cover hereof. The obligation of the Underwriters to purchase the Bonds is subject to certain conditions precedent, and they will be obligated to purchase all the Bonds if any Bonds are purchased. The Underwriters may offer to sell the Bonds to certain dealers (including dealers depositing the Bonds into unit investment trusts, certain of which may be sponsored or managed by the Underwriters) and others at prices lower than the initial public offering prices. The offering prices may be changed from time to time by the Underwriters.

The Underwriters and their respective affiliates are financial institutions engaged in various activities, which may include securities trading, commercial and investment banking, financial advisory, investment management, principal investment, hedging, financing and brokerage activities. Certain of the Underwriters and their respective affiliates have, from time to time, performed, and may in the future perform, various investment banking services for the Commonwealth and/or its instrumentalities, for which they received or will receive customary fees and expenses.

In the ordinary course of their various business activities, the Underwriters and their respective affiliates may make or hold a broad array of investments and actively trade debt and equity securities (or related derivative securities) and financial instruments (which may include bank loans and/or credit default swaps) for their own account and for the accounts of their customers and may at any time hold long and short positions in such securities and instruments. Such investment and securities activities may involve securities and instruments of the Commonwealth and/or its instrumentalities.

A portion of the Bond proceeds will be used to make a swap termination payment to Wells Fargo Bank N.A., as successor swap counterparty, in connection with the an interest rate hedge agreement between the Ports Authority and Wells Fargo Bank, N.A. (successor by merger to Wachovia Bank, N.A.), an affiliate of Wells Fargo Securities, LLC, an underwriter of this offering. A portion of the Bond proceeds will also be used to repay a loan to the Ports Authority from Wells Fargo Bank, N.A., and a loan to the Ports Authority from Banco Bilbao Vizcaya Argentaria Puerto Rico (BBVAPR), Banco Santander Puerto Rico (BSPR), and FirstBank Puerto Rico Corp. (FBPR). BBVAPR MSD, is a division of BBVAPR, FirstBank Puerto Rico Securities is a subsidiary of FBPR and Santander Securities is an affiliate BSPR. All three entities are underwriters of this issue.

Wells Fargo Securities, LLC has entered into a joint underwriting agreement with Scotia MSD to assist the Commonwealth of Puerto Rico, its public corporations, agencies, instrumentalities, and municipalities in structuring and facilitating the issuance of certain municipal securities. Pursuant to the terms of the joint underwriting agreement and in compliance with applicable rules, compensation with respect to the underwriting of the applicable securities will be allocated between the firms. Wells Fargo Securities is the trade name for certain capital markets and investment banking services of Wells Fargo & Company and its subsidiaries, including Wells Fargo Securities, LLC, member NYSE, FINRA, and SIPC.

J.P. Morgan Securities LLC ("JPMS"), one of the Underwriters of the Bonds, has entered into a negotiated dealer agreement (the "Dealer Agreement") with Charles Schwab & Co., Inc. ("CS&Co.") for the retail distribution of certain securities offerings, including the Bonds, at the original issue prices. Pursuant to the Dealer Agreement, CS&Co. will purchase Bonds from JPMS at the original issue price less a negotiated portion of the selling concession applicable to any Bonds that CS&Co. sells. JPMS has also entered into an agreement with FirstBank Puerto Rico Securities Corp. to assist the Commonwealth of Puerto Rico, its public corporations, agencies, instrumentalities, and municipalities in structuring and facilitating the issuance of certain municipal securities. Pursuant to the terms of the agreement and in compliance with applicable rules, compensation with respect to the underwriting of such municipal securities will be allocated between the parties.

Pershing LLC, a subsidiary of The Bank of New York Mellon Corporation, and Barclays Capital Inc. established a strategic alliance in May of 2009, which enables Pershing LLC to participate as a selling group member and a retail distributor for all new issue municipal bond offerings underwritten by Barclays Capital Inc., including the Bonds offered hereby. Pershing LLC will receive a selling concession from Barclays Capital Inc. in connection with its distribution activities relating to the Bonds.

BMO Capital Markets GKST Inc. has entered into an alliance agreement (the "Alliance Agreement") with VAB Financial LLC, under which the parties shall provide services and advise each other in matters related to the structuring and execution of certain municipal finance transactions in the U.S. capital markets with governmental entities located in the Commonwealth of Puerto Rico. Pursuant to the terms of the Alliance Agreement and in compliance with any applicable rules, the parties will be entitled to receive a portion of each other's net profits from the underwriting of the Bonds as consideration for their professional services.

BMO Capital Markets is the trade name for certain capital markets and investment banking services of Bank of Montreal and its subsidiaries, including BMO Capital Markets GKST Inc., which is a direct, wholly-owned subsidiary of Harris Financial Corp. which is itself a wholly-owned subsidiary of Bank of Montreal.

Citigroup Inc. and Morgan Stanley, the respective parent companies of Citigroup Global Markets Inc. ("Citigroup") and Morgan Stanley & Co. LLC ("Morgan Stanley"), each an underwriter of the Bonds, have entered into a retail brokerage joint venture. As part of the joint venture each of Citigroup and Morgan Stanley will distribute municipal securities to retail investors through the financial advisor network of a new broker-dealer, Morgan Stanley Smith Barney LLC. This distribution arrangement became effective on June 1, 2009. As part of this arrangement, each of Citigroup and Morgan Stanley will compensate Morgan Stanley Smith Barney LLC for its selling efforts in connection with their respective allocations of Bonds.

Goldman, Sachs & Co. and UBS Financial Services Incorporated of Puerto Rico have entered into an agreement relating to structuring and coordinating the marketing and execution of bond offerings in the United States and global capital markets for the Commonwealth of Puerto Rico's governmental entities and other municipal bond issuers. For each issuance of municipal securities for which both parties act as managers, the parties will be entitled to receive a portion of each other's revenues from the underwriting in consideration for their professional services.

Popular Securities, Inc. has entered into a joint venture agreement (the "JV Agreement") with Morgan Stanley, under which the parties shall provide services and advise to each other related to the structuring and execution of certain municipal finance transactions in the U.S. capital markets with governmental entities located in the Commonwealth of Puerto Rico. Pursuant to the terms of the JV Agreement and in compliance with applicable rules, the parties will be entitled to receive a portion of each other's net profits from the underwriting of the Bonds as consideration for their professional services.

Santander Securities Corporation ("SSC") and Merrill Lynch, Pierce, Fenner & Smith Incorporated ("Merrill") have entered into an agreement pursuant to which they will provide services and advice to each other related to the structuring and execution of certain municipal finance transactions for the Commonwealth of Puerto Rico's governmental entities in the global capital markets and in the United States market and in the Puerto Rico market if issued in connection with such global or U.S. issuances. SSC and Merrill will be entitled to receive a portion of each other's revenues from the underwriting of the Bonds as consideration for their professional services.

Oriental Financial Services Corp. ("Oriental") and Raymond James & Associates, Inc. ("Raymond James") have entered into an agreement under which the parties provide services and advice to each other to assist the Commonwealth and its issuers in the structuring and execution of their municipal securities offerings. As part of the agreement, Oriental and Raymond James share in the risk from the underwriting of the Bonds as part of the consideration for their professional services.

BBVAPR División de Valores Municipales ("BBVAPR MSD") and RBC Capital Markets, LLC ("RBC") have entered into an agreement under which the parties provide services and advice to each other to assist the Commonwealth and its issuers in the structuring and execution of their municipal securities offerings. As part of the agreement, BBVAPR MSD and RBC share in the risk from the underwriting of the Bonds as part of the consideration for their professional services.

COMMONWEALTH COVENANT

Pursuant to the Enabling Act, the Commonwealth has pledged to all owners of the Bonds that it will not limit or alter the rights or powers vested in the Financing Authority by the Enabling Act so as to impair the rights of such owners until the Bonds and the interest thereon are fully met and discharged.

FINANCIAL ADVISOR

As required by Act No. 272 of the Legislative Assembly of Puerto Rico, approved May 15, 1945, as amended, Government Development Bank has acted as financial advisor to the Financing Authority in connection with the offering of the Bonds. As financial advisor, Government Development Bank participated in the selection of the Underwriters of the Bonds. Certain of the Underwriters have been selected by Government Development Bank to serve from time to time as underwriters of its obligations and the obligations of the Commonwealth of Puerto Rico, its instrumentalities and public corporations. Certain Underwriters or their affiliates also participate in other financial transactions with Government Development Bank.

LEGAL MATTERS

Legal matters incident to the authorization, issuance, sale and delivery of the Bonds are subject to the unqualified approving legal opinion of Greenberg Traurig LLP, Boston, Massachusetts, Bond Counsel. The form of the proposed opinion of Bond Counsel is set forth in APPENDIX F. Certain legal matters will be passed upon for the Financing Authority, the Ports Authority and Government Development Bank by Greenberg Traurig LLP, Boston, Massachusetts, as special counsel. Certain legal matters also will be passed upon for Government Development Bank by its General Counsel. Certain tax matters are being passed upon by Ferraiuoli LLC, Special Puerto Rico Tax Counsel. The form of the proposed tax opinion of Special Puerto Rico Tax Counsel is set forth in APPENDIX G. Certain legal matters will be passed upon for the Underwriters by Ferraiuoli LLC, San Juan, Puerto Rico.

RATINGS

The Bonds have been assigned a rating of "Baa1" by Moody's Investors Service, Inc.; and a rating of "BBB" by Standard & Poor's Rating Services, a division of Standard & Poor's Financial Services LLC. The rating agencies were provided with materials related to Government Development Bank and the Bonds and other relevant information, and no application has been made to any other rating agency for the purpose of obtaining a rating on the Bonds.

Any explanation regarding the reasons for and the significance of such ratings must be obtained only from the respective rating agency furnishing the same. The ratings reflect only the respective opinions of such rating agencies. There is no assurance that the ratings will continue for any given period of time or will not be revised downward or withdrawn entirely by either or both of such rating agencies. Any such downward revision or withdrawal of the ratings could have an adverse effect on the market prices of the Bonds.

CONTINUING DISCLOSURE

The Financing Authority has determined that no financial or operating data concerning the Financing Authority is material to any decision to purchase, hold, or sell the Bonds and the Financing Authority will not provide any such information. The Ports Authority and Government Development Bank have undertaken all responsibilities for any continuing disclosure to Bondowners or beneficial owners of the Bonds as described below, and the Financing Authority shall have no liability to the Bondowners or beneficial owners of the Bonds or any other person with respect to such disclosures.

In accordance with the requirements of Rule 15c2-12, as amended (the "Rule"), promulgated by the Securities and Exchange Commission ("SEC"), Government Development Bank has agreed to the following:

1. Financial information and operating data for the Commonwealth is available through EMMA. If the Commonwealth were to cease to provide such financial and operating information to the MSRB through EMMA, Government Development Bank has agreed to cause such information to be made available.

2. Government Development Bank will file, within 305 days after the end of each fiscal year, commencing with the fiscal year ended June 30, 2011, with the MSRB through EMMA, core financial information and operating data for such fiscal year, including (i) its audited financial statements, prepared in accordance with generally accepted accounting principles in effect from time to time, and (ii) material historical quantitative data (including financial information and operating data) and information as to revenues, expenditures, financial operations and indebtedness of Government Development Bank of the type generally found or incorporated by reference in this Official Statement; and

3. Government Development Bank will file in a timely manner, with the MSRB through EMMA, notice of a failure to provide the required annual financial information on or before the specified period.

Moreover, in accordance with the requirements of the Rule, the Ports Authority has agreed to file, as applicable, in a timely manner, not in excess of ten (10) business days after the occurrence of the event, with the MSRB through EMMA, notice the occurrence of any of the following events with respect to the Bonds. Government Development Bank has agreed to notify the Ports Authority, in a timely manner, but not more than seven business days after the occurrence of an event described in items m. and n., below:

a. principal and interest payment delinquencies;
b. non-payment related defaults, if material;
c. unscheduled draws on debt service reserves reflecting financial difficulties;
d. unscheduled draws on credit enhancements reflecting financial difficulties;
e. substitution of credit or liquidity facility providers, or their failure to perform;
f. adverse tax opinions, the issuance by the IRS of proposed or final determinations of taxability, Notices of Proposed Issue (IRS Form 5701-TEB) or other material notices or determinations with respect to the tax status of the Bonds, or other material events affecting the tax status of the Bonds;
g. modifications to rights of the owners (including Beneficial Owners) of the Bonds, if material;
h. bond calls, if material;
i. defeasances;
j. release, substitution, or sale of property securing repayment of the Bonds, if material;
k. rating changes;
l. tender offers;
m. bankruptcy, insolvency, receivership, or similar proceeding of the Ports Authority or Government Development Bank;
n. the consummation of a merger, consolidation or acquisition involving the Ports Authority or Government Development Bank or the sale of substantially all of the assets of the Ports Authority or Government Development, other than in the ordinary course of business, the entry into a definitive agreement to undertake such action or the termination of a definitive agreement relating to any such actions, other than pursuant to its terms, if material; and
o. the appointment of a successor or additional trustee, or the change of name of a trustee, if material.

Event c. is included pursuant to a letter from the SEC staff to the National Association of Bond Lawyers, dated September 19, 1995. However, event c. may not be applicable since the terms of the Bonds do not provide for "debt service reserves." In addition, with respect to the following events:

Events d. and e. The Ports Authority does not undertake to provide any notice with respect to credit enhancement added after the primary offering of the Bonds, unless the Financing Authority applies for or participates in obtaining the enhancement.

Event f. For information on the tax status of the Bonds, see *"Tax Matters."*

Event h. The Ports Authority does not undertake to provide the above-described event notice of a mandatory scheduled redemption, not otherwise contingent upon the occurrence of an event, if (i) the terms, dates and amounts of redemption are set forth in detail in this Official Statement, (ii) the only open issue is which Bonds will be redeemed in the case of a partial redemption, (iii) notice of redemption is given to the Bond owners as required under the terms of the Bonds, and (iv) public notice of the redemption is given pursuant to Securities Exchange Act of 1934 Release No. 34-23856 of the SEC, even if the originally scheduled amounts are reduced by prior optional redemptions or bond purchases.

Event m. According to the Rule, the event is considered to occur when any of the following occur: the appointment of a receiver, fiscal agent, or similar officer for an obligated person in a proceeding under the U.S. Bankruptcy Code or in any other proceeding under state or federal law in which a court or governmental authority has assumed jurisdiction over substantially all of the assets or business of the obligated person, or if such jurisdiction has been assumed by leaving the existing governing body and officials or officers in possession but subject to the supervision and orders of a court or governmental authority, or the entry of an order confirming a plan of reorganization, arrangement or liquidation by a court or governmental authority having supervision or jurisdiction over substantially all of the assets or business of the obligated person.

The Ports Authority may from time to time choose to provide notice of the occurrence of certain other events in addition to those listed above if, in the judgment of the Ports Authority, such other events are material with respect to the Bonds, but the Ports Authority does not undertake to provide any such notice of the occurrence of any material event except those events listed above.

The Ports Authority and Government Development Bank acknowledge that their respective undertakings pursuant to the Rule described under this heading are intended to be for the benefit of the holders of the Bonds, including Beneficial Owners, and shall be enforceable by the Trustee for their benefit; provided, however, that the right to enforce the provisions of this undertaking shall be limited to a right to obtain specific enforcement of the Ports Authority's and Government Development Bank's obligations hereunder, as the case may be, and any failure by the Ports Authority or Government Development Bank to comply with the provisions of this undertaking shall not be an event of default with respect to the Bonds under the Loan and Trust Agreement. No Bondowner or Beneficial Owner may institute any suit, action or proceeding at law or in equity ("Proceeding") for the enforcement of the foregoing covenants (the "Covenants") or for any remedy for breach thereof, unless such Bondowner or Beneficial Owner shall have filed with the Ports Authority or Government Development Bank written notice of any request to cure such breach, and the Ports Authority or Government Development Bank, as the case may be, shall have refused to comply within a reasonable time. All Proceedings shall be instituted only in a Commonwealth court located in the Municipality of San Juan for the equal benefit of all Bondowners or Beneficial Owners of the Outstanding Bonds benefited by the Covenants, and no remedy shall be sought or granted other than specific performance of any of the Covenants at issue. Notwithstanding the foregoing, no challenge to the adequacy of the information provided in accordance with the filings mentioned above may be prosecuted by any Bondowner or Beneficial Owner except in compliance with the remedial and enforcement provisions contained in the Loan and Trust Agreement.

The Covenants may only be amended if:

(a) the amendment is made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature, or status of the Ports Authority and/or Government Development Bank or the type of business conducted by them; the Covenants, as amended, would have complied with the requirements of the Rule at the time of award of the Bonds, after taking into account any amendments or change in circumstances; and the amendment does not materially impair the interests of Bondowners or Beneficial Owners, as determined by parties unaffiliated with the Ports Authority and/or the Government Development Bank; or (b) all or any part of the Rule, as interpreted by the staff of the Securities and Exchange Commission at the date of the adoption of such Rule, ceases to be in effect for any reason, and the Ports Authority and/or Government Development Bank elects that the Covenants shall be deemed amended accordingly. Government Development Bank has agreed that the annual financial information containing any amended operating data or financial information will explain, in narrative form, the reasons for the amendment and the impact of the change in the type of operating data or financial information being provided.

Any assertion of beneficial ownership must be filed, with full documentary support, as part of the written request described above.

These Covenants have been made in order to assist the Underwriters in complying with the Rule.

Prior Continuing Disclosure Non-Compliance

Government Development Bank has made similar continuing disclosure undertakings in connection with prior bond issuances, and has complied with all such covenants, except as hereinafter noted.

Government Development Bank's financial and operating information for fiscal year ended June 30, 2007 was filed after the filing deadline of May 1, 2008.

The Commonwealth of Puerto Rico's audited financial statements for the fiscal year ended June 30, 2002 were filed after the Commonwealth of Puerto Rico's filing deadline of May 1, 2003 because of delays in finalizing such financial statements resulting from the implementation of GASB Statement No. 34 ("GASB 34"). The Commonwealth of Puerto Rico's audited financial statements for the fiscal year ended June 30, 2003 were also filed after the Commonwealth of Puerto Rico's filing deadline of April 30, 2004, because of delays in finalizing the financial statements of certain of the Commonwealth of Puerto Rico's reporting units due to the implementation of GASB 34. The Commonwealth of Puerto Rico's audited financial statements for the fiscal years ended June 30, 2004, 2006, 2007 and 2008 were also filed after the Commonwealth of Puerto Rico's respective filing deadlines of May 1, 2005, 2007, 2008 and 2009, because various governmental agencies did not submit their audited financial statements to the central government's external auditors on time, thereby delaying submission of the Commonwealth of Puerto Rico's audited financial statements. The Commonwealth of Puerto Rico's audited financial statements for the fiscal year ended June 30, 2009 were also filed after the Commonwealth of Puerto Rico's filing deadline of May 1, 2010, due to delays in the engagement and transition of new external auditors, the implementation of new government accounting pronouncements, and the restatement of the financial statements of certain discretely presented component units. The Commonwealth of Puerto Rico's audited financial statements for fiscal years ended June 30, 2004, 2006, 2007 and 2008 were filed by the end of the first quarter of the following fiscal year, while the Commonwealth of Puerto Rico's audited financial statements for the fiscal year ended June 30, 2009 was filed on October 25, 2010.

The Commonwealth Report for the fiscal year ended June 30, 2008 containing the information described in paragraph l(ii) above, was filed after the Commonwealth of Puerto Rico's filing deadline of May 1, 2009. Such Commonwealth Report was filed on June 1, 2009. Except for that Commonwealth Report, the Commonwealth has timely filed the Commonwealth Report for all other fiscal years.

In 2011, the Commonwealth complied with its continuing disclosure undertaking relating to fiscal year 2010. As of the date of this Official Statement, the Commonwealth is in compliance with its continuing disclosure filing requirements related to its outstanding general obligation bonds.

The Commonwealth has established new policies and procedures that it believes will ensure full and timely compliance with all continuing disclosure obligations in the future. Such new policies and procedures include: (i) the assignment of additional resources from local and international audit firms to those component units whose financial statements have not been timely provided to the Commonwealth of Puerto Rico; (ii) the assignment of dedicated external and internal resources to (a) assist the Central Accounting Division at the Treasury Department in the preparation of complex financial information that has historically delayed the audit and (b) provide periodic and consistent follow up on component unit financial statement deliverables and deadlines; (iii) the execution of a memorandum of understanding between the Treasury Department, OMB and Government Development Bank for the coordination of all financial statement related tasks and the designation of Government Development Bank, in its role as fiscal agent, to review and monitor the progress of certain component units; and (iv) the establishment of an Audit Oversight Committee comprised of the Treasury Department and Government Development Bank personnel in order to continuously monitor the status of the audit and the Commonwealth of Puerto Rico's financial statements.

MISCELLANEOUS

The foregoing references to and summaries of certain provisions of the Loan and Trust Agreement, the Reimbursement Agreement, the GDB Letter of Credit, the Enabling Act, the Constitution of Puerto and the Bonds are subject to all the detailed provisions thereof. Such references and summaries do not purport to be complete and are qualified in their entirety by reference to such acts, laws, documents, agreements or decisions. Copies of the Loan and Trust Agreement and the Reimbursement Agreement are available for inspection during regular business hours at the offices of Government Development Bank or at the principal corporate trust office of the Trustee.

Any statements in this Official Statement involving matters of opinion, whether or not expressly so stated, are intended as such and not as representations of fact.

Information relating to DTC and the book-entry system described herein under the heading "DESCRIPTION OF THE BONDS - Book-Entry Only System" has been furnished by DTC and is believed to be reliable, but none of the Financing Authority, the Ports Authority, Government Development Bank and the Underwriters makes representations or warranties whatsoever with respect to such information.

The Financing Authority has consented to the use of this Official Statement. The Financing Authority is responsible only for the statements contained under the caption "The Financing Authority" and the information pertaining to the Financing Authority under the caption "Litigation," and the Financing Authority makes no representation as to the accuracy or completeness of any other information. The Ports Authority is responsible only for the statements contained under the caption "The Ports Authority," "Risk Factors – Risks relating to the Ports Authority," and the information pertaining to the Ports Authority under the caption "Litigation," and the Ports Authority makes no representation as to the accuracy or completeness of any other information. Information relating to DTC and its book-entry system has been furnished by DTC and is believed to be reliable. Information relating to Government Development Bank and the Commonwealth has been furnished by Government Development Bank and is believed to be reliable. Except as otherwise stated herein, neither the Financing Authority nor the Underwriters makes any representations or warranties whatsoever with respect to the information contained herein.

APPENDIX A - "Definitions of Certain Terms" has been prepared by Greenberg Traurig, LLP, Bond Counsel.

APPENDIX B - "Summary of Certain Provisions of the Loan and Trust Agreement" has been prepared by Greenberg Traurig, LLP, Bond Counsel.

APPENDIX C - "Forms of GDB Letter of Credit" has been provided by Government Development Bank.

APPENDIX D - "Summary of Certain Provisions of the Reimbursement Agreement" has been prepared by Greenberg Traurig, LLP, special counsel to Government Development Bank.

APPENDIX E - "Basic Financial Statements and Required Supplementary Information of Government Development Bank for Puerto Rico as of and for the Year Ended June 30, 2011" has been provided by Government Development Bank.

APPENDIX F - "Form of Bond Counsel Opinion" has been provided by Greenberg Traurig, LLP, Bond Counsel.

APPENDIX G - "Form of Special Tax Counsel Opinion" has been provided by Ferraiuoli LLC, Special Tax Counsel.

APPENDIX H - "Tables of Discount Bonds and Premium Bonds" has been provided by Wells Fargo Securities, LLC.

APPENDIX I: Commonwealth of Puerto Rico Financial Information and Operating Data Report, dated December 6, 2011.

All Appendices are incorporated herein as an integral part of this Official Statement.

This Official Statement will be filed with the MSRB through EMMA.

PUERTO RICO INFRASTRUCTURE FINANCING AUTHORITY

By: /s/José E. Basora Fagundo
Executive Director

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DEFINITIONS OF CERTAIN TERMS

In addition to the definitions appearing elsewhere in this Official Statement, the following are definitions used in this Official Statement and in the Loan and Trust Agreement, dated as of December 1, 2011 (the "Agreement"), among the Issuer, the Borrower and the Trustee pertaining to the Bonds.

"*Act of Bankruptcy of the Bank*" means (i) the Bank shall commence any case, proceeding or other action under any existing or future law (A) relating to bankruptcy, insolvency, reorganization or relief of debtors, seeking to have an order for relief entered with respect to it, or seeking to adjudicate it as bankrupt or insolvent, or seeking reorganization, arrangement, adjustment, winding-up, liquidation, dissolution, composition or other relief with respect to it or its debts, or (B) seeking appointment of a receiver, trustee, custodian or other similar official for it or for all or any substantial part of its assets, or the Bank shall make a general assignment for the benefit of its creditors; (ii) there shall be commenced against the Bank any case, proceeding or other action of a nature referred to in clause (i) above which (X) results in an order for such relief or in the appointment of a receiver or similar official or (Y) remains undismissed, undischarged or unbonded for a period of 90 days; (iii) there shall be commenced against the Bank any case, proceeding or other action seeking issuance of a warrant of attachment, execution, distraint or similar process against all or any substantial part of its assets, which results in the entry of an order for any such relief which shall not have been vacated, discharged, or stayed or bonded pending appeal within ninety (90) days from the entry thereof; (iv) the Bank shall take any action in furtherance of, or indicating its consent to, approval of, or acquiescence in, any of the acts set forth in clause (i), (ii) or (iii) above; (v) the Bank shall generally not, or shall be unable to, or shall admit in writing its inability to, pay its debts; or (vi) the Bank or any other governmental authority having jurisdiction over the Bank imposes a debt moratorium, debt restructuring, or comparable restriction on the repayment when due and payable of the principal of or interest on any general obligation indebtedness of the Bank.

"*Affiliate*" means with respect to each party, any entity in which such party has a direct or indirect interest, financial or otherwise, or any entity established for the benefit of such party.

"*Authorized Officer*" means: (i) in the case of the Issuer, any the Executive Director, or any other official of the Issuer so designated by a resolution of the Issuer; and (ii) in the case of the Borrower, the Executive Director or Chief Financial Officer and when used with reference to an act or document of the Borrower, also means any other person authorized to perform the act or execute the document.

"*Bank*" means Government Development Bank for Puerto Rico, as issuer of the Letter of Credit.

"*Bank Bond*" means any Series C Bond purchased with proceeds provided by the Series C Letter of Credit.

"*Bank Default*" means the (i) the occurrence of an Act of Bankruptcy of the Bank, or (ii) the failure of the Bank to honor a properly presented and conforming draw on the Letter of Credit.

"*Bank Rate*" means the per annum rate of interest applicable to Bank Bonds described in the Reimbursement Agreement. In no event shall the Bank Rate exceed the highest interest rate permitted by law. Payment of interest to the Bank under the Reimbursement Agreement on any advances thereunder corresponding to Bank Bonds shall satisfy the Borrower's obligation to pay interest on such Bank Bonds.

"*Bond Counsel*" means Greenberg Traurig, LLP or any attorney at law or firm of attorneys selected by the Issuer of nationally recognized standing in matters pertaining to the federal tax exemption of interest on bonds issued by states and political subdivisions, and duly admitted to practice law before the highest court of any state of the United States.

"*Bond Fund*" means the fund established and so designated pursuant to the Agreement.

"Bond Purchase Fund" means the fund established and so designated pursuant to the Agreement.

"*Bondowners*," *"Owners," "Registered Owners,"* or words of similar import mean the registered owners of the Bonds from time to time as shown in the books kept by the Trustee, as bond registrar and transfer agent, except that wherever appropriate the term *"Owners"* shall mean the owners of the Bonds for federal income tax purposes.

"*Bonds*" means, collectively, the Series A Bonds, the Series B Bonds and the Series C Bonds.

"Borrower" means the Puerto Rico Ports Authority.

"*Borrower Bond*" means any Series C Bond, the Purchase Price of which was paid through funds provided by and registered to the Borrower pursuant the Agreement.

"*Business Day*" means a day (i) that is not a Saturday, Sunday, or legal holiday; (ii) on which banks are not required or authorized to close in New York, New York, or San Juan, Puerto Rico, (iii) on which banking institutions in all of the cities in which the Principal Office of the Trustee and the Bank are located are not required or authorized to remain closed; and (iv) on which the New York Stock Exchange is not closed.

"Code" means the Internal Revenue Code of 1986, as it may be amended from time to time.

"*Commonwealth*" means the Commonwealth of Puerto Rico.

"*Credit Facility Fund*" means the fund established and so designated pursuant to the Agreement.

"*DTC*" means The Depository Trust Company, a limited purpose trust company, New York, New York.

"*Effective Date*" means, with respect to a Series C Bond in the Term Rate Mode, the date on which a new Term Rate Period for that Series C Bond takes effect. The Effective Date shall initially be the date of issuance of the Series C Bonds and thereafter first day of each Term Rate Period.

"*Electronic Means*" means telecopy, facsimile transmission, e-mail transmission or other similar electronic means of communication providing evidence of transmission, including a telephonic communication confirmed by any other method set forth in this definition.

"*Eligible Funds*" means (i) amounts drawn on the Letter of Credit; (ii) amounts paid to the Trustee pursuant to this Agreement which have been held by it for a period of at least 91 days during which no Event of Bankruptcy has occurred and commingled only with other Eligible Funds; (ii) amounts which if applied to the payment of the Bonds would not, in the opinion of nationally recognized counsel experienced in bankruptcy matters selected by the Borrower, be subject to avoidance as a preference under the United States Bankruptcy Code upon an Event of Bankruptcy; and (iv) income derived from the investment of the foregoing; provided that such income shall not be deemed Eligible Funds if an injunction, restraining order, stay, or similar court action is in effect preventing the payment of such income to Bondowners. The Trustee shall maintain records of Eligible Funds held by it.

"*Enabling Act*" means Act No. 44 of the Legislature of Puerto Rico, approved June 21, 1988, as amended.

"*Event of Bankruptcy*" means the filing of a petition in bankruptcy or the commencement of a proceeding under the United States Bankruptcy Code or any other applicable law concerning insolvency, reorganization, or bankruptcy by or against the Borrower, any affiliates thereof, any guarantor of the Bonds (other than the Bank), or the Issuer, as debtor.

"Financing Authority" means the Issuer.

"*Fixed Rate*" means a rate or rates of interest on the Series C Bonds that is fixed for the remaining term of the Series C Bonds.

"Fixed Rate Conversion Date" means the date on which the Series C Bonds are converted to the Fixed Rate Mode, at the option of the Borrower.

"*Fixed Rate Mode*" means an interest rate mode in which the Series C Bonds bear interest at a Fixed Rate.

"GDB" or *"Government Development Bank"* means the Bank.

"*Government or Equivalent Obligations*" means (i) obligations issued or guaranteed by the United States; (ii) certificates evidencing ownership of the right to the payment of the principal of and interest on obligations described in clause (i), provided that such obligations are held in the custody of a bank or trust company satisfactory to the Trustee or the Issuer, as the case may be, in a special account separate from the general assets of such custodian; and (iii) shares of any open-end or closed-end management type investment company or trust registered under 15 U.S.C. §80(a)-1 et seq., including, without limitation, any mutual fund for which the Trustee or an affiliate of the Trustee serves as investment manager, administrator, shareholder servicing agent, and/or custodian or subcustodian, notwithstanding that (A) the Trustee or an affiliate of the Trustee receives fees from such funds for services rendered, (B) the Trustee charges and collects fees for services rendered pursuant to this Agreement, which fees are separate from the fees received from such funds, and (C) services performed for such funds and pursuant to this Agreement may at times duplicate those provided to such funds by the Trustee or its affiliates; provided, that the portfolio of such investment company or trust is limited to obligations described in clause (i) and repurchase agreements fully collateralized by such obligations, and provided further that such investment company or trust shall take custody of such collateral either directly or through a custodian satisfactory to the Trustee or the Issuer.

"Initial Term Rate" means the Term Rate in effect during the Initial Term Rate Period, as shown on the inside cover of this Official Statement.

"Initial Term Rate Period" means the rate period initially applicable to the Series C Bonds, commencing on the date of issuance of the Series C Bonds through and including the End of Initial Term Rate Periods set forth on the inside cover of this Official Statement.

"*Interest Payment Date*" means each date on which interest shall be payable on the Bonds according to their terms so long as any of the Bonds shall be Outstanding. The Interest Payment Dates shall be the 15th day of June and December of each year, commencing with June 15, 2012. The Interest Payment Date shall also be the maturity date or redemption date of any Bond, and the Purchase Date of any Series C Bond.

"Letter of Credit" or *"GDB Letter of Credit"* means, singly and collectively, the Series A/B Letter of Credit and the Series C Letter of Credit.

"Issuer" means the Puerto Rico Infrastructure Financing Authority.

"Loan and Trust Agreement" means the Agreement.

"*Mode*" means the period for and the manner in which the interest rates on the Series C Bonds are set and includes the Term Rate Mode and the Fixed Rate Mode.

"*Mode Change Date*" means the day following the last day of one Mode, or a Term Rate Period, on which another Mode or Term Rate Period begins.

"*Moody's*" means Moody's Investors Service or any of its successors or assigns.

"*Opinion of Bond Counsel*" means an opinion of Bond Counsel to the effect that the matter or action in question will not have an adverse impact on the tax-exempt status of the Series B Bonds or the Series C Bonds for federal income tax purposes.

"*Outstanding*," when used to modify Bonds, refers to Bonds issued, authenticated, and delivered under this Agreement, excluding: (i) Bonds which have been exchanged or replaced; (ii) Bonds which have been paid; (iii)

Bonds which have become due and for the payment of which moneys have been duly provided; and (iv) Bonds with respect to which the Agreement has been defeased pursuant to the terms thereof.

"Ports Authority" means the Borrower.

"Ports Authority Enabling Act" means Act No. 125 of the Legislature of Puerto Rico, approved May 7, 1942, as amended.

"*Principal Office*," when used with respect to the Trustee, means its office located at 101 Barclay Street - 7W, New York, New York 10286, or such other address as the Trustee shall designate; and, when used with respect to any other Paying Agent, means the office thereof designated in writing to the Trustee.

"*Project*" means (i) the refinancing of the Refinanced Loans, the proceeds of which were used to (A) finance and refinance the acquisition of land, site development, construction, renovation or installation of airport or seaport facilities, related infrastructure or buildings, or acquisition or installation of furnishings, equipment, vehicles, or any combination of the foregoing, and (B) provide working capital to the Borrower, (ii) the financing of certain operating expenses of the Ports Authority, and (iii) the financing of the costs of issuance of the Bonds and a swap termination fee.

The word "*Project*" also refers to the facilities which result or have resulted from the foregoing activities.

"*Project Costs*" means the costs of issuing the Bonds and carrying out the Project, but excluding general administrative expenses and overhead of the Borrower and interest on internal advances.

"Purchase Date" means, while the Series C Bonds are in the Term Rate Mode, the date on which Series C Bonds shall be required to be purchased pursuant to a mandatory tender in accordance with the provisions in the form of Term Rate Bonds in the Agreement, which shall be the Business Day following the last day of each Term Rate Period.

"*Purchase Price*" means an amount equal to the principal amount of any Series C Bond mandatorily tendered or deemed tendered for purchase, plus any accrued and unpaid interest thereon to the date of purchase. If the date of purchase is an Interest Payment Date, then the Purchase Price shall not include accrued and unpaid interest, which shall be paid to the Bondowner of record on the applicable Record Date.

"*Rate Determination Date*" means, with respect to Series C Bonds that are to be in the Term Rate Mode, a Business Day not earlier than 15 Business Days nor less than one Business Day next preceding the first day of the next Term Rate Period, and with respect to Series C Bonds that are to be in the Fixed Rate Mode, a Business Day not earlier than two Business Days next preceding the first day of the Fixed Rate Period, each as determined by the Remarketing Agent.

"*Rating Agency*" means each of Moody's and S&P, so long as the Bonds are rated by Moody's and S&P, or any other successor rating agency then rating the Bonds.

"*Redemption Price*" means an amount equal to the principal of and accrued interest, if any, on Bonds subject to redemption to be paid on the date of redemption thereof.

"*Refinanced Loans*" means, collectively, the Tax-Exempt Refinanced Loans and the Taxable Refinanced Loans.

"*Reimbursement Agreement*" means the Letter of Credit Disbursement and Reimbursement Agreement, dated as of December 1, 2011, by and between the Bank and the Borrower, and any amendments and supplements thereto.

"*Remarketing Agent*" means a Person appointed pursuant to a Remarketing Agreement to serve as the Borrower's agent in connection with the remarketing of the Series C Bonds while in the Term Rate Mode, and to perform the duties of a Remarketing Agent hereunder. Wells Fargo Securities, LLC will serve as the initial Remarketing Agent.

"*Remarketing Agreement*" means an agreement by and between the Borrower and the Remarketing Agent relating to the remarketing of Series C Bonds in the Term Rate Mode, as the same may be amended or supplemented from time to time in accordance with the provisions thereof.

"Required Stated Amount" the stated amount of the Series C Letter of Credit, equal to the amount of principal of the Series C Bonds to be remarketed on the Purchase Date, plus an amount equal to interest on such Series C Bonds for 180 days, calculated at the actual rates of interest in effect with respect to Series C Bonds to be remarketed in the Fixed Rate Mode, and at the Term Rate in effect as of such Purchase Date, on Series C Bonds to be remarketed in the Term Rate Mode, and computed on the basis of a 360-day year, consisting of twelve 30-day months.

"*Revenues*" means all rates, rents, fees, charges, and other income and receipts, including proceeds derived from any security provided under the Agreement (which includes draws on the Letter of Credit), payable to the Issuer or the Trustee under the Agreement, excluding administrative fees of the Issuer, fees of the Trustee, reimbursements to the Issuer or the Trustee for expenses incurred by the Issuer or the Trustee, as applicable, and indemnification of the Issuer and the Trustee.

"*Rule*" means Rule 15c2-12 under the Securities Exchange Act of 1934, as amended.

"*Series A Bonds*" or the "*Series 2011A Bonds"* means the $340,000,000 principal amount of Puerto Rico Infrastructure Financing Authority Revenue Bonds (Ports Authority Project), Series 2011A (Federally Taxable), dated the date of delivery thereof, and any bond or bonds duly issued in exchange or replacement thereof.

"*Series B Bonds*" or the "*Series 2011B Bonds"* means the $192,830,000 principal amount of Puerto Rico Infrastructure Financing Authority Revenue Bonds (Ports Authority Project), Series 2011B (Non-AMT), dated the date of delivery thereof, and any bond or bonds duly issued in exchange or replacement thereof.

"*Series C Bonds*" or the "*Series 2011C Bonds"* means the $136,385,000 principal amount of Puerto Rico Infrastructure Financing Authority Revenue Bonds (Ports Authority Project), Series 2011C (AMT), dated the date of delivery thereof, and any bond or bonds duly issued in exchange or replacement thereof.

"Series A/B Letter of Credit" means the irrevocable, transferable direct pay letter of credit issued by the Bank to the Trustee, for the account of the Borrower, as security for the payment of the principal of and interest on the Series A Bonds and the Series B Bonds.

"Series C Letter of Credit" means the irrevocable, transferable direct pay letter of credit issued by the Bank to the Trustee, for the account of the Borrower, as security for the payment of the principal and Purchase Price of and interest on the Series C Bonds.

"*Stated Expiration Date*" means the stated expiration date of a Letter of Credit, and with respect to the Series C Letter of Credit, as it may be extended from time to time as provided in the Agreement.

"S&P" means Standard & Poor's Ratings Group, Inc., or any of its successors or assigns.

"*Tax Agreement*" means the Arbitrage and Tax Certificate, dated December 28, 2011, of the Issuer.

"*Tender Date*" means any date on which a Series C Bond is required to be purchased in accordance with the mandatory tender provisions set forth in the Agreement.

"*Term Rate Mode*" means an interest rate mode in which the Series C Bonds bear interest at the Term Rate.

"*Term Rate*" means the Initial Term Rate, and thereafter the rate of interest determined by the Remarketing Agent for each Term Rate Period to be the lowest rate which, in its judgment, on the basis of prevailing financial market conditions, would permit the sale of the Series C Bonds in the Term Rate Mode at par on and as of the first day of each Term Rate Period, but not in excess of the maximum interest rate permitted by applicable law.

"*Term Rate Index*" means that indication of the lowest interest rate appropriate for bonds similar to the Series C Bonds while in the Term Rate Mode being priced in terms of security, creditworthiness, term and tender privilege which will permit the Series C Bonds while in the Term Rate Mode to be sold at a purchase price equal (excluding accrued interest) to their principal amount, determined first by interviewing three investors of portfolios holding significant numbers of such bonds (none of whom is a Bondowner) and second, if that is not practicable, by referring to the best available database or publication of national recognition containing a recent calculation of such an interest rate for comparable securities.

"*Term Rate Period*" means a period during which a particular rate of interest for the Series C Bonds while in the Term Rate Mode is in effect, including the Initial Term Rate Period, and which is the period from (and including) the date of issue of the Series C Bonds or thereafter the first date of each successive Term Rate Period selected for the Series C Bonds by the Borrower to (but excluding) the commencement date of the next succeeding Term Rate Period. Each Term Rate Period shall be six months, or any multiple of six months.

"*Trustee*" means The Bank of New York Mellon, as trustee under the Agreement, and its successors in such capacity.

"*UCC*" means the Commercial Transactions Act, as now or hereafter in effect in the Commonwealth of Puerto Rico.

"*Underwriter*" means Wells Fargo Securities, LLC, as the representative of the underwriters of the Bonds.

SUMMARY OF CERTAIN PROVISIONS OF THE LOAN AND TRUST AGREEMENT

The following description is a brief summary prepared by Greenberg Traurig, LLP, Bond Counsel, of certain provisions of the Loan and Trust Agreement, dated as of December 1, 2011 (the "Agreement"), pertaining to the Bonds. This summary does not purport to be a complete description or restatement of the material provisions of the Agreement. Investors should obtain and review a copy of the Agreement in order to understand all of the terms of that document. See Appendix A for the definitions of the terms used in this Appendix B.

The Agreement provides for the following transactions: (i) the Issuer's issuance of the Bonds; (ii) the Issuer's loan of the proceeds of the Bonds to the Borrower to finance and refinance the Project; (iii) the Borrower's repayment of the loan from the Issuer through payment to the Trustee of all amounts necessary to pay the Bonds issued by the Issuer; and (iv) the Issuer's assignment to the Trustee in trust for the benefit and security of the Bondowners of certain of the Issuer's rights with respect to the loan to the Borrower under the Agreement, including repayment of the loan to be received from the Borrower.

Establishment of Funds

The Agreement creates the following funds to be held by the Trustee: the Bond Fund, the Credit Facility Fund, and the Bond Purchase Fund. (Sections 303, 306 and 315)

Bond Fund

The Bond Fund is established under the Agreement for the payment of debt service on the Bonds. The Borrower shall make payments to the Trustee for deposit in the Bond Fund not later than tenth (10^{th}) of each month, commencing January 10, 2012, in an amount equal to one-sixth ($1/6^{th}$) of the interest coming due on the Bonds on the next June 15 and December 15. The Borrower also shall make payments to Trustee for deposit to the Bond Fund not later than the tenth (10^{th}) day of each month, commencing January 10, 2013, in an amount equal to one-twelfth ($1/12^{th}$) of the principal coming due on the Bonds on the next December 15 (including any scheduled mandatory redemption of the Bonds under the Agreement). However, the failure of the Borrower to make such payments to the Bond Fund as herein described shall not constitute a default or Event of Default under the Agreement, so long as the principal and interest on the Bonds is paid when due through drawings on the Letter of Credit, and any amounts paid by the Borrower for deposit to the Bond Fund will be used to reimburse the Bank for drawings on the Letter of Credit. At any time when any principal of the Bonds is overdue, the Borrower shall also have a continuing obligation to pay to the Trustee for deposit in the Bond Fund an amount equal to interest on the overdue principal to the date of acceleration, if any, but interest payments shall not bear interest.

If the Borrower makes payments to the Trustee in anticipation of the redemption of the Bonds, the Trustee shall deposit such payments in the Bond Fund, and the Trustee shall use such amounts, following the direction by the Borrower to optionally redeem the Bonds, or to reimburse the Bank for draws on the Letter of Credit as a result of such redemptions. Promptly after December 15^{th} of each Bond Year, if the amount deposited by the Borrower in the Bond Fund during the preceding Bond Year was in excess of the amount required to be so deposited, the Trustee shall transfer such excess amounts *first* to the Bank to reimburse it for any outstanding draws under the Letter of Credit, *second* to the Trustee and the Issuer, if any amounts are owing to either under the Agreement, and *third* to the Borrower, with the consent of the Bank.

In case, any moneys deposited with the Trustee for the payments of principal of, premium, if any, and interest on any Bond which remain unclaimed for five years, the Trustee may upon written request by an Authorized Officer of the Borrower, pay over such deposited amounts *first* to the Bank to reimburse it for any outstanding draws under the Letter of Credit, and *second* to the Borrower, and thereafter the Trustee and the Issuer shall be released from further liability with respect to such amounts and the owner of such Bond shall be entitled to look only to the Borrower as an unsecured creditor for payment thereof.

The obligation of the Borrower to make payments to the Issuer and the Trustee under the Agreement shall be absolute and unconditional, shall be binding and enforceable in all circumstances whatsoever, shall not be subject to setoff, recoupment or counterclaim, and shall be a general obligation of the Borrower to which the full faith and credit of the Borrower is pledged. (Sections 303, 307 and 308)

Credit Facility Fund

Amounts received by the Trustee from drawings under the Letter of Credit shall be held in trust in the Credit Facility Fund, in a Series A/B Account or a Series C Account, as applicable, separate and apart from all other amounts held by the Trustee. Moneys held in the Credit Facility Fund will remain uninvested and will be used to pay the principal and Purchase Price of, premium, if any, interest on the Bonds. Principal and the Purchase Price of, and premium, if any, and interest on Borrower Bonds and Bank Bonds shall not be paid from drawings under the Letter of Credit.

Bond Purchase Fund

For so long as any Series C Bonds are Outstanding in the Term Rate Mode, the Trustee shall maintain the Bond Purchase Fund and any amounts received from the Remarketing Agent as a result of remarketing the Series C Bonds shall be deposited in such fund and be used to pay the Purchase Price of such remarketed Series C Bonds. Drawings on the Letter of Credit shall not be deposited in the Bond Purchase Fund.

Application of Moneys

If, in addition to moneys drawn on the Letter of Credit, available moneys in the Bond Fund are not sufficient on any day to pay all principal, premium, if any, and interest on the Outstanding Bonds then due or overdue, such moneys shall, after payment of all amounts owing to the Trustee and the Issuer under the Agreement, be applied *first* to the payment of interest, including interest on overdue principal, in the order in which the same became due (pro rata with respect to interest which became due at the same time) and *second* to the payment of principal and redemption premiums, if any, without regard to the order in which the same became due in each case pro rata among Bondowners; provided, however, that amounts drawn on the Letter of Credit shall be applied exclusively to pay interest, premium, if any, and principal on the Bonds in accordance with the Letter of Credit. If the owners of the Bonds have received all payments of principal, premium, if any, and interest that have become due and payable from a draw on the Letter of Credit, the Bank shall be treated as the owner of the Bonds for purposes of applying the provisions of the Agreement described in this paragraph. Whenever moneys are to be applied pursuant to the provisions of the Agreement described in this paragraph, such moneys shall be applied at such times, and from time to time, as the Trustee in its discretion shall determine, having due regard to the amount of such moneys becoming available for such application and the likelihood of additional moneys becoming available for such application in the future. Whenever the Trustee shall exercise such discretion it shall fix the date (which shall be the fifteenth day of a month unless the Trustee shall deem another date more suitable) upon which such application is to be made, and upon such date interest on the amounts of principal paid on such date shall cease to accrue; provided, however, that the interest on any Bonds subject to acceleration shall cease to accrue as of the date of acceleration. Whenever overdue interest is to be paid on the Bonds, the Trustee may establish a special record date as provided in the Agreement. The Trustee shall give such notice as it may deem appropriate of the fixing of any such date and the special record date. When interest or a portion of the principal is to be paid on an overdue Bond, the Trustee may require presentation of the Bond for endorsement of the payment. (Section 306)

Remarketing of Bonds Tendered

While the Series C Bonds are in the Term Rate Mode, the Remarketing Agent shall solicit offers to purchase and use its best efforts to find a purchaser for Series C Bonds required to be tendered on a Tender Date, Bank Bonds and Borrower Bonds, provided that Series C Bonds shall not be remarketed to the Issuer, the Borrower, any guarantor of the Series C Bonds (other than the Bank) or "insiders" of any of them as that term is defined in the United States Bankruptcy Code. Any such purchase shall be made by payment of the Purchase Price in immediately available funds to the Trustee. On the Purchase Date, Series C Bonds remarketed under the Agreement shall be made available by the Trustee to the purchasers thereof and shall be registered in the manner directed by the recipient thereof, provided that such Series C Bonds shall not be delivered unless and until the Trustee has received the Purchase Price therefor. Series C Bonds not remarketed shall be held by the Trustee. Series C Bonds previously purchased with moneys drawn under the Series C Letter of Credit shall not be released by the Trustee upon remarketing unless the Trustee has received written evidence from the Bank that the Series C Letter of Credit has been reinstated as provided in the Agreement. No Series C Bonds shall be remarketed unless the Trustee has received, no later than the Purchase Date, an extension or amendment to the Series C Letter of Credit, as applicable, in the Required Stated Amount and with a Stated Expiration Date not earlier than, in the case of Series 2011C Bonds to be remarketed in the Term Rate Mode, the next Purchase Date, and in the case of Series 2011C Bonds to be remarketed in the Fixed Rate Mode, the final maturity date of the Series 2011C Bonds. (Section 312)

Payment for Purchase of Series C Bonds

The Agreement provides that the Trustee shall draw upon the Series C Letter of Credit the amount necessary to purchase the tendered Series C Bonds for which the Remarketing Agent has not received the Purchase Price. Any such Series C Bonds so purchased with moneys drawn on the Series C Letter of Credit shall be *"Bank Bonds."* If the Remarketing Agent does not deliver to the Trustee proceeds of remarketing sufficient, together with amounts received from draws under the Series C Letter of Credit, to pay in full the Purchase Price of all Series C Bonds due on the Purchase Date, the Trustee will notify the Borrower and the Remarketing Agent of the deficiency, and the Borrower shall pay to the Trustee the amount of the deficiency in immediately available funds. Any Series C Bonds so purchased with moneys furnished by the Borrower shall be *"Borrower Bonds."* If sufficient funds are not available for all Series C Bonds tendered or deemed tendered on any Purchase Date, no purchase shall be consummated. (Section 307)

Covenants of the Borrower

In the Agreement, the Borrower covenants, among other things, that:

(a) the Borrower will not take or omit to take any action if such action or omission (i) would cause the Series B Bonds or the Series C Bonds to be "arbitrage bonds" under Section 148 of the Code, (ii) would cause the Series B Bonds or the Series C Bonds to not meet any of the requirements of Section 149 of the Code, or (iii) would adversely affect the exclusion from gross income of the interest on the Series B Bonds or the Series C Bonds under Section 103 of the Code;

(b) in the acquisition, construction, maintenance, improvement and operation of the Project, the Borrower has complied and will comply in all material respects with all applicable and material building, subdivision, zoning, land use, environmental protection, historical, sanitary and safety laws, rules and regulations, and will not permit any nuisance thereon, except that failure to comply with any law, rule, requirement or regulation shall not be a breach of this covenant so long as the Borrower is diligently and in good faith contesting the validity thereof;

(c) the Borrower will make timely payment of all taxes and assessments and other municipal or governmental charges and all claims and demands for work, labor, services, materials or other objects which, if unpaid, might by law become a lien on the Project or any part thereof; but it shall not be a breach of this covenant if the Borrower fails to pay any such item during any period in which the Borrower is diligently and in good faith contesting the validity thereof; and

(d) the Borrower shall not dissolve or consolidate with or merge into another entity or entities, or permit one or more other entities to consolidate with or merge into it, or change the ownership interests of the Borrower unless the (i) surviving, resulting or transferee entity or entities each has the status and powers granted to the Borrower pursuant to the Ports Enabling Act, (ii) the ownership of the Project by the surviving entity will not adversely affect the exclusion from gross income of the interest on the Series B Bonds or the Series C Bonds under Section 103 of the Code, and (iii) the surviving entity (A) assumes by written agreement with the Issuer and the Trustee of all the obligations of the Borrower under the Agreement, (B) notifies the Issuer and the Trustee of any change in the name of the Borrower, and (C) executes, delivers, registers, records and files such other instruments as the Trustee may reasonably require to confirm, perfect or maintain the security granted under the Agreement. (Sections 902, 903, 904 and 905)

Events of Default

"Event of Default" in the Agreement means any one of the events set forth below and "default" means any Event of Default without regard to any lapse of time or notice:

(a) Any principal or premium, if any, of or interest on any Bond shall not be paid when due, whether at maturity, by acceleration, upon redemption or otherwise, or the Purchase Price of any Series C Bonds shall not be paid as provided in the Agreement.

(b) An act of Bankruptcy of the Bank shall occur and be continuing.

(c) If a request for funding is made on the Letter of Credit in accordance with the formal requirements for making such request, and the Bank fails to fund such request on the day and at or prior to the time required for any reason.

(d) If interest on the Series B Bonds or the Series C Bonds no longer is excludable from the gross income of the owners of such Bonds for federal income tax purposes, as confirmed by an Opinion of Bond Counsel delivered to the Issuer, the Trustee and the Borrower.

No Event of Default described in paragraph (a) shall be deemed to exist under the Agreement to the extent that the amounts due and payable are paid from drawings on the Letter of Credit.

Remedies for Events of Default

If an Event of Default occurs and is continuing, the following remedies are provided for in the Agreement:

(a) ***Acceleration***. If an Event of Default occurs, the Trustee shall give notice by Electronic Means to the Borrower, the Issuer and the Bank, declaring immediately due and payable the principal of the Outstanding Bonds and the accrued interest thereon, whereupon the same shall become immediately due and payable without any further action or notice; provided, however, that upon an Event of Default described in paragraph (d) under the heading "Events of Default," above, only the Series B Bonds or the Series C Bonds, or both, the interest on which is no longer excludable from gross income of the owners of such Bonds for federal tax purposes, shall be subject to acceleration. Upon such declaration by the Trustee, interest shall cease to accrue and the principal so accelerated, together with accrued interest, if any, thereon shall become due and payable, the Trustee shall immediately draw upon the Letter of Credit in an amount that is sufficient to pay the principal and accrued interest, if any, to the acceleration date, on all of the Outstanding Bonds. If, after the principal of the accelerated Bonds has been declared due and payable, all arrears of principal and interest on such Bonds are paid, and the Letter of Credit is reinstated in full on all Outstanding Bonds and is in full force and effect, then, and in every such case, the Bondowners of a majority in aggregate principal amount of the accelerated Outstanding Bonds, by notice to the Issuer and the Trustee, may annul such declaration and its consequences, and such annulment shall be binding upon the Trustee and upon all Bondowners. No such annulment shall extend to or affect any subsequent default or impair any right or remedy consequent thereon.

(b) ***Legal Proceedings***. If any Event of Default has occurred and is continuing, the Trustee may, in its discretion, and upon the written request of the owners of a majority in aggregate principal amount of all Bonds so accelerated and upon receipt of indemnity to its satisfaction shall, in its own name:

(i) By mandamus, or other suit, action or proceeding at law or in equity, enforce all rights of the Bondowners under the Agreement, including the right to require the Issuer to enforce any rights under the Agreement and to require the Issuer to carry out any other provisions of the Agreement for the benefit of the Bondowners and to perform its duties under the Enabling Act;

(ii) Bring suit upon the Bonds;

(iii) By action or suit in equity require the Issuer to account as if it were the trustee of an express trust for the Bondowners; and

(iv) By action or suit in equity enjoin any acts or things which may be unlawful or in violation of the rights of the Bondowners.

(c) ***Rights as a Secured Party***. The Trustee may exercise all of the rights and remedies of a secured party under the UCC. Notice sent by registered or certified mail, postage prepaid, or delivered during business hours, to the Borrower at least ten (10) days before an event under UCC Section 9-504 or any successor provision of law shall constitute reasonable notification of such event. (Section 502(d))

Revenues after Default

After the occurrence of an Event of Default, any funds pledged as security under the Agreement and any other moneys received by the Trustee (other than amounts irrevocably set aside to pay particular Bonds and amounts drawn on the Letter of Credit to pay the principal or redemption price of or the interest on the Bonds) *first* shall be applied, after payment of all charges and disbursements to the Trustee in accordance with the Agreement, to pay any rebate that may be due to the United States Treasury with respect to the Series B Bonds and the Series C Bonds, in accordance with the provisions of the Agreement, and *second* shall be deposited and held in the Bond Fund and applied to debt service on the Bonds, in the order described under the heading "Application of Moneys," above.

Any surplus, after application of the funds as described above, shall be applied *first*, to the reimbursement of the Bank for any payments made by it under the Letter of Credit, and *second*, to the payment of costs and expenses of the Issuer and the Trustee, including counsel fees, incurred in connection with the Event of Default, and any remaining balances shall be paid to the Borrower or the person lawfully entitled to receive the same as a court of competent jurisdiction may direct. (Section 505)

The Letter of Credit; Acceleration

Upon declaration of acceleration of the Bonds, the Trustee shall draw promptly on the Letter of Credit in an amount equal to the aggregate unpaid principal of and premium, if any, and interest on the Bonds to the date of acceleration upon which interest shall cease to accrue. Upon receipt of payment of such a draw, the Trustee shall immediately pay therefrom to the owners of the Bonds the principal and accrued interest due. Notwithstanding the foregoing, the Trustee agrees to draw on the Letter of Credit in accordance with its terms and to accelerate payments under the Bonds, subject to provisions of the Agreement, without asserting any claim for indemnity before taking such actions. (Section 506)

Rights of Bondowners

The Bondowners of a majority in aggregate principal amount of the accelerated Bonds shall have the right, after indemnifying the Trustee, to direct the method and place of conducting all remedial proceedings by the Trustee under the Agreement; provided, that such direction shall not be in conflict with any rule of law or with the Agreement or unduly prejudice the rights of minority Bondowners; and provided further, that unless a Bank Default has occurred and is continuing, the Bank shall exercise all of the rights of the Bondowners under the Agreement. No Bondowner shall have any right to pursue any remedy under the Agreement unless: (i) any payment to it of principal, purchase price or redemption price, or interest on its Bonds has not been paid, or if the interest on any Series B Bond or Series C Bond owned by it is no longer excludable from gross income under the provisions of the Code; (ii) any of its Bonds have been accelerated; (iii) the Trustee shall have been given written notice of an Event of Default by the Bondowner; (iv) the Bondowners of a majority in aggregate principal amount of the Bonds accelerated shall have requested the Trustee, in writing, to exercise the powers hereinabove granted to or pursue such remedy in its or their name or names; and (v) the Trustee shall have been offered indemnity satisfactory to it against costs, expenses and liabilities; and (vi) the Trustee shall have failed to comply with such request within a reasonable time. (Sections 502, 507 and 802)

Subrogation Rights of Bank

In the event the Trustee shall draw under the Letter of Credit in connection with the payment of the principal of, or premium, if any, or interest on the Bonds, and the Bank shall have provided the Trustee with funds pursuant to the Letter of Credit for the payment of the principal of, or premium, if any, or interest on the Bonds, then the Bank shall be subrogated to all rights theretofore possessed under the Agreement by the Trustee and the Bondowners in respect of which such principal, premium, if any, and interest shall have been paid with funds provided by the Bank (to the extent such funds provided by the Bank pursuant to the Letter of Credit shall not have been reimbursed to the Bank). After the payment of any such Outstanding Bonds owned by the Bondowners other than the Bank, any reference in the Agreement to the owners of such Bonds or such Bondowners shall mean the Bank to the extent of its subrogation rights resulting from the payments made pursuant to the Letter of Credit. Notwithstanding any provision contained in the Agreement to the contrary, under no circumstances shall the Issuer's rights, or the Trustee's rights relating to the Trustee, as opposed to rights for the benefit of Bondowners reserved in the Agreement, including, without limitation the right of indemnification or the Issuer's right or the Trustee's right to enforce the same, be subrogated to the Bank. (Section 510)

Rights of the Bank

All consents, approvals and requests required of the Bank under the Agreement shall be deemed not required if a Bank Default has occurred and is continuing. (Section 511)

Performance of Borrower's Obligations

If the Borrower shall fail to observe or perform any of its agreements or obligations under the Agreement with respect to the Project or the maintenance of the tax-exempt status of the Series B Bonds or the Series C Bonds, the Issuer or the Trustee may (but shall have no obligation to) perform the same in its own name or in the Borrower's name and each is irrevocably appointed the Borrower's attorney-in-fact for such purpose. Unless an Event of Default exists, the Issuer or the Trustee, as the case may be, shall give at least five (5) days' written notice to the Borrower before taking action as described under this heading, except that in case of emergency as reasonably determined by the acting party, it may act on lesser notice or give the notice promptly after rather than before taking the action. The reasonable cost of any such action performed by the Trustee or the Issuer shall be paid or reimbursed by the Borrower within thirty (30) days after the Trustee or the Issuer notifies the Borrower of such cost. (Section 512)

Amendments

The Agreement may be amended without the consent of the owners of the Bonds, but upon notice to the Bank, in order to (i) cure any ambiguity, defect or omission that does not materially adversely affect the interests of the Bondowners or the Bank, (ii) grant additional rights or security to the Trustee for the benefit of the Bondowners, (iii) add additional Events of Default that are not inconsistent with the Agreement and which will not materially adversely affect the interests of the Bondowners or the Bank, (iv) qualify the Agreement under the Trust Indenture Act of 1939, as amended, or corresponding provisions of federal laws from time to time in effect, or (v) make any other provisions in regard to matters or questions arising under the Agreement that are not inconsistent with the Agreement and which will not materially adversely affect the interests of the Bondowners or the Bank.

The Agreement may otherwise be amended only with the consent of the registered owners of more than 50% in aggregate principal amount of the Bonds Outstanding; provided, that no amendment shall be made which adversely affects the rights of some but less than all the Bonds Outstanding without the consent of the owners of more than 50% in aggregate principal amount of the Bonds so affected. Notwithstanding the foregoing or any provision of the Agreement to the contrary, no amendment shall be effective to (i) change the principal of, premium, if any, or interest on any Bonds, (ii) change the interest payment dates, maturity dates or purchase or redemption provisions of any Bonds, (iii) reduce the percentage of Bondowners whose consent is required for the amendment of the Agreement, or (iv) modify the lien upon or pledge of the payments and other revenues assigned and pledged under the Agreement (including the Letter of Credit), without the consent, in each case, of the owner of each Bond which would be affected by the action proposed to be taken. When the Trustee determines that the requisite number of consents has been obtained for an amendment which requires Bondowner consent, it shall, within ninety (90) days, file a certificate to that effect in its records and mail notice to the Bondowners. No action or proceeding to invalidate the amendment shall be instituted or maintained unless it is commenced within sixty (60) days after such mailing. A consent to an amendment may be revoked by a written notice given by the Bondowner and received by the Trustee prior to the Trustee's certification that the requisite consents have been obtained. (Section 1001)

Indemnification; Limits of Responsibility; Replacement of the Trustee

The Agreement sets forth certain immunities and limitations of the responsibilities of the Issuer and the Trustee and provides for indemnification of the Issuer and the Trustee against claims relating to the Agreement or the Project.

The Trustee may resign on not less than 30 days' notice given in writing to the Issuer, the Bondowners, the Bank, the Borrower and each Rating Agency, but such resignation shall not take effect until a successor has been appointed and has accepted the appointment. The Trustee may be removed (i) by written notice from the owners of a majority in principal amount of the Outstanding Bonds to the Trustee, the Issuer and the Borrower, (ii) with or without cause by the Borrower if no Event of Default has occurred that has not been waived, or (iii) with or without cause by the Issuer, but no such removal shall take effect until a successor has been appointed and has assumed its duties under the Agreement. (Sections 604 and 605)

Defeasance

When there are in the Bond Fund and/or the Credit Facility Fund sufficient funds, or non callable and non-prepayable Government or Equivalent Obligations in such principal amounts, bearing interest at such rates and with such maturities as will provide, without reinvestment, sufficient funds to pay the principal of and interest on the Bonds in full as and when such amounts become due (as verified in an accountant's report provided by the Borrower at its own expense, if required by the Trustee in order to protect the interest of the Bondowners), and when all the rights under the Agreement of the Issuer (including the right to receive payments under the Agreement), the Bank and the Trustee (including the right to receive payments under the Agreement) have been provided for, the Bondowners will cease to be entitled to any right, benefit or security under the Agreement except the right to receive payment of the funds deposited and held for payment, and other rights which by their nature cannot be satisfied prior to or simultaneously with termination of the lien of the Agreement, the security interests created by the Agreement (except in such funds and investments) shall terminate, the Bonds shall be deemed paid, and the Issuer and the Trustee shall execute and deliver such instruments as may be necessary to discharge the lien and security interests created under the Agreement; provided, however, that (i) all such funds and obligations in the Bond Fund and/or the Credit Facility Fund shall be Eligible Funds, and (ii) if any such Bonds are to be redeemed prior to the maturity, such Bonds shall have been duly called for redemption or irrevocable written instructions for such a call shall have been given to the Trustee. Upon defeasance, the funds and investments required to pay or redeem the Bonds in full shall be irrevocably set aside, and the Letter of Credit will be returned to the Bank. The Trustee shall cause to be mailed to all Bondowners in the manner required for redemption of Bonds under the Agreement, within fifteen (15) days of the conditions under the Agreement being met, a written notice stating that such conditions have been met and that the lien of the Agreement has been discharged, and, if the Bonds are to be redeemed prior to maturity, specifying the date of redemption and the redemption price. Any funds or property held by the Trustee for payment of the Bonds under the Agreement and not required for such payment shall (unless there is an Event of Default under the Agreement, in which case they shall be applied in the manner revenues are applied after default), after satisfaction of all the rights of the Issuer, the Trustee and the Bank and payment of the rebate, if any, due to the United States under Section 148 of the Code, as certified by the Borrower, and upon such indemnification, if any, as the Issuer or the Trustee may reasonably require, be distributed to the Borrower. If Bonds are not presented for final payment when due, and moneys are available in the hands of the Trustee, the Trustee shall, without investment or liability for interest, continue to hold the moneys held for that purpose subject to unclaimed money provisions of the Agreement, and interest shall cease to accrue on the principal amount represented thereby.

Notwithstanding the foregoing, those provisions in the Agreement relating to the maturity of Bonds, interest payments and dates of such payments and the Trustee's remedies with respect to such payments, and provisions relating to exchange, transfer, and registration of Bonds, replacement and cancellation of Bonds, the holding of moneys in trust and the duties of the Trustee in connection with all of the foregoing and the fees, expenses, and indemnities of the Trustee and the Issuer and any obligation of the Borrower to make rebate payments to the United States will remain in full force and effect and will be binding upon the Trustee, the Issuer, the Borrower, and the Bondowners notwithstanding the release and discharge of the Agreement until the Bonds have been actually paid in full. (Section 203)

FORM OF SERIES A/B LETTER OF CREDIT

IRREVOCABLE TRANSFERABLE LETTER OF CREDIT

December 28, 2011

The Bank of New York Mellon, as Trustee
101 Barclay Street - 7W
New York, New York 10286 (the "Beneficiary")

Attention:

OUR REFERENCE:	**LETTER OF CREDIT NO. GDB-2012-01**
APPLICANT:	**PUERTO RICO PORTS AUTHORITY**
STATED AMOUNT:	**U.S. $543,076,007**

Gentlemen:

Government Development Bank for Puerto Rico hereby establishes, at the request and for the account of Puerto Rico Ports Authority (the "Borrower"), pursuant to the Letter of Credit Disbursement and Reimbursement Agreement, dated as of December 1, 2011, between us and the Borrower (as amended or supplemented from time to time pursuant to its terms, the "Letter of Credit Agreement"), in the Beneficiary's favor, our direct pay Irrevocable Transferable Letter of Credit No. GDB-2012-01 (Puerto Rico Ports Authority - AFI Bonds), in the amount of Five Hundred Forty-Three Million Seventy-Six Thousand Seven Dollars (U.S. $543,076,007) (such amount being the "Stated Amount"). The Stated Amount is available to (i) pay principal due with respect to the $340,000,000 original principal amount of the Puerto Rico Infrastructure Financing Authority Revenue Bonds (Ports Authority Project), Series 2011A (Federally Taxable) (the "Series A Bonds") and the $192,830,000 original principal amount of the Puerto Rico Infrastructure Financing Authority Revenue Bonds (Ports Authority Project), Series 2011B (Non-AMT) (the "Series B Bonds," and together with the Series A Bonds, the "Bonds") issued under the Loan and Trust Agreement, dated as of December 1, 2011, among the Puerto Rico Infrastructure Financing Authority, the Borrower and the Beneficiary, as Trustee (the "Trust Agreement"), in an amount not exceeding $532,830,000 in respect of principal, on the dates principal is due in accordance with the Bonds and the Trust Agreement, whether at maturity, upon redemption, by acceleration or otherwise, and (ii) interest accrued on the Bonds pursuant to the Trust Agreement in an amount not exceeding $10,246,007 (calculated as 180 days' accrued interest on the amount in clause (i), at the actual interest rates in effect on the Bonds, on the basis of a 360-day year, and when such interest is due and payable pursuant to the terms of the Bonds and the Trust Agreement. This Letter of Credit is effective immediately and shall expire on the earliest to occur of (a) the payment by us of the full amount available to be drawn hereunder upon a final drawing by the Beneficiary accompanied by the surrender to us of this Letter of Credit for cancellation, (b) 5:00 p.m., Atlantic Standard Time on December 15, 2026 (the "Expiration Date"), or (c) the receipt by us of the Beneficiary's written certificate in the form of

Annex C hereto and the surrender to us by the Beneficiary of this Letter of Credit for cancellation (the earliest to occur of any of the foregoing being the "Termination Date"). This Letter of Credit may not be terminated due to a default by the Borrower under the Letter of Credit Agreement.

We hereby irrevocably authorize the Beneficiary to draw on us, in accordance with the terms and conditions hereof, in one or more drawings by the Beneficiary's draft drawn on us (each such drawing being a "Drawing" and together, the "Drawings") stating on its face "Drawn under Government Development Bank for Puerto Rico Irrevocable Transferable Letter of Credit No. GDB-2012-01 (Puerto Rico Ports Authority - AFI Bonds)" and accompanied by the Beneficiary's written and completed drawing certificate. Each drawing certificate shall be:

(a) in the form of **Annex A** attached hereto (a "Principal Drawing"), if the drawing is made with respect to the payment of the principal due on the Bonds; and

(b) in the form of **Annex B** attached hereto, if the drawing is made with respect to the payment of accrued and unpaid interest due on the Bonds.

The aforesaid certificates shall have all blanks appropriately filled in and shall be signed by the Beneficiary's authorized representative and shall be delivered to us on or before the Termination Date by hand delivery, facsimile, registered mail, overnight courier, or a communication by tested telex at our office at Roberto Sánchez Vilella Government Center, De Diego Avenue, Stop 22, San Juan, Puerto Rico, Attention: Executive Vice President for Financing, Facsimile No.: (787) 723-7388. Any tested telex pursuant to which a Drawing is made hereunder shall be promptly confirmed to us in writing. Each certificate described above shall state therein that it is given by the Beneficiary's duly authorized officer and dated the date such certificate is presented hereunder. The Beneficiary shall use its best efforts to give notice of a Drawing to us by telephone at (787) 722-2525, ext. 5948 and 6047 and by email at Javier.A.Ramos@bgfpr.com; Jesus.M.Garcia@bgfpr.com; Hector.BetancourtNieves@bgfpr.com; on the Business Day preceding the day of such Drawing (but such notice shall not be a condition to drawing hereunder and the Beneficiary shall have no liability for not doing so).

If a Drawing is made by the Beneficiary hereunder at or prior to 10:00 a.m., Atlantic Standard Time, on a Business Day, and, provided that such drawing and the documents presented in connection therewith conform to the terms and conditions hereof, payment shall be made of the amount specified in immediately available funds, no later than 10:00 a.m., Atlantic Standard Time, on the next succeeding Business Day. If a Drawing is made by the Beneficiary hereunder after 10:00 a.m., Atlantic Standard Time, and, provided that such Drawing and the documents presented in connection therewith conform to the terms and conditions hereof, payment shall be made of the amount specified, in immediately available funds, no later than 2:00 p.m., Atlantic Standard Time, on the next succeeding Business Day. No demand for payment may be made after the Termination Date. Payment under this Letter of Credit shall be made by wire transfer of Federal Reserve Bank of New York funds to the Beneficiary's account in a bank on the Federal Reserve wire system, as described in the certificate used to make such Drawing. Drawings under this Letter of Credit will be paid, in accordance with the terms and conditions of this Letter of Credit, with our own funds. As used in this Letter of Credit, the term

"Business Day" shall mean a day other than a Saturday, Sunday or public holiday or the equivalent for banks generally in the cities of New York, New York or San Juan, Puerto Rico.

Only the Beneficiary (or its successor or a transferee as permitted by the terms of this Letter of Credit) may make drawings under this Letter of Credit. Upon payment in full in the manner provided above of the amount specified in a Drawing certificate hereunder, we shall be fully discharged of our obligation under this Letter of Credit with respect to such Drawing certificate.

Multiple Drawings may be made hereunder, provided, subject to the next paragraph hereof, that each Drawing honored by us hereunder shall *pro tanto* reduce the amount available under this Letter of Credit. Payments made in respect of any Drawing (whether or not complying with the terms of this Letter of Credit) which have been transferred to the account specified in the preceding paragraph hereof (or which have been received by the Beneficiary in another account or otherwise) shall reduce by the amount of such payment the amounts which the Beneficiary may draw hereunder notwithstanding any acts or omissions, whether authorized or unauthorized, of the Beneficiary or any of its officers, directors, employees or agents in connection with any Drawing hereunder or the proceeds thereof or otherwise in connection with this Letter of Credit.

Upon delivery by the Beneficiary to us of the Beneficiary's written certificate in the form of **Annex A** hereto, appropriately completed, signed by the Beneficiary's duly authorized officer, and payment by us of the amount specified in such certificate, the Available Amount (as defined below) shall be reduced by the amount of such payment specified in such certificate and by an amount equal to the interest due on such amount (the "corresponding interest"). Such reduction shall be effective as of the next Business Day following the date of delivery of such certificate. If the Available Amount shall be reduced pursuant to this paragraph, we shall have the right to require the Beneficiary to surrender this Letter of Credit to us on or before the tenth (10^{th}) Business Day following the effective date of such reduction of the Available Amount, in order to, at our option, either (a) return this Letter of Credit after endorsing thereon the amounts of such adjustment, or (b) cancel this Letter of Credit and issue to the Beneficiary, in substitution therefor, a substitute irrevocable transferable letter of credit dated the date of such surrender, for an amount equal to the amount to which the Available Amount shall have been so adjusted but otherwise having terms identical to this Letter of Credit. The "Available Amount" shall mean the Stated Amount, less the amount of all prior reductions pursuant to Principal Drawings. Without limiting the foregoing, upon delivery by the Beneficiary to us of the Beneficiary's written certificate in the form of **Annex B** hereto and payment by us of the amount specified in such certificate, the Available Amount automatically shall be reinstated, except for the amount of corresponding interest, if any, as described above.

If any demand for payment made by the Beneficiary under this Letter of Credit does not, in any instance, conform to the terms and conditions of this Letter of Credit, we shall give the Beneficiary immediate notice that such demand for payment was not effected in accordance with the terms and conditions of this Letter of Credit, stating the reasons therefor and that we are holding any documents at the Beneficiary's disposal or are returning the same to the Beneficiary, as it may elect. Upon being notified that such demand for payment made by the Beneficiary under this Letter of Credit was not effected in conformity with this Letter of Credit, the Beneficiary may attempt to correct such nonconforming demand for payment if, and to the extent that, the Beneficiary is entitled (without regard the provisions of this sentence) and able to do so.

The Beneficiary may transfer its rights under this Letter of Credit in its entirety (but not in part) to any transferee who has succeeded to the Beneficiary as Trustee under the Trust Agreement, and such transferred rights may be successively transferred to any subsequent successor transferee under the Trust Agreement. Transfer of the Beneficiary's rights under this Letter of Credit to any such transferee shall be effected upon the presentation to us of this Letter of Credit accompanied by an Instruction to Transfer in the form attached hereto as **Annex D**. The Beneficiary's rights under this Letter of Credit shall automatically transfer to any other entity with which or into which the Beneficiary is merged or with which the Beneficiary is consolidated.

This Letter of Credit sets forth in full our undertaking, and such undertaking shall not in any way be modified, amended, amplified or limited by reference to any document, instrument or agreement referred to herein (including, without limitation, the Trust Agreement), and except the drafts and the certificates referred to herein; and any such reference shall not be deemed to incorporate herein by reference any document, instrument or agreement except for such terms, drafts and certificates.

References to this Letter of Credit include the certificates attached hereto.

This Letter of Credit is issued under and governed by the Uniform Customs and Practice for Documentary Credits (2007 Revision), International Chamber of Commerce Publication No. 600 (the "Uniform Customs"), except to the extent otherwise specifically set forth herein or therein. This Letter of Credit shall be deemed to be a contract made under the laws of Puerto Rico and shall, as to matters not governed by the Uniform Customs, be governed by and construed in accordance with the laws of Puerto Rico.

All notices and other communications to us with respect to this Letter of Credit (other than drafts and certificates with respect to Drawings which shall be delivered as described above), shall be in writing and shall be addressed to us at Roberto Sánchez Vilella Government Center, De Diego Avenue, Stop 22, San Juan, Puerto Rico, Attention: Executive Vice President for Financing, Facsimile No. (787) 723-7288 (or such other office or facsimile number as we shall designate to the Beneficiary in writing) specifically referring thereon to "Government Development Bank for Puerto Rico Irrevocable Transferable Letter of Credit No. GDB-2012-01 (Puerto Rico Ports Authority - AFI Bonds)."

All notices and other communications to the Beneficiary with respect to this Letter of Credit shall be in writing and shall be addressed to the Beneficiary at its address set forth above (or such other office as the Beneficiary shall designate to us in writing). Such notices and other communications shall be sent by registered or certified mail, postage prepaid, and shall be effective upon receipt or by tested facsimile to the following number: 787-728-6835, Attn: Jesús M. Garcia and Héctor Betancourt Nieves. Copies of notices and other communications to us also shall be sent by electronic mail to Javier.A.Ramos@bgfpr.com; Jesus.M.Garcia@bgfpr.com; and Hector.BetancourtNieves@bgfpr.com.

Very truly yours,

GOVERNMENT DEVELOPMENT BANK
FOR PUERTO RICO

By:_______________________________________
José Otero-Freiría
Executive Vice President for Financing

ANNEX A
TO
IRREVOCABLE TRANSFERABLE LETTER OF CREDIT NO. 2012-01

Government Development Bank for Puerto Rico
Roberto Sánchez Vilella Government Center
De Diego Avenue, Stop 22
San Juan, Puerto Rico 00940

Attention: Executive Vice President for Financing

Re: **Principal/Redemption Drawing Certificate** - Drawn under Government Development Bank for Puerto Rico Irrevocable Transferable Letter of Credit No. 2012-01 (Puerto Rico Ports Authority - AFI Bonds)

Gentlemen:

______________, as Trustee (the "Beneficiary") hereby certifies to Government Development Bank for Puerto Rico (the "Bank") with reference to Irrevocable Transferable Letter of Credit No. 2012-01 (Puerto Rico Ports Authority - AFI Bonds) (the "Letter of Credit," with capitalized terms used herein and not otherwise defined herein having their respective meanings set forth in the Letter of Credit) that:

1. The Beneficiary is making a demand for payment under the Letter of Credit in the amount of $___________ to be applied to the payment of principal due on the Bonds [, as a result of the redemption of Bonds pursuant to Section __ of the Trust Agreement].

2. The amount of this demand for payment was computed in accordance with the terms and conditions of the Bonds and is made in accordance with the provisions of the Trust Agreement.

3. After application of the above payment, the aggregate amount of principal outstanding on the Bonds is $___________.

4. Payment of the amount hereby requested shall be made to the Beneficiary's account as follows:

[WIRE INSTRUCTIONS]

5. The amount hereby demanded does not exceed the Available Amount under the Letter of Credit nor the amount due and payable on the Bonds.

6. Effective on ____________ [insert date hereof], and subject to your payment of this Drawing, the portion of the Available Amount of the Letter of Credit shall be reduced to

$___________, with $___________ available for the payment of principal on the Bonds and $___________ available for the payment of accrued interest on the Bonds.

7. Following the reduction specified in paragraph 6 above, the Available Amount of the Letter of Credit shall not be less than the outstanding aggregate principal amount of the Bonds, plus 180 days' interest due thereon at the actual interest rates in effect on the Outstanding Bonds, calculated on the basis of a year of a 360-day year, consisting of twelve 30-day months.

8. Upon receipt by the Beneficiary of the amount demanded hereby, (a) the Beneficiary will apply the same directly to the payment of the appropriate amount of principal owing and due on the Bonds, and (b) no portion of said amount shall be applied by the Beneficiary for any other purpose.

IN WITNESS WHEREOF, the undersigned has executed and delivered this Certificate as of the day ____ of _________, 20__.

_______________________, as Trustee

By:_____________________________
Authorized Representative

ANNEX B
TO
IRREVOCABLE TRANSFERABLE LETTER OF CREDIT NO. 2012-01

Government Development Bank for Puerto Rico
Roberto Sánchez Vilella Government Center
De Diego Avenue, Stop 22
San Juan, Puerto Rico 00940

Attention: Executive Vice President for Financing

Re: **Interest Drawing Certificate** - Drawn under Government Development Bank for Puerto Rico Irrevocable Transferable Letter of Credit No. 2012-01 (Puerto Rico Ports Authority AFI Bonds)

Gentlemen:

_______________________, as Trustee (the "Beneficiary") hereby certifies to Government Development Bank for Puerto Rico (the "Bank") with reference to Irrevocable Transferable Letter of Credit No. 2012-01 (Puerto Rico Ports Authority - AFI Bonds) (the "Letter of Credit," with capitalized terms used herein and not otherwise defined herein having their respective meanings set forth in the Letter of Credit) that:

1. The Beneficiary is making a demand for payment under the Letter of Credit in the amount of $___________ to be applied to the payment of interest due on the Bonds[, as a result of the redemption of Bonds pursuant to Section __ of the Trust Agreement].

2. The amount of this demand for payment was computed in accordance with the terms and conditions of the Bonds and is made in accordance with the provisions of the Trust Agreement.

3. The amount hereby demanded does not exceed the Available Amount under the Letter of Credit for this drawing.

4. Payment of the amount hereby requested shall be made to the Beneficiary account as follows:

[WIRE INSTRUCTIONS]

5. Upon receipt by the Beneficiary of the amount demanded hereby, (a) the Beneficiary will apply the same directly to the payment when due of interest owing and due on the Bonds, and (b) no portion of said amount shall be applied by the Beneficiary for any other purpose.

IN WITNESS WHEREOF, the undersigned has executed and delivered this Certificate as of the ____ day of________, 20__.

____________________________, as Trustee

By: __________________________________
Authorized Representative

ANNEX C
TO
IRREVOCABLE TRANSFERABLE LETTER OF CREDIT NO. 2012-01

[Letterhead of Beneficiary]

Government Development Bank for Puerto Rico
Roberto Sánchez Vilella Government Center
De Diego Avenue, Stop 22
San Juan, Puerto Rico 00940

Attention: Executive Vice President for Financing

CERTIFICATE FOR CANCELLATION OF LETTER OF CREDIT

The undersigned, acting by its duly authorized officer, hereby certifies to Government Development Bank for Puerto Rico, with reference to Irrevocable Transferable Letter of Credit No. 2012-01 (Puerto Rico Ports Authority - AFI Bonds) (the "Letter of Credit," with any capitalized term used herein and not defined having its respective meaning as set forth in the Letter of Credit) issued by Government Development Bank for Puerto Rico, in favor of the Beneficiary, that there are no Bonds Outstanding under the Trust Agreement. The Letter of Credit, which accompanies this Certificate, is hereby surrendered for cancellation.

IN WITNESS WHEREOF, the Beneficiary has executed and delivered this Certificate as of the _____ day of ______________ 20__.

[NAME OF BENEFICIARY]

By:__________________________
Name:
Title:

SIGNATURE AUTHENTICATED

____
(Bank)

____
(Authorized Signature)

ANNEX D
TO
IRREVOCABLE TRANSFERABLE LETTER OF CREDIT NO. 2012-01

INSTRUCTION TO TRANSFER

[Date]

Government Development Bank for Puerto Rico
Roberto Sánchez Vilella Government Center
De Diego Avenue, Stop 22
San Juan, Puerto Rico 00940

Attention: Executive Vice President for Financing

Government Development Bank for Puerto Rico
Irrevocable Transferable Letter of Credit No. 2012-01
(Puerto Rico Ports Authority - AFI Bonds)

Gentlemen:

For value received, the undersigned beneficiary hereby irrevocably transfers to:

____
[Name of Transferee]

____
[Address of Transferee]

all rights of the undersigned beneficiary under the above-referenced Letter of Credit. The transferee is the successor Trustee under the Trust Agreement referred to in the first paragraph of the above-referenced Letter of Credit.

By this transfer, all rights of the undersigned beneficiary in the above-referenced Letter of Credit are transferred to the transferee and the transferee shall hereafter have the sole rights as beneficiary thereof.

The above-referenced Letter of Credit is returned herewith, and we ask that this transfer be effective and that you issue a new irrevocable transferable letter of credit in favor of the transferee substantially identical to such Letter of Credit.

Very truly yours,

[NAME OF BENEFICIARY]

FORM OF SERIES C LETTER OF CREDIT

IRREVOCABLE TRANSFERABLE LETTER OF CREDIT

December 28, 2011

The Bank of New York Mellon, as Trustee
101 Barclay Street - 7W
New York, New York 10286 (the "Beneficiary")

Attention:

OUR REFERENCE: **LETTER OF CREDIT NO. GDB-2012-02**
APPLICANT: **PUERTO RICO PORTS AUTHORITY**
STATED AMOUNT: **U.S. $ 138,309,794**

Gentlemen:

Government Development Bank for Puerto Rico hereby establishes, at the request and for the account of Puerto Rico Ports Authority (the "Borrower"), pursuant to the Letter of Credit Disbursement and Reimbursement Agreement, dated as of December 1, 2011, between us and the Borrower (as amended or supplemented from time to time pursuant to its terms, the "Letter of Credit Agreement"), in the Beneficiary's favor, our direct pay Irrevocable Transferable Letter of Credit No. GDB-2012-02 (Puerto Rico Ports Authority - AFI Bonds), in the amount of One Hundred Thirty-Eight Million Three Hundred Nine Thousand Seven Hundred Ninety-Four Dollars (U.S. $138,309,794) (such amount being the "Stated Amount"). The Stated Amount is available to (i) pay principal due or the portion of the purchase price equal to the principal amount with respect to the $136,385,000 original principal amount of the Puerto Rico Infrastructure Financing Authority Revenue Bonds (Ports Authority Project), Series 2011C (AMT) (the "Bonds") issued under the Loan and Trust Agreement, dated as of December 1, 2011, among the Puerto Rico Infrastructure Financing Authority, the Borrower and the Beneficiary, as Trustee (the "Trust Agreement"), in an amount not exceeding $136,385,000 in respect of principal on the dates principal is due or the portion of the purchase price equal to the principal amount of the Bonds, in accordance with the Bonds and the Trust Agreement, whether at maturity, upon redemption, upon tender for purchase, by acceleration or otherwise, and (ii) interest accrued on the Bonds or the portion of the purchase price equal to interest accrued on the Bonds, pursuant to the Trust Agreement in an amount not exceeding $1,924,794 (calculated as 180 days' accrued interest on the amount in clause (i), at the current Term Rate in effect on the Bonds, on the basis of a 360-day year, and when such interest is due and payable pursuant to the terms of the Bonds and the Trust Agreement. This Letter of Credit is effective immediately and shall expire on the earliest to occur of (a) the payment by us of the full amount available to be drawn hereunder upon a final drawing by the Beneficiary accompanied by the surrender to us of this Letter of Credit for cancellation, (b) 5:00 p.m., Atlantic Standard Time on December 16, 2013 (the "Expiration Date"), or (c) the receipt by us of the Beneficiary's written certificate in the form of **Annex D** hereto and the surrender to us by the Beneficiary of this Letter of Credit for cancellation (the earliest to occur of any of the foregoing being the "Termination Date"). This Letter of Credit may not be terminated due to a default by the Borrower under the Letter of Credit Agreement.

We hereby irrevocably authorize the Beneficiary to draw on us, in accordance with the terms and conditions hereof, in one or more drawings by the Beneficiary's draft drawn on us (each such drawing being a "Drawing" and together, the "Drawings") stating on its face "Drawn under Government Development Bank for Puerto Rico Irrevocable Transferable Letter of Credit No. GDB-2012-02 (Puerto Rico Ports Authority - AFI Bonds)" and accompanied by the Beneficiary's written and completed drawing certificate. Each drawing certificate shall be:

(a) in the form of **Annex A** attached hereto (a "Principal Drawing"), if the drawing is made with respect to the payment of the principal due on the Bonds;

(b) in the form of **Annex B** attached hereto (a "Tender Drawing"), if the drawing is made with respect to the payment of the purchase price of Bonds tendered for purchase which have not been successfully remarketed or for which the purchase price has not been received by the Beneficiary by 2:00 P.M. on the Business Day next preceding the purchase date, provided that in the event the purchase date coincides with an Interest Payment Date, the Tender Drawing shall not include interest on the Bonds (which interest is payable pursuant to an Interest Drawing as set forth below); and

(c) in the form of **Annex C** attached hereto (an "Interest Drawing"), if the drawing is made with respect to the payment of accrued and unpaid interest due on the Bonds.

The aforesaid certificates shall have all blanks appropriately filled in and shall be signed by the Beneficiary's authorized representative and shall be delivered to us on or before the Termination Date by hand delivery, facsimile, registered mail, overnight courier, or a communication by tested telex at our office at Roberto Sánchez Vilella Government Center, De Diego Avenue, Stop 22, San Juan, Puerto Rico, Attention: Executive Vice President for Financing, Facsimile No.: (787) 723-7388. Any tested telex pursuant to which a Drawing is made hereunder shall be promptly confirmed to us in writing. Each certificate described above shall state therein that it is given by the Beneficiary's duly authorized officer and dated the date such certificate is presented hereunder. The Beneficiary shall use its best efforts to give notice of a Drawing to us by telephone at (787) 722-2525, ext. 5948 and 6047 and by email at Javier.A.Ramos@bgfpr.com; Jesus.M.Garcia@bgfpr.com; Hector.BetancourtNieves@bgfpr.com; on the Business Day preceding the day of such Drawing (but such notice shall not be a condition to drawing hereunder and the Beneficiary shall have no liability for not doing so).

If a Drawing (other than a Tender Drawing) is made by the Beneficiary hereunder at or prior to 10:00 a.m., Atlantic Standard Time, on a Business Day, and, provided that such drawing and the documents presented in connection therewith conform to the terms and conditions hereof, payment shall be made of the amount specified in immediately available funds, no later than 10:00 a.m., Atlantic Standard Time, on the next succeeding Business Day. If a Drawing (other than a Tender Drawing) is made by the Beneficiary hereunder after 10:00 a.m., Atlantic Standard Time, and, provided that such Drawing and the documents presented in connection therewith conform to the terms and conditions hereof, payment shall be made of the amount specified, in immediately available funds, no later than 2:00 p.m., Atlantic Standard Time, on the next succeeding Business Day.

If a Tender Drawing is made by the Beneficiary hereunder at or prior to 10:00 a.m., Atlantic Standard Time, on a Business Day, and, provided that such drawing and the documents presented in connection therewith conform to the terms and conditions hereof, payment shall be made of the amount specified in immediately available funds, no later than 2:00 p.m., Atlantic Standard Time, on the same Business Day. If a Tender Drawing is made by the Beneficiary hereunder after 10:00 a.m., Atlantic Standard Time, and, provided that such Drawing and the documents presented in connection therewith conform to the terms and conditions hereof, payment shall be made of the amount specified, in immediately available funds, no later than 10:00 a.m., Atlantic Standard Time, on the next succeeding Business Day.

No demand for payment may be made after the Termination Date. Payment under this Letter of Credit shall be made by wire transfer of Federal Reserve Bank of New York funds to the Beneficiary's account in a bank on the Federal Reserve wire system, as described in the certificate used to make such Drawing. Drawings under this Letter of Credit will be paid, in accordance with the terms and conditions of this Letter of Credit, with our own funds. As used in this Letter of Credit, the term "Business Day" shall mean a day other than a Saturday, Sunday or public holiday or the equivalent for banks generally in the cities of New York, New York or San Juan, Puerto Rico.

Only the Beneficiary (or its successor or a transferee as permitted by the terms of this Letter of Credit) may make drawings under this Letter of Credit. Upon payment in full in the manner provided above of the amount specified in a Drawing certificate hereunder, we shall be fully discharged of our obligation under this Letter of Credit with respect to such Drawing certificate.

Multiple Drawings may be made hereunder, provided, subject to the following paragraphs, that each Drawing honored by us hereunder shall *pro tanto* reduce the amount available under this Letter of Credit. Payments made in respect of any Drawing (whether or not complying with the terms of this Letter of Credit) which have been transferred to the account specified in the preceding paragraph hereof (or which have been received by the Beneficiary in another account or otherwise) shall reduce by the amount of such payment the amounts which the Beneficiary may draw hereunder notwithstanding any acts or omissions, whether authorized or unauthorized, of the Beneficiary or any of its officers, directors, employees or agents in connection with any Drawing hereunder or the proceeds thereof or otherwise in connection with this Letter of Credit.

Upon delivery by the Beneficiary to us of the Beneficiary's written certificate in the form of **Annex A** hereto, appropriately completed, signed by the Beneficiary's duly authorized officer, and payment by us of the amount specified in such certificate, the Available Amount (as defined below) shall be reduced by the amount of such payment specified in such certificate and by an amount equal to the interest due on such amount (the "corresponding interest"). Such reduction shall be effective as of the next Business Day following the date of delivery of such certificate. If the Available Amount shall be reduced pursuant to this paragraph, we shall have the right to require the Beneficiary to surrender this Letter of Credit to us on or before the tenth (10^{th}) Business Day following the effective date of such reduction of the Available Amount, in order to, at our option, either (a) return this Letter of Credit after endorsing thereon the amounts of such adjustment, or (b) cancel this Letter of Credit and issue to the Beneficiary, in substitution therefor, a substitute irrevocable transferable letter of credit dated the date of such surrender, for an amount equal to the amount to which the Available Amount shall have been so adjusted but otherwise having terms identical to this Letter of Credit.

Upon delivery by the Beneficiary to us of the Beneficiary's written certificate in the form of **Annex B** hereto, appropriately completed, signed by the Beneficiary's duly authorized officer, and payment by us of the amount specified in such certificate, the Available Amount (as defined below) shall be reduced by the amount of such payment specified in such certificate plus the amount of corresponding interest. Such reduction shall be effective as of the next Business Day following the date of delivery of such certificate. In the event of the remarketing of Bonds (or portions thereof) previously purchased with the proceeds of a Tender Drawing, the amount available to be drawn hereunder will be automatically reinstated concurrently upon the Beneficiary providing a certificate in the form of **Annex F** hereto to us and when and to the extent that we are reimbursed for any amount drawn hereunder pursuant to such Tender Drawing.

The "<u>Available Amount</u>" shall mean the Stated Amount, less the amount of all prior reductions pursuant to Principal Drawings or Tender Drawings, plus the amount of any reinstatements with respect to Tender Drawings as provided above. Without limiting the foregoing, upon delivery by the Beneficiary to us of the Beneficiary's written certificate in the form of **Annex C** hereto and payment by us of the amount specified in such certificate, the Available Amount automatically shall be reinstated, except for the amount of corresponding interest, if any, as described above.

If any demand for payment made by the Beneficiary under this Letter of Credit does not, in any instance, conform to the terms and conditions of this Letter of Credit, we shall give the Beneficiary immediate notice that such demand for payment was not effected in accordance with the terms and conditions of this Letter of Credit, stating the reasons therefor and that we are holding any documents at the Beneficiary's disposal or are returning the same to the Beneficiary, as it may elect. Upon being notified that such demand for payment made by the Beneficiary under this Letter of Credit was not effected in conformity with this Letter of Credit, the Beneficiary may attempt to correct such nonconforming demand for payment if, and to the extent that, the Beneficiary is entitled (without regard the provisions of this sentence) and able to do so.

The Beneficiary may transfer its rights under this Letter of Credit in its entirety (but not in part) to any transferee who has succeeded to the Beneficiary as Trustee under the Trust Agreement, and such transferred rights may be successively transferred to any subsequent successor transferee under the Trust Agreement. Transfer of the Beneficiary's rights under this Letter of Credit to any such transferee shall be effected upon the presentation to us of this Letter of Credit accompanied by an Instruction to Transfer in the form attached hereto as **Annex E**. The

Beneficiary's rights under this Letter of Credit shall automatically transfer to any other entity with which or into which the Beneficiary is merged or with which the Beneficiary is consolidated.

This Letter of Credit sets forth in full our undertaking, and such undertaking shall not in any way be modified, amended, amplified or limited by reference to any document, instrument or agreement referred to herein (including, without limitation, the Trust Agreement), and except the drafts and the certificates referred to herein; and any such reference shall not be deemed to incorporate herein by reference any document, instrument or agreement except for such terms, drafts and certificates.

References to this Letter of Credit include the certificates attached hereto.

This Letter of Credit is issued under and governed by the Uniform Customs and Practice for Documentary Credits (2007 Revision), International Chamber of Commerce Publication No. 600 (the "Uniform Customs"), except to the extent otherwise specifically set forth herein or therein. This Letter of Credit shall be deemed to be a contract made under the laws of Puerto Rico and shall, as to matters not governed by the Uniform Customs, be governed by and construed in accordance with the laws of Puerto Rico.

All notices and other communications to us with respect to this Letter of Credit (other than drafts and certificates with respect to Drawings which shall be delivered as described above), shall be in writing and shall be addressed to us at Roberto Sánchez Vilella Government Center, De Diego Avenue, Stop 22, San Juan, Puerto Rico, Attention: Executive Vice President for Financing, Facsimile No. (787) 723-7288 (or such other office or facsimile number as we shall designate to the Beneficiary in writing) specifically referring thereon to "Government Development Bank for Puerto Rico Irrevocable Transferable Letter of Credit No. GDB-2012-02 (Puerto Rico Ports Authority - AFI Bonds)."

All notices and other communications to the Beneficiary with respect to this Letter of Credit shall be in writing and shall be addressed to the Beneficiary at its address set forth above (or such other office as the Beneficiary shall designate to us in writing). Such notices and other communications shall be sent by registered or certified mail, postage prepaid, and shall be effective upon receipt or by tested facsimile to the following number: 787-728-6835, Attn: Jesús M. Garcia and Héctor Betancourt Nieves. Copies of notices and other communications to us also shall be sent by electronic mail to Javier.A.Ramos@bgfpr.com; Jesus.M.Garcia@bgfpr.com; and Hector.BetancourtNieves@bgfpr.com.

Very truly yours,

GOVERNMENT DEVELOPMENT BANK
FOR PUERTO RICO

By:______________________________________
José Otero-Freiría
Executive Vice President for Financing

ANNEX A
TO
IRREVOCABLE TRANSFERABLE LETTER OF CREDIT NO. 2012-02

Government Development Bank for Puerto Rico
Roberto Sánchez Vilella Government Center
De Diego Avenue, Stop 22
San Juan, Puerto Rico 00940

Attention: Executive Vice President for Financing

Re: **Principal/Redemption Drawing Certificate** - Drawn under Government Development Bank for Puerto Rico Irrevocable Transferable Letter of Credit No. 2012-02 (Puerto Rico Ports Authority - AFI Bonds)

Gentlemen:

______________, as Trustee (the "Beneficiary") hereby certifies to Government Development Bank for Puerto Rico (the "Bank") with reference to Irrevocable Transferable Letter of Credit No. 2012-02 (Puerto Rico Ports Authority - AFI Bonds) (the "Letter of Credit," with capitalized terms used herein and not otherwise defined herein having their respective meanings set forth in the Letter of Credit) that:

1. The Beneficiary is making a demand for payment under the Letter of Credit in the amount of $___________ to be applied to the payment of principal due on the Bonds [, as a result of the redemption of Bonds pursuant to Section __ of the Trust Agreement].

2. The amount of this demand for payment was computed in accordance with the terms and conditions of the Bonds and is made in accordance with the provisions of the Trust Agreement.

3. After application of the above payment, the aggregate amount of principal outstanding on the Bonds is $___________.

4. Payment of the amount hereby requested shall be made to the Beneficiary's account as follows:

[WIRE INSTRUCTIONS]

5. The amount hereby demanded does not exceed the Available Amount under the Letter of Credit nor the amount due and payable on the Bonds.

6. Effective on ____________ [insert date hereof], and subject to your payment of this Drawing, the portion of the Available Amount of the Letter of Credit shall be reduced to

$___________, with $___________ available for the payment of principal on the Bonds and $___________ available for the payment of accrued interest on the Bonds.

7. Following the reduction specified in paragraph 6 above, the Available Amount of the Letter of Credit shall not be less than the outstanding aggregate principal amount of the Bonds, plus 180 days' interest due thereon at the actual interest rates in effect on the Outstanding Bonds, calculated on the basis of a year of a 360-day year, consisting of twelve 30-day months.

8. Upon receipt by the Beneficiary of the amount demanded hereby, (a) the Beneficiary will apply the same directly to the payment of the appropriate amount of principal owing and due on the Bonds, and (b) no portion of said amount shall be applied by the Beneficiary for any other purpose.

IN WITNESS WHEREOF, the undersigned has executed and delivered this Certificate as of the day ____ of _________, 20__.

_______________________, as Trustee

By:_____________________________
Authorized Representative

ANNEX B
TO
IRREVOCABLE TRANSFERABLE LETTER OF CREDIT NO. 2012-02

Government Development Bank for Puerto Rico
Roberto Sánchez Vilella Government Center
De Diego Avenue, Stop 22
San Juan, Puerto Rico 00940

Attention: Executive Vice President for Financing

Re: **Tender Drawing Certificate** - Drawn under Government Development Bank for Puerto Rico Irrevocable Transferable Letter of Credit No. 2012-02 (Puerto Rico Ports Authority - AFI Bonds)

Gentlemen:

______________, as Trustee (the "Beneficiary") hereby certifies to Government Development Bank for Puerto Rico (the "Bank") with reference to Irrevocable Transferable Letter of Credit No. 2012-02 (Puerto Rico Ports Authority - AFI Bonds) (the "Letter of Credit," with capitalized terms used herein and not otherwise defined herein having their respective meanings set forth in the Letter of Credit) that:

l. The Beneficiary is making a demand for payment under the Letter of Credit in the amount of $___________ to be applied to the payment of the purchase price of the Bonds, as a result of the tender of Bonds pursuant to Section 311 of the Trust Agreement.

2. The amount of this demand for payment was computed in accordance with the terms and conditions of the Bonds and is made in accordance with the provisions of the Trust Agreement.

3. Payment of the amount hereby requested shall be made to the Beneficiary's account as follows:

[WIRE INSTRUCTIONS]

4. The amount hereby demanded does not exceed the Available Amount under the Letter of Credit nor the amount due and payable on the Bonds.

5. Effective on ____________ [insert date hereof], and subject to your payment of this Drawing, the portion of the Available Amount of the Letter of Credit shall be reduced to $___________, with $___________ available for the payment of the purchase price of the Bonds and $___________ available for the payment of accrued interest on the Bonds.

6. Following the reduction specified in paragraph 5 above, the Available Amount of the Letter of Credit shall not be less than the outstanding aggregate principal amount of the Bonds, plus 180 days' interest due thereon at the actual interest rates in effect on the Outstanding Bonds, calculated on the basis of a year of a 360-day years.

7. Upon receipt by the Beneficiary of the amount demanded hereby, (a) the Beneficiary will apply the same directly to the payment of the appropriate amount of the purchase price of Bonds to be tendered for purchase, and (b) no portion of said amount shall be applied by the Beneficiary for any other purpose.

IN WITNESS WHEREOF, the undersigned has executed and delivered this Certificate as of the day ____ of _________, 20__.

________________________, as Trustee

By:______________________________
Authorized Representative

ANNEX C
TO
IRREVOCABLE TRANSFERABLE LETTER OF CREDIT NO. 2012-02

Government Development Bank for Puerto Rico
Roberto Sánchez Vilella Government Center
De Diego Avenue, Stop 22
San Juan, Puerto Rico 00940

Attention: Executive Vice President for Financing

Re: **Interest Drawing Certificate** - Drawn under Government Development Bank for Puerto Rico Irrevocable Transferable Letter of Credit No. 2012-02 (Puerto Rico Ports Authority AFI Bonds)

Gentlemen:

________________________, as Trustee (the "Beneficiary") hereby certifies to Government Development Bank for Puerto Rico (the "Bank") with reference to Irrevocable Transferable Letter of Credit No. 2012-02 (Puerto Rico Ports Authority - AFI Bonds) (the "Letter of Credit," with capitalized terms used herein and not otherwise defined herein having their respective meanings set forth in the Letter of Credit) that:

1. The Beneficiary is making a demand for payment under the Letter of Credit in the amount of $___________ to be applied to the payment of interest due on the Bonds[, as a result of the redemption of Bonds pursuant to Section 309(__) of the Trust Agreement].

2. The amount of this demand for payment was computed in accordance with the terms and conditions of the Bonds and is made in accordance with the provisions of the Trust Agreement.

3. The amount hereby demanded does not exceed the Available Amount under the Letter of Credit for this drawing.

4. Payment of the amount hereby requested shall be made to the Beneficiary account as follows:

[WIRE INSTRUCTIONS]

5. Upon receipt by the Beneficiary of the amount demanded hereby, (a) the Beneficiary will apply the same directly to the payment when due of interest owing and due on the Bonds, and (b) no portion of said amount shall be applied by the Beneficiary for any other purpose.

IN WITNESS WHEREOF, the undersigned has executed and delivered this Certificate as of the ____ day of________, 20__.

____________________________, as Trustee

By: __________________________________
Authorized Representative

ANNEX D
TO
IRREVOCABLE TRANSFERABLE LETTER OF CREDIT NO. 2012-02

[Letterhead of Beneficiary]

Government Development Bank for Puerto Rico
Roberto Sánchez Vilella Government Center
De Diego Avenue, Stop 22
San Juan, Puerto Rico 00940

Attention: Executive Vice President for Financing

CERTIFICATE FOR CANCELLATION OF LETTER OF CREDIT

The undersigned, acting by its duly authorized officer, hereby certifies to Government Development Bank for Puerto Rico, with reference to Irrevocable Transferable Letter of Credit No. 2012-02 (Puerto Rico Ports Authority - AFI Bonds) (the "Letter of Credit," with any capitalized term used herein and not defined having its respective meaning as set forth in the Letter of Credit) issued by Government Development Bank for Puerto Rico, in favor of the Beneficiary, that there are no Bonds Outstanding under the Trust Agreement. The Letter of Credit, which accompanies this Certificate, is hereby surrendered for cancellation.

IN WITNESS WHEREOF, the Beneficiary has executed and delivered this Certificate as of the _____ day of ______________ 20__.

[NAME OF BENEFICIARY]

By:__________________________
Name:
Title:

SIGNATURE AUTHENTICATED

____
(Bank)

____
(Authorized Signature)

ANNEX E
TO
IRREVOCABLE TRANSFERABLE LETTER OF CREDIT NO. 2012-02 _

INSTRUCTION TO TRANSFER

[Date]

Government Development Bank for Puerto Rico
Roberto Sánchez Vilella Government Center
De Diego Avenue, Stop 22
San Juan, Puerto Rico 00940

Attention: Executive Vice President for Financing

Government Development Bank for Puerto Rico
Irrevocable Transferable Letter of Credit No. 2012-02
(Puerto Rico Ports Authority - AFI Bonds)

Gentlemen:

For value received, the undersigned beneficiary hereby irrevocably transfers to:

____
[Name of Transferee]

____
[Address of Transferee]

all rights of the undersigned beneficiary under the above-referenced Letter of Credit. The transferee is the successor Trustee under the Trust Agreement referred to in the first paragraph of the above-referenced Letter of Credit.

By this transfer, all rights of the undersigned beneficiary in the above-referenced Letter of Credit are transferred to the transferee and the transferee shall hereafter have the sole rights as beneficiary thereof.

The above-referenced Letter of Credit is returned herewith, and we ask that this transfer be effective and that you issue a new irrevocable transferable letter of credit in favor of the transferee substantially identical to such Letter of Credit.

Very truly yours,

[NAME OF BENEFICIARY]

ANNEX F
TO
IRREVOCABLE TRANSFERABLE LETTER OF CREDIT NO. 2012-02

Government Development Bank for Puerto Rico
Roberto Sánchez Vilella Government Center
De Diego Avenue, Stop 22
San Juan, Puerto Rico 00940

Attention: Letter of Credit Department

Re: **Notice of Remarketing** - Irrevocable Transferable Letter of Credit No. 2012-02 (Puerto Rico Ports Authority - AFI Bonds)

Gentlemen:

The undersigned, a duly authorized officer of ______________, as Trustee (the "Beneficiary") hereby certifies to Government Development Bank for Puerto Rico (the "Bank") with reference to Irrevocable Transferable Letter of Credit No. 2012-02 (Puerto Rico Ports Authority - AFI Bonds) (the "Letter of Credit," with capitalized terms used herein and not otherwise defined herein having their respective meanings set forth in the Letter of Credit) that:

1. ____________________ is the Remarketing Agent under the Trust Agreement for the holders of the Bonds.

2. The Beneficiary has been advised by the Remarketing Agent that the amount of $____________ paid to Government Development Bank for Puerto Rico ("GDB") today by the Remarketing Agent is a payment made to reimburse GDB, pursuant to the Reimbursement Agreement, for amounts drawn under the Letter of Credit pursuant to a Tender Drawing.

3. $___________ of the amount referred to in paragraph 2 represents the aggregate principal amount of the Bonds resold or to be resold and $___________ of the amount referred to in paragraph 2 represents accrued and unpaid interest on such Bonds.

IN WITNESS WHEREOF, the undersigned has executed and delivered this Certificate as of the day ____ of _________, 20__.

________________________, as Trustee

By:______________________________
Authorized Representative

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SUMMARY OF CERTAIN PROVISIONS OF THE REIMBURSEMENT AGREEMENT

The following description is a brief summary prepared by Greenberg Traurig, LLP, special counsel to the Bank, of certain provisions of the Letter of Credit Disbursement and Reimbursement Agreement (the "Reimbursement Agreement"), dated as of December 1, 2011, between the Borrower and the Bank. This summary does not purport to be a complete description or restatement of the material provisions of the Reimbursement Agreement. Investors should obtain and review a copy of the Reimbursement Agreement in order to understand all of the terms of that document. See Appendix A for the definitions of terms used in this Appendix D and not otherwise defined herein.

General

The Reimbursement Agreement provides that the Bank shall issue an irrevocable transferable direct-pay letter of credit securing the Series A Bonds and the Series B Bonds (the "Series A/B Letter of Credit") and an irrevocable transferable direct-pay letter of credit securing the Series C Bonds (the "Series C Letter of Credit," and together with the Series A/B Letter of Credit, singly and collectively, the "Letter of Credit"), subject to the terms and conditions of the Reimbursement Agreement. The Series A/B Letter of Credit will expire on the earlier of (i) December 15, 2026, (ii) the date on which the Bank shall have received a certificate signed by the Trustee accompanied by the Series A/B Letter of Credit stating that there are no Series A Bonds or Series B Bonds Outstanding, or (iii) the honoring of a final drawing by the Trustee under the Series A/B Letter of Credit, accompanied by the Series A/B Letter of Credit. The Series C Letter of Credit will expire on the earlier of (i) December 16, 2013, (ii) the date on which the Bank shall have received a certificate signed by the Trustee accompanied by the Series C Letter of Credit stating that there are no Series C Bonds Outstanding, or (iii) the honoring of a final drawing by the Trustee under the Series C Letter of Credit, accompanied by the Series C Letter of Credit.

Issuance of the Letter of Credit by the Bank

Subject to the terms and conditions of the Reimbursement Agreement, the Bank agrees, on the terms and subject to the satisfaction of the conditions contained in the Reimbursement Agreement, to issue the Series A/B Letter of Credit in favor of the Trustee, as security for the Borrower's payment obligations with respect to the Series A Bonds and the Series B Bonds under the Agreement, in an amount not exceeding $543,076,007 (as reduced or reinstated from time to time in accordance with the terms of the Series A/B Letter of Credit), consisting of $532,830,000 in respect of principal of the Series A Bonds and the Series B Bonds, and $10,246,007 in respect of interest on the Series A Bonds and the Series B Bonds for 180 days, calculated at the actual rates of interest on the Series A Bonds and the Series B Bonds, and based on a 360-day year. In addition, subject to the terms and conditions of the Reimbursement Agreement, the Bank agrees, on the terms and subject to the satisfaction of the conditions contained in the Reimbursement Agreement, to issue the Series C Letter of Credit in favor of the Trustee, as security for the Borrower's payment obligations with respect to the Series C Bonds under the Agreement, in an amount not exceeding $138,309,794 (as reduced or reinstated from time to time in accordance with the terms of the Series C Letter of Credit), consisting of $136,385,000 in respect of principal and purchase price of the Series C Bonds, and $1,924,794 in respect of interest on the Series C Bonds for 180 days, calculated at the current Term Rate in effect on the Series C Bonds, and based on a 360-day year.

Conditions Precedent

The obligation of the Bank to issue the Letter of Credit shall be subject to the fulfillment of the following conditions precedent, among others, to the satisfaction of the Bank:

(a) the Bank shall have received the following, in form and substance satisfactory to the Bank: (i) copies of the resolutions of the Board of Directors of the Borrower authorizing the execution, delivery and performance by the Borrower of the Reimbursement Agreement, the other financing documents, and all other agreements, documents, certificates and notices executed by the Borrower in connection with the transactions contemplated therein, certified by the Secretary or an Assistant Secretary of the Borrower as of the date of issuance of the Letter of Credit (the "Issuance Date"); (ii) a certificate, dated as of the Issuance Date, of the Secretary or an Assistant Secretary of the Borrower certifying the names, incumbency and true signatures of the officers or representatives of the Borrower authorized to sign the Reimbursement Agreement and all other agreements, documents, certificates and notices executed by the Borrower in connection with the transactions contemplated therein; (iii) an original executed counterpart of the Reimbursement Agreement and executed originals or photocopies of each other financing documents, each of which shall be in form and substance satisfactory to the Bank; and (iv) an opinion or opinions of counsel to the Borrower, dated the Issuance Date, in form and substance satisfactory to the Bank covering the due authorization, execution and delivery of the Reimbursement Agreement and the other financing documents to which the Borrower is a party, and such matters as the Bank may reasonably request;

(b) the following statements shall be true and correct on the Issuance Date and the Bank shall have received a certificate signed by an Authorized Officer of the Borrower, dated the Issuance Date, stating that: (i) the representations and warranties contained in the Reimbursement Agreement shall be true and correct in all material respects on and as of the Issuance Date as though made on such date; and (ii) no Default or Event of Default (each as hereafter defined) shall have occurred and be continuing, or would result from the issuance of the Letter of Credit or the execution and delivery of any other document executed in connection therewith; and

(c) the Bank shall have received payment of all fees, costs and expenses due and payable to it pursuant to the Reimbursement Agreement.

Covenants of the Borrower

The following are certain covenants of the Borrower contained in the Reimbursement Agreement:

(a) the Borrower shall make all payments required to be made by it, in accordance with the Reimbursement Agreement, as and when due;

(b) the Borrower shall cause the Bonds to be redeemed, in accordance with the extraordinary optional redemption provisions set forth in the Reimbursement Agreement, from any payment (the "concession payment") received by the Borrower as a result and in consideration of entering into a concession agreement (or other similar use, long-term lease or operations agreement) with respect to the Luís Muñoz Marín International Airport (the "concession agreement"), in an amount equal to the amount of the concession payment (less any costs incurred by the Borrower in connection with entering into the concession agreement), or such lesser amount as may be agreed to by the Borrower and the Bank, within 120 days of receipt of the concession payment;

(c) the Borrower shall not take any actions or omit to take any actions that would cause the interest on the Series B Bonds or the Series C Bonds to cease to be excludable from gross income of the owners thereof for federal income tax purposes;

(d) the Borrower will not incur any additional indebtedness nor lien any of its property without the express prior written consent of the Bank;

(e) the Borrower will furnish, or will cause to be furnished, to the Bank copies of the following reports, notices and information: (i) as soon as possible and in any event within 15 days after the occurrence of each Event of Default or event or condition which, with the lapse of time or the giving of notice, or both, would constitute an Event of Default (a "Default"), a statement of an Authorized Officer of the Borrower setting forth details of such Default or Event of Default; (ii) promptly upon receipt thereof, copies of all notices of default received or given by the Borrower which relate to the Agreement and, from time to time upon request by the Bank, such information and reports regarding the Agreement as the Bank may reasonably request; (iii) promptly after the amendment of, waiver to, or any other modification of, any of the Agreement or other financing documents, a copy of such amendment, waiver or modification; and (iv) such other information respecting the condition or operations, financial or otherwise, of the Borrower as the Bank may from time to time reasonably request;

(f) the Borrower will not amend or otherwise permit to occur any amendment, modification or waiver of any of the terms of the Agreement or any other financing document which could increase the obligations of the

Bank under the Letter of Credit or adversely affect the rights of the Bank without the prior written consent of the Bank; and

(g) the Borrower will comply with (i) all applicable laws, rules, regulations and orders (including, without limitation, the maintenance and preservation of its corporate existence) except where such non compliance would not have a Material Adverse Effect (as hereinafter defined) and (ii) all other laws, rules regulations and orders, promptly upon discovery of any noncompliance, except where such noncompliance would not have a Material Adverse Effect. *"Material Adverse Effect"* means, relative to any event, occurrence or circumstance of any nature whatsoever (including any adverse determination in any litigation, arbitration, investigation proceeding or labor controversy), a material adverse effect on: (a) the financial condition, operations, assets, business or properties of the Borrower; or (b) the ability of the Borrower to perform its obligations under the Reimbursement Agreement or any document delivered to the Bank as security therefor (the *"Related Documents"*); or (c) the validity or enforceability of the Reimbursement Agreement, the Letter of Credit or any Related Document.

Security for Obligations under the Reimbursement Agreement

To secure the payment of the obligations of the Borrower to reimburse the Bank for any drawing under the Letter of Credit, and the satisfaction and performance of all other covenants, agreements and obligations made or undertaken by the Borrower under the Reimbursement Agreement or under the other financing documents, for the benefit of the Bank, the Borrower shall pledge and grant to the Bank a lien upon and security interest (the maximum extent possible under federal and Puerto Rico law) in all right, title and interest in and to the Net Revenues (as hereinafter defined), whether in the form of proceeds of accounts receivable or contract rights or otherwise, and in any rights to receive the same. *"Net Revenues"* means the amount of the excess of the Borrower's Revenues over its Current Expenses (as such terms are defined in the Trust Agreement, dated as of January 1, 1972 as amended and supplemented to date, by and among the Borrower, JPMorgan Chase Bank, as successor trustee, and Banco Popular de Puerto Rico, as successor co-trustee (the *"Ports Trust Agreement"*)); provided that the Bank shall release the lien on any Net Revenues that may be derived from the ownership, management or operation of the Luís Muñoz Marín International Airport, in connection with the Borrower's entering into any concession agreement, as the Bank may determine necessary and appropriate to effectuate the terms of any such concession agreement. If any required payment under the Reimbursement Agreement is not made when due, any Net Revenues with respect to which such security interest remains perfected pursuant to law shall, subject to the provisions of the Ports Trust Agreement, be transferred or paid over immediately to the Bank without being commingled with other funds (unless already commingled) and any such Net Revenues thereafter received shall, subject to the provisions of the Ports Trust Agreement, upon receipt be transferred to the Bank in the form received and may be converted to cash and applied by the Bank to the extent necessary to cure the deficiency. Such lien upon the Net Revenues shall at all times be a first priority lien, subject only to liens granted under the Ports Trust Agreement or any other lien consented to by the Bank in writing.

The Borrower also shall assign to the Bank a lien upon and security interest in the leases and rents from its various properties and facilities, to the extent permitted by the applicable lease or rental agreement.

Events of Default

The occurrence of any of the following events, among others, shall constitute an "Event of Default" under the Reimbursement Agreement (reference is made to the Reimbursement Agreement for a complete listing of all Events of Default):

(a) the Borrower (i) shall fail to pay any amount payable pursuant to the Agreement as reimbursement for a drawing under the Letter of Credit when and as due and such failure shall continue for 10 days, (ii) shall fail to pay any other amount due under the Reimbursement Agreement when and as due and such failure shall continue for 15 days following written notice thereof from the Bank, or (iii) shall fail to make any other payment required of it, within 15 days of the due date thereof, pursuant to Agreement;

(b) except as set forth in paragraph (a) above, the Borrower shall default in the observance or performance of any other covenant or agreement under the Reimbursement Agreement and such default shall remain unremedied for 15 days following written notice thereof from the Bank (in the event that such Default shall be capable of being remedied and the Borrower shall have commenced within such 15-day period all such action as may be required to remedy such Default, a 20-day extension shall be granted by the Bank);

(c) any representation, warranty, certificate or statement made by the Borrower in the Reimbursement Agreement or in any certificate, financial statement or other document delivered pursuant thereto shall prove to have been incorrect in any material respect when made or deemed made; or

(d) any of the following shall occur: (i) the Borrower shall become insolvent or generally fail to pay, or admit in writing its inability or unwillingness to pay, its debts as they become due, (ii) the Borrower shall apply for, consent to, or acquiesce in, the appointment of a trustee, receiver, sequestrator, rehabilitator, liquidator, conservator or other custodian (or similar official) for the Borrower or all or substantially all of its assets, or make a general assignment for the benefit of creditors, (iii) in the absence of such application, a trustee, receiver, sequestrator, rehabilitator, liquidator, conservator or other custodian (or similar official) shall have been appointed for the Borrower or all or substantially all of its assets, (iv) the Borrower shall permit or suffer to exist the commencement of any bankruptcy, reorganization, debt arrangement or other case or proceeding under any bankruptcy or insolvency law, or any dissolution, winding up or liquidation proceedings in respect of the Borrower, and, if any such case or proceeding is not commenced by the Borrower, such case or proceeding shall be consented to or acquiesced in by the Borrower or shall result in the entry of an order for relief or shall remain for 60 days undismissed, or (v) the Borrower shall take any corporate action authorizing, or in furtherance of, any of the foregoing.

Remedies

If any Event of Default occurs that is not waived by the Bank, the Bank may pursue, in its sole discretion, all remedies available to it against the Borrower or the Borrower’s property, including under the Related Documents and with respect to the Net Revenues, at law, by contract, in equity or otherwise.

Government Development Bank for Puerto Rico

(A Component Unit of the Commonwealth of Puerto Rico)

Basic Financial Statements and Required Supplementary Information as of and for the Year Ended June 30, 2011, and Independent Auditors' Report

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO
(A Component Unit of the Commonwealth of Puerto Rico)

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INDEPENDENT AUDITORS' REPORT

To the Members of the Board of Directors of
Government Development Bank for Puerto Rico:

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of Government Development Bank for Puerto Rico (the "Bank"), a component unit of the Commonwealth of Puerto Rico, as of and for the year ended June 30, 2011, which collectively comprise the Bank's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Bank's management. Our responsibility is to express an opinion on the respective financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the respective financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the respective financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, business-type activities, each major fund, and the aggregate remaining fund information of Government Development Bank for Puerto Rico, as of June 30, 2011, and the respective changes in financial position and respective cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

As discussed in Notes 2 and 5 to the financial statements, loans to the Commonwealth of Puerto Rico and its agencies and instrumentalities amounted to approximately $6.0 billion or 38.7% of the Bank's total assets as of June 30, 2011. These loans are expected to be collected from appropriations from, proceeds from bond issuances of, or revenues generated by the Commonwealth of Puerto Rico and/or its agencies and instrumentalities. Since 2000, the Commonwealth's recurring expenditures have exceeded its recurring revenues and its credit ratings have been lowered. In addition, many of the Commonwealth's agencies and instrumentalities have had losses from operations during the past years. The collectibility of these loans may be affected by budgetary constraints, the fiscal situation and the credit ratings of the Commonwealth of Puerto Rico and its agencies and instrumentalities, and their ability to generate sufficient funds from taxes, charges and/or bond issuances. Continuance of and/or significant negative changes in these factors may affect the ability of the Commonwealth and agencies and instrumentalities to repay their outstanding loan balances with the Bank and, accordingly, may have an adverse impact on the Bank's financial condition, liquidity, funding sources, and results of operations.

The management's discussion and analysis on pages 3 to 17 is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. This supplementary information is the responsibility of Government Development Bank for Puerto Rico's management. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit such information and we do not express an opinion on it.

Deloitte & Touche LLP

December 1, 2011

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This section presents a narrative overview and analysis of the financial performance of Government Development Bank for Puerto Rico (the "Bank" or "GDB") as of and for the year ended June 30, 2011. The information presented here should be read in conjunction with the basic financial statements, including the notes thereto.

1. FINANCIAL HIGHLIGHTS

- Total assets government wide at June 30, 2011 amounted to $15,510 million for an increase of $1,461 million or 10.4% from the $14,049 million at June 30, 2010. Liabilities increased by 12.4% or $1,421 million to $12,926 million from $11,505 million.

- Net assets government wide grew to $2,584 million from $2,544 million at June 30, 2010. The increase in net assets of $40 million in fiscal year 2011 is composed of $74 million from business-type activities offset by an excess of expenses and transfers over revenues of $34 million from governmental activities. Net assets to total assets decreased to 16.7% at June 30, 2011 from 18.1% at June 30, 2010.

- The operating income of the GDB Operating Fund increased from $67.5 million in 2010 to $107.1 million or $39.6 million in fiscal year 2011. This increase represented an improvement of 58.6% from the previous year.

- The Bank issued approximately $3,503 million of Senior Notes consisting of $1,448.7 million of Senior Notes 2010 Series A; $151.3 million of Senior Notes 2010 Series B; $1,086 million of Senior Notes 2010 Series C; $96.4 million of Senior Notes 2010 Series D; $70 million of Senior Notes 2011 Series A, and $650 million of Senior Notes 2011 Series B. The Bank used the proceeds of these issuances mainly to repay previously issued notes with higher interest rates, increase the investment portfolio, and make loans to and purchase obligations of the Commonwealth of Puerto Rico (Commonwealth), its public corporations and municipalities.

- Interest income on loans in the GDB Operating Fund amounted to $405.8 million in 2011, an increase of $79.3 million over the prior year. The Bank collected approximately $24.9 million in principal and $139.1 million in interest on loans to the public sector from the general fund of the Commonwealth.

- Included within salaries and fringe benefits expense is approximately $2.6 million related to an employees' voluntary termination plan provided under Act No. 70 of July 2, 2010.

2. OVERVIEW OF THE FINANCIAL STATEMENTS

This discussion and analysis is required supplementary information to the basic financial statements and is intended to serve as introduction to the basic financial statements of the Bank. The basic financial statements comprise three components: (1) government-wide financial statements, (2) fund financial statements, and (3) notes to the basic financial statements.

Government-Wide Financial Statements — The government-wide financial statements are designed to provide readers with a broad overview of the Bank's finances, in a manner similar to a private-sector business. The statement of net assets provides information on the Bank's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Bank is improving or deteriorating. The statement of activities presents information on how the Bank's net assets changed during the reporting period. Changes in net assets are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows.

Fund Financial Statements — A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The Bank's funds are divided in two categories: governmental funds and enterprise funds.

- *Governmental Funds* — Governmental funds are used to account for the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on near-term inflows and outflows of expendable resources, as well as balances of expendable resources available at the end of the fiscal year. Such information may be useful in evaluating a government's near-term financing requirements.

  Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of financial decisions related to the Bank's governmental activities. Both the governmental fund balance sheet and the governmental statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

- *Enterprise Funds* — Enterprise funds provide the same type of information as the business-type activities in the government-wide financial statements, only in more detail. The enterprise fund financial statements of the Bank provide separate information on the business-type activities of the Bank's blended component units.

Notes to the Basic Financial Statements — The notes provide additional information that is essential to a full understanding of the data provided in the government-wide financial statements and the fund financial statements.

3. GOVERNMENT-WIDE FINANCIAL ANALYSIS

Total assets and total liabilities of the Bank at June 30, 2011 amounted to $15,510 million and $12,926 million, respectively, for net assets of $2,584 million or 16.7% of total assets. Within assets, excluding the loans portfolio, cash and due from banks, and deposits placed with banks show the most significant growth of $332 million and $696 million, respectively, over fiscal year 2010 balances of $15 million and $45 million, respectively. Investments and investment contracts decreased by $870 million or 14% when compared to prior year. The proportion of investments to total assets decreased to 34.5% in 2011 from 44.3% in 2010. In addition, federal funds sold decreased by approximately $242 million or 73.2% when compared to the previous year.

Loan portfolio of $8,396 million at June 30, 2011 shows an increase of 20.5% when compared to the prior year ending balance of $6,966 million. Loans as a percentage of total assets grew 4.5% from 49.6% in fiscal year 2010 to 54.1% in fiscal year 2011.

The Bank's Operating Fund issued several note series during fiscal year 2011 for a net increase of $2,125 million in this line item. The Bank has primarily used the proceeds from these notes to increase its investment portfolio, to make loans to the Commonwealth, its public corporations and municipalities, and to repay certain higher interest rate debt. On the other hand, the Bank decreased its funding from securities sold under agreements to repurchase by 8.3% over the 2010 balance.

Out of the $2,584 million in net assets, $2,151 million or 83.2% is unrestricted, $301 million or 11.7% is restricted for use in housing programs, and the remaining $132 million or 5.1% is invested in capital assets and restricted for the mortgage loan insurance program. Governmental and business-type activities are discussed separately in the following subsections.

Governmental Activities — Total assets of governmental activities amounted to $164.2 million at June 30, 2011, before $127.7 million in net balances due to business-type activities. Total liabilities amounted to $72.1 million, for a net deficit of $35.6 million. Net deficit has been broken down into the amounts restricted for affordable housing programs of $50.7 million, and the unrestricted deficit of $86.4 million, which means that the restriction on the use of available assets will not allow the Bank to satisfy its existing liabilities from those assets, and therefore that it will depend on future appropriations for the repayment of part of its obligations.

Condensed financial information on assets, liabilities, and net assets of governmental activities as of June 30, 2011 and 2010 is shown below (amounts in thousands):

	June 30, 2011	June 30, 2010	Change Amount	Change Percent
Assets:				
Restricted:				
Cash and due from banks, and deposits placed with banks	$ 72,295	$ 7,527	$ 64,768	860.5%
Investments and investment contracts	70,165	93,892	(23,727)	(25.3)%
Other assets	21,723	29,494	(7,771)	(26.3)%
Total assets before internal balances	164,183	130,913	33,270	25.4%
Internal balances	(127,675)	(80,287)	(47,388)	59.0%
Total assets	36,508	50,626	(14,118)	(27.9)%
Liabilities:				
Accounts payable and accrued liabilities	67,303	47,394	19,909	42.0%
Notes payable — due in more than one year	4,811	4,811	-	0.0%
Total liabilities	72,114	52,205	19,909	38.1%
Net deficit:				
Invested in capital assets	42	-	42	100.0%
Restricted for affordable housing programs	50,720	52,933	(2,213)	(4.2)%
Unrestricted deficit	(86,368)	(54,512)	(31,856)	58.4%
Total net deficit	$ (35,606)	$ (1,579)	$ (34,027)	2,155.0%

Investments and investment contracts amounted to $70.2 million and, together with cash and due from banks, and deposits placed with banks of $72.3 million, account for the majority of the assets held by governmental activities. These assets are held to provide funds for the execution of the various affordable and other housing programs managed by the Puerto Rico Housing Finance Authority (the "Housing Finance Authority"). Other assets are composed principally of due from the HUD, Home, and ARRA federal programs. Accrued liabilities mainly consist of unpaid expenditures related to the ARRA and My New Home Program funds and of subsidies payable on various housing programs.

Condensed financial information on expenses, program and general revenues, and changes in net assets of governmental activities for the years ended June 30, 2011 and 2010 is shown below (in thousands):

	Year Ended June 30, 2011		
	General Government	Housing Assistance Programs	Total
Expenses	$ 6,155	$ 311,951	$ 318,106
Program revenues:			
Charges for services — financing and investment		4,690	4,690
Operating grants and contributions	-	279,609	279,609
Net expenses	$ (6,155)	$ (27,652)	(33,807)
Transfers — net			(220)
Change in net assets			(34,027)
Net deficiency — beginning of year			(1,579)
Net deficiency — end of year			$ (35,606)

	Year Ended June 30, 2010		
	General Government	Housing Assistance Programs	Total
Expenses	$ 4,777	$ 250,787	$ 255,564
Program revenues:			
Charges for services — financing and investment		4,743	4,743
Operating grants and contributions	-	225,268	225,268
Net expenses	$ (4,777)	$ (20,776)	(25,553)
Transfers — net			(4,902)
Change in net assets			(30,455)
Net assets — beginning of year			28,876
Net deficiency — end of year			$ (1,579)

4. GOVERNMENTAL FUND RESULTS

Operating grants and contributions increased by $54 million when compared to the prior year. Operating grants and contributions increased from $225 million in 2010 to $279 million in 2011 mainly because this year the Housing Finance Authority earned $96 million in ARRA funds as compared to $87 million in 2010. In addition, the Housing Finance Authority received $36.8 million from the Local Economic Stimulus Program to fund its Closing Costs Assistance Program as compares to $10 million in 2010. In addition, during fiscal year 2011, the Housing Finance Authority earned $16.4 million related to the Home program, which is administered by the Housing Finance Authority effective July 1, 2010.

Following is an analysis of the financial position and results of operations of the Bank's major governmental funds:

HUD Programs — This fund accounts for the U.S. Housing Act Section 8 programs administered by the Housing Finance Authority under the authorization of the U.S. Department of Housing and Urban Development. Presently, the Housing Finance Authority operates three programs whereby low-income families receive directly or indirectly subsidies to pay for their rent. The housing vouchers program enables families to obtain rental housing in a neighborhood of their choice. The other programs are project-based subsidies whereby housing developers are given incentives to keep their properties available for certain markets. The expenditures of the HUD programs increased $2 million from $125 million in 2010 to $127 million in 2011. The expenditures in the housing vouchers program increased $1 million when compared to the previous year because additional vouchers were awarded.

ARRA Funds — This fund accounts for two federal programs established by ARRA. ARRA established a federal funding opportunity through two separate programs, the Section 1602, "Cash Assistance in Lieu of Tax Credits" program called the Tax Credit Exchange Program (TCEP) and Tax Credit Assistance Program (TCAP). Both programs make stimulus package funding available to multi-family rental projects that meet the requirements of the Low Income Housing Tax Credits program (LIHTC). TCEP allows state housing tax credit allocating agencies to exchange a portion of the housing tax credits for cash grants. The cash grants can then be used by the allocating agencies to make "subawards" to finance the construction or acquisition and rehabilitation of qualified low-income buildings. TCAP provides grant funding for capital investment in LIHTC projects through a formula-based allocation to each state. The purpose of the TCAP funding is to assist in filling the funding gap resulting from the decline in equity pricing. The revenues and expenditures of ARRA funds amounted to $95.7 million in 2011as compared to $86.6 million in 2010.

Closing Costs Assistance Program — This fund accounts for the subsidy to eligible individuals or families for the purchase of an eligible principal residence. The subsidy consists of the reimbursement of origination and closing costs up to 5% of the selling price, which cannot exceed $300,000, of the eligible principal residence. The Housing Finance Authority finances this program with transfers from its operating and administrative fund and from appropriations from the Commonwealth. During the year ended June 30, 2011, the program received $36.8 million in appropriations from the Commonwealth. During the year ended June 30, 2011, subsidy expenditures amounted to $35.9 million.

My New Home Program — This program provides closing costs assistance to eligible families for the purchase of a principal residence through reimbursements of origination and closing costs. During the year ended June 30, 2011, total subsidy expenditures amounted to $31 million.

At June 30, 2011, the Housing Finance Authority had various governmental funds in a deficit position. The Housing Finance Authority expects to cover these deficits through contributions from the Commonwealth. Refer to Note 22 to the basic financial statements for additional information on these funds.

5. BUSINESS-TYPE ACTIVITIES

Condensed financial information on assets, liabilities, and net assets as of June 30, 2011 and 2010, is presented below (amounts in thousands):

	June 30,		Change	
	2011	2010	Amount	Percent
Assets:				
Cash and due from banks	$ 343,214	$ 13,851	$ 329,363	2,377.9%
Federal funds sold	88,850	331,000	(242,150)	(73.2)%
Deposits placed with banks	672,362	38,853	633,509	1,630.5%
Investments and investment contracts	5,278,429	6,124,707	(846,278)	(13.8)%
Loans receivable — net	8,395,959	6,966,384	1,429,575	20.5%
Interest and other receivables	235,085	178,245	56,840	31.9%
Real estate available for sale	128,568	207,792	(79,224)	(38.1)%
Other assets	132,151	41,072	91,079	221.8%
Due from other funds	127,675	80,287	47,388	59.0%
Capital assets	71,008	15,750	55,258	350.8%
Total assets	15,473,301	13,997,941	1,475,360	10.5%
Liabilities:				
Deposits:				
Demand	3,782,555	3,253,713	528,842	16.3%
Certificates of deposit	1,771,133	2,895,485	(1,124,352)	(38.8)%
Securities sold under agreements to repurchase	970,819	1,058,835	(88,016)	(8.3)%
Accrued interest payable	30,466	28,325	2,141	7.6%
Accounts payable, accrued liabilities, and other liabilities	109,255	98,038	11,217	11.4%
Certificates of indebtedness	4,300	11,800	(7,500)	(63.6)%
Bonds, notes, and mortgage-backed certificates payable:				
Due in one year	159,697	226,219	(66,522)	(29.4)%
Due in more than one year	6,025,328	3,879,986	2,145,342	55.3%
Total liabilities	12,853,553	11,452,401	1,401,152	12.2%
Net assets:				
Invested in capital assets	71,008	15,750	55,258	350.8%
Restricted for:				
Mortgage loan insurance	61,119	61,899	(780)	(1.3)%
Affordable housing programs	247,643	230,895	16,748	7.3%
Other housing programs	2,567	4,183	(1,616)	(38.6)%
Unrestricted	2,237,411	2,232,813	4,598	0.2%
Total net assets	$ 2,619,748	$ 2,545,540	$ 74,208	2.9%

Federal Funds Sold and Deposits Placed with Banks — The Bank decreased its federal funds sold by $242 million, from $331million at June 30, 2010 to $89 million at June 30, 2011. The Bank reduced the federal funds in favor of higher rate short term deposits placed with banks. Deposits placed with banks increased by $633.5 million, from $38.9 million to $672.4 million. The increase is mostly attributed to a deposit of $400 million with a financial institution for the refunding of a portion the GDB Senior Notes Series 2009 C and D on July 1, 2011.

Investments and Investment Contracts — Investments and investment contracts held in business-type activities amounted to $5,278.4 million at June 30, 2011. This amount represents a decrease of $846.3 million or 13.8% when compared to the prior year balance of $6,124.7 million. The investment portfolio has consisted primarily of U.S. Treasury Notes, Treasury Bills and U.S. sponsored agency notes and mortgage-backed securities with very high credit ratings, reflecting the Bank's prudent and conservative investment policies. The majority of the Bank's investment portfolio is invested in AAA to A- rated securities. The investment portfolio comprised 34% of the total assets of the Bank's business-type activities at June 30, 2011, down by 10% as compared to 44% at the close of fiscal year 2010. Within the investment securities portfolio, $1,503 million at June 30, 2011 and $1,539 million at June 30, 2010, were restricted or pledged as collateral or payment source for specific borrowings.

Loans Receivable — Net loans receivable increased by $1,429.6 million, from the $6,966.4 million balance at June 30, 2010 to $8,396 million at June 30, 2011. The increase primarily arises from the Bank's basic role of providing financial support to the Commonwealth's public works, particularly in times of economic hardship, such as the prevailing circumstances in the Island and world-wide. To support the governmental efforts of improving and stimulating the Island's economy, the Bank finances the development and construction of infrastructure, housing projects, and hotels.

Loans to municipalities had a net increase of $325.3 million over the prior year balance. Some of these loans were possible with the improvement of the municipalities' debt margin capacity as a result of increases in the property and municipal sales taxes.

Private sector loans outstanding at June 30, 2011 and 2010 amounted to $605 million and $530 million, respectively, net of an allowance for loan losses and deferred origination fees of $132.1 million and $20 million at June 30, 2011, and $85 million and $9.5 million at June 30, 2010, respectively. Private sector loans mainly include loan facilities for the housing and tourism sectors through some component units of the Bank. Refer to Note 5 for further information on loans receivable and allowance for loan losses.

Real Estate Available for Sale — Real estate available for sale includes several properties received in fiscal year 2009 in lieu of payment of a loan whose principal balance and accrued interest receivable amounted to $144.2 million at December 30, 2008. The current appraised value of these properties amounts to $78 million. Additional properties are being negotiated with the parties involved to satisfy the deficiency.

In the meantime, the Bank has recorded a receivable for this difference as permitted by the agreement with the transferor. The Office of Management and Budget of the Commonwealth ("OMB") will disburse approximately $7.5 million before December 31, 2011 to cover a portion of this difference. In addition, the OMB has committed to include in the Commonwealth general fund budget an amount of approximately $3.8 million plus interest at the rate of 7% for the next fifteen years to assist the agencies involved in the transaction in repaying the accounts receivable of the Bank. The proposed appropriation will be subject to the approval of the Legislature of the Commonwealth of Puerto Rico.

Capital Assets — Capital assets, net of accumulated depreciation and amortization, amounted to $71 million at June 30, 2011, an increase of $55 million from the prior year. Additions to capital assets during the year ended June 30, 2011 aggregated to $1.3 million principally in the software line item. Depreciation and amortization of $2.5 million was charged to operations during fiscal year 2011. In addition, property from real estate available for sale of approximately $56.4 was transferred to capital assets as of June 30, 2011. Refer to Note 8 to the basic financial statements for additional information on capital assets.

Deposits — Deposits mainly consist of interest-bearing demand deposit accounts, special government deposit accounts, and time deposits from the Commonwealth, its agencies, instrumentalities, and municipalities.

Demand deposits and certificates of deposit had a combined decrease of $595 million, from $6,149 million at June 30, 2010 to $5,554 million at June 30, 2011. Deposits constitute approximately 43% and 54% of total liabilities at June 30, 2011 and 2010, respectively. Maturing deposits have been offset by the issuance of medium term notes and other borrowed funds.

Securities Sold under Agreement to Repurchase — Securities sold under agreements to repurchase decreased by $88 million or 8.3% from $1,058.8 million to $970.8 million at June 30, 2011.

Other Borrowed Funds — The Bank issued several note series during fiscal year 2011, which explains the net growth of $2,078.8 million or 51% over prior year balance of $4,106.2 million. Most of the notes issued during fiscal year 2011 consist of term notes maturing on various dates from August 1, 2011 to August 1, 2025. Most of such notes have early redemption options. Interest rates on such notes range from 2% to 5.75%. Certain notes, upon compliance with certain requirements of the U.S. Internal Revenue Code, will receive a subsidy payment from the federal government equal to 35% of the amount of each interest payment of these notes. The Bank used the proceeds from these obligations for general operational purposes that include, among others, the substitution of higher cost debt, the increase of its investment portfolio and the funding of loans. Responding to market conditions, the Bank has increased its issuance of medium term notes and significantly reduced its commercial paper borrowings, which has lengthened the average maturity of its liabilities. Refer to Note 12 to the basic financial statements for additional information on borrowed funds.

Condensed financial information on expenses, program revenues, and changes in net assets for business-type activities for the years ended June 30, 2011 and 2010 is presented below (in thousands):

	Year Ended June 30, 2011			
		Program revenues		
		Charges for services		
Activity	Expenses	Fees, commissions, and others	Financing and investment	Net revenues (expenses)
GDB Operating Fund	$ 409,653	$ 14,084	$ 486,860	$ 91,291
Housing Finance Authority	93,504	13,321	89,326	9,143
Tourism Development Fund	50,125	5,191	28,042	(16,892)
Public Finance Corporation	4		1	(3)
Capital Fund	37	35	1	(1)
Development Fund	10,947	-	(1,434)	(12,381)
Other nonmajor	110	2,381	5	2,276
Total	$ 564,380	$ 35,012	$ 602,801	73,433
Special item —Contribution from Puerto Rico Infrastructure Financing Authority				555
Transfers from governmental activities				220
Change in net assets				74,208
Net assets — beginning of year				2,545,540
Net assets — end of year				$ 2,619,748

	Year Ended June 30, 2010				
		Program revenues			
		Charges for services			
Activity	**Expenses**	**Fees, commissions, and other**	**Financing and investment**	**Operating grants and contributions**	**Net revenues (expenses)**
GDB Operating Fund	$ 342,854	$ 23,518	$ 382,737	$ -	$ 63,401
Housing Finance Authority	96,153	11,114	104,413	34,000	53,374
Tourism Development Fund	28,410	1,968	9,717	15,000	(1,725)
Public Finance Corporation	4,681		4,679		(2)
Capital Fund	68	1	5,807		5,740
Development Fund	3,555	3	622		(2,930)
Other nonmajor	140	-	3	-	(137)
Total	$ 475,861	$ 36,604	$ 507,978	$ 49,000	117,721
Special item — Contribution from Puerto Rico Infrastructure Financing Authority					1,110
Transfers from governmental activities					4,902
Change in net assets					123,733
Net assets — beginning of year					2,421,807
Net assets — end of year					$ 2,545,540

Activities presented in the statement of activities coincide with the major enterprise funds of the Bank. GDB Operating Fund generated financing and investment revenues of $486.9 million from its loan and investment portfolios, and $14.1 million in other charges for services, including its fiscal agency function. These revenues covered $409.7 million in expenses for a change in net assets from GDB Operating Fund of $91.7 million, surpassing the change in net assets of any other activity.

The Housing Finance Authority's activities were the second largest contributor to the change in net assets with a $9.4 million increase. Operating losses of other major component units for fiscal year 2011 were as follows: Tourism Development Fund with $16.9 million and Development Fund with $12.4 million.

Enterprise Funds — Following is a brief discussion of the most significant changes in the Bank's enterprise funds, not previously discussed. Our main focus will be on GDB Operating Fund, since separate basic financial statements are issued for each of the Bank's other major enterprise funds, which are blended component units.

GDB Operating Fund — Total assets of the GDB Operating Fund amounted to $14,547 million at June 30, 2011, compared to $13,209 million at June 30, 2010. This represents an increase of $1,338 million, which was sustained by the net increase in liabilities of $1,247 million and the change in net assets of $92 million. As already discussed, the GDB Operating Fund issued debt widening its assets base and obtaining more liquidity to assist governmental entities in times of economic distress. Investments decreased by $829 million and loans to the public sector increased by $1,355 million. Accrued interest receivable increased from $128 million at June 30, 2010 to $234 million at June 30, 2011, mainly because of increases in interest rates on loans due to a pricing initiative during the first semester of last year and a net increase of $1.4 billion on loans. During the year, a portion of principal and interest on loans, aggregating to approximately $164 million was collected from the general fund of the Commonwealth of Puerto Rico. Refer to Note 5 to the basic financial statements for additional information on loan receivables and allowances on loan losses.

Operating income of the GDB Operating Fund experienced an increment from $67.5 million in fiscal year 2010 to $107.1 million in fiscal year 2011, or an increase of $39.6 million, which represents a 59% increase. Change in net assets had a significant increase from $64.4 million in fiscal year 2010 to $91.7 million in fiscal year 2011. Following is a discussion of the various components of the change in net assets of the GDB Operating Fund, compared to the prior year:

(a) *Interest Income, Interest Expense, and Change in Fair Value of Investments*

Net investment income, the difference between investment income and interest expense, increased $26.5 million or 28%, from $95.7 million in 2010 to $122.2 million in 2011. Most of the increase results from the loan portfolio, which shows an increase of $79 million or 24% when compared to the prior year results. This increase is directly related to the increase on loans of $1,395 million from $6,803 million in fiscal year 2010 to $8,198 million in fiscal year 2011. Change in fair value of investments contributed to the increase with a gain of $33.8 million. That is $17 million more than the gain of $16.8 million of fiscal year 2010. Interest income from investments increased $7.8 million or 19.8% mainly because of concentration of our investment portfolio in U.S. Government and U.S. agencies securities where interest rates increased. Interest expense increased by $77.6 million, or 27.1%, mainly as a result of a net increase of $2,125 million in the notes line item offset by decreases of $776 million in the deposits and $88 million in the securities sold under agreements to repurchase line items.

(b) *Provision for Losses on Loans*

The experience with the public sector loan portfolio, even in periods of economic distress such as the present, provides continued comfort to management. After an analysis performed, management believes that there is no need for further provisions, instead, there was a credit to the provision for loan losses of $5.6 million leaving the allowance for loan losses with a balance of $4 million at June 30, 2011. Management believes that there is no need for an allowance for possible losses on guarantees and letters of credit to public sector entities.

(c) Noninterest Income

Noninterest income decreased to $14.1 million in fiscal year 2011 from $23.5 million in fiscal year 2010, or $9.4 million. Fiscal agency fees constitute the main component of noninterest income. There was an intense activity of bond issuances of public sector entities during fiscal year 2010 when compared to fiscal year 2011. The fiscal agency fees decreased from $17.2 million in fiscal year 2010 to $5.7 million in fiscal year 2011, representing a decrease of 67%.

(d) Noninterest Expenses

Total noninterest expenses showed a decrease of $17 million from $51.7 million in fiscal year 2010 to $34.7 million in fiscal year 2011. Decrease is mainly because of the following three major items in fiscal year 2010: (1) write downs to real estate available for sale of approximately $11.9 million, (2) voluntary and involuntary terminations costs of $3.5 million and (3) a $2.2 million termination fee linked to the adjustable refunding bonds. These 2010 items were presented within salaries and fringe benefits and other expense line items.

Housing Finance Authority — Net assets of the Housing Finance Authority increased by $9.4 million from $635.2 million at June 30, 2010 to $644.6 million at June 30, 2011 as a result of decreases in total assets of $19.5 million and in liabilities of $28.9 million. The decrease in total assets is mainly due to the following:

- Cash decreased from $31.6 million at June 30, 2010 to $9.7 million at June 30, 2011 or a $21.9 million decrease. The decrease was the result of the following factors: reduction of $12 million on the Home Purchase Stimulus Program due to payment of second mortgages to financial institutions, reduction of $8 million used for bonds principal payment on Mortgage Trust III, and reduction of $4 million due to origination of multifamily and single-family loans offset by an increase of $3 million of My New Home Program.

- Investments and deposits placed with banks decreased from $1,265 million at June 30, 2010 to $1,199 million at June 30, 2011 or a $66 million decrease. This decrease was principally the result of investment redemptions to originate construction and single-family loans.

- Loans receivable, net, increased to $246.8 million at June 30, 2011 from $208.1 million in 2010 or a $38.7 million increase. This increase was directly related to the origination of construction and single-family loans.

- Assets, excluding cash, deposits placed with banks, loans and investments, increased from $40 million at June 30, 2010 to $70 million at June 30, 2011 or a $30 million increase. There was an increase in balances due from governmental funds of approximately $41 million and a decrease of approximately $11 million in accrued interest receivable.

- The decrease in long-term liabilities of approximately $33 million is mainly due to an early redemption of Single-Family Mortgage Revenue Bonds Portfolios and Homeownership Mortgage Revenue Bonds. Also, current liabilities increased to $103.6 million at June 30, 2011 from $99.9 million at June 30, 2010 or an increase of $3.7 million.

- Change in net assets decreased $48.9 million, from $58.3 million in 2010 to $9.4 million in 2011. Three main items contributed to this: one-time operating contribution received from the Commonwealth during fiscal year 2010 aggregating to $34 million, declines in operating income of $10 million and net transfers-in of $4.7 million.

Tourism Development Fund — Total assets increased to $611.3 million from $586.2 million in 2010 or an increase of $25.1 million. The Tourism Development Fund mostly finances its loan portfolio through credit facilities obtained from the Bank. Notes payable due to the Bank at year-end were $399.5 million for an increase of $36.7 million from June 30, 2010. The Tourism Fund originated approximately $56 million in loans to the private sector during the year ended June 30, 2011. These loans are principally collateralized by real estate property to minimize the credit risk. The analysis of the allowance for loan losses required an incremental adjustment of $31 million during the year ended June 30, 2011.

At June 30, 2011, outstanding guarantees and letters of credit of the Tourism Development Fund amounted to $328.5 million. Also, the exposure assessment required an increase of the allowance for possible losses on guarantees and letters of credit of $2.4 million.

Change in net assets of the Tourism Development Fund decreased by $87.2 million from the increase of $70.3 million recorded last year to a loss of $16.9 million in 2011.

Capital Fund — The Capital Fund had a net loss of $687 for the year ended on June 30, 2011. After transferring most of its assets to the Tourism Development Fund, the Capital Fund's activities have been significantly reduced.

Public Finance Corporation — The Public Finance Corporation had a net loss of approximately $2,900 for the year ended on June 30, 2011. Also, when compared to the previous year, it showed an increase in net loss of approximately $300. The main operation of this component unit is the issuance of special appropriation bonds and during fiscal year 2011 there was no activity related to this area. The only income this component unit received was for a deposit on an interest bearing account held at the Bank. Interest income for fiscal year 2011was about $1,000 offset by legal and professional fees of approximately $4,000.

Development Fund — The Development Fund's net loss of $12.4 million was mostly attributed to the result of a net investment loss of $1.4 million, $9.3 million provision for loan losses related to loans to the private sector and a $1.5 million provision for possible losses on its guarantees to The Key for Your Business Program managed by the Economic Development Bank for Puerto Rico, a component unit of the Commonwealth. The Development Fund guarantees one third of the loans' principal plus interest and charges, up to $15 million. At June 30, 2011, the outstanding balance of loans guaranteed by the Development Fund amounted to approximately $14.2 million.

6. CONTACTING THE BANK'S FINANCIAL MANAGEMENT

This report is designed to provide all interested with a general overview of the Bank's finances. Questions concerning any of the information provided in this report or requests for additional information should be addressed to Government Development Bank for Puerto Rico, P.O. Box 42001, San Juan, Puerto Rico, 00940-2001.

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO
(A Component Unit of the Commonwealth of Puerto Rico)

STATEMENT OF NET ASSETS (DEFICIENCY)
AS OF JUNE 30, 2011

ASSETS	Governmental Activities	Business-type Activities	Total
Cash and due from banks	$ -	$ 341,790,505	$ 341,790,505
Federal funds sold		88,850,000	88,850,000
Deposits placed with banks		219,315,862	219,315,862
Investments and investment contracts		3,775,241,121	3,775,241,121
Loans receivable — net		8,360,977,041	8,360,977,041
Accrued interest receivable		231,027,713	231,027,713
Due from (to) other funds	(127,674,517)	127,674,517	
Restricted assets:			
Cash and due from banks	4,193,481	1,423,514	5,616,995
Deposits placed with banks	68,101,498	453,046,031	521,147,529
Due from federal government	21,251,149		21,251,149
Investment and investment contracts	70,164,635	1,503,187,819	1,573,352,454
Loan receivable — net		34,981,843	34,981,843
Interest and other receivables	247,717	4,057,047	4,304,764
Real estate available for sale		1,926,940	1,926,940
Other assets	182,776	5,286,518	5,469,294
Real estate available for sale		126,641,380	126,641,380
Capital assets:			
Land and other nondepreciable assets		59,299,861	59,299,861
Other capital assets	41,711	11,708,153	11,749,864
Other receivables		75,874,423	75,874,423
Other assets	-	50,990,295	50,990,295
TOTAL	36,508,450	15,473,300,583	15,509,809,033
LIABILITIES			
Deposits, principally from the Commonwealth of Puerto Rico and its public entities:			
Demand		3,782,554,519	3,782,554,519
Certificates of deposit:			
Due within one year		1,738,468,217	1,738,468,217
Due in more than one year		32,664,518	32,664,518
Securities sold under agreements to repurchase — due in one year		970,818,550	970,818,550
Accrued interest payable		29,123,864	29,123,864
Accounts payable and accrued liabilities:			
Due within one year		52,108,194	52,108,194
Due in more than one year		6,196,208	6,196,208
Allowance for losses on guarantees and letters of credit:			
Due within one year		4,277,650	4,277,650
Due in more than one year		20,877,548	20,877,548
Certificates of indebtedness — due in one year		4,300,000	4,300,000
Participation agreement payable		26,000,000	26,000,000
Bonds and notes payable:			
Due within one year		91,138,136	91,138,136
Due in more than one year		5,391,934,330	5,391,934,330
Liabilities payable from restricted assets:			
Accrued interest payable	256,830	1,341,647	1,598,477
Accounts payable and accrued liabilities — due in one year	67,046,546	22,124,221	89,170,767
Allowance for losses on mortgage loan insurance		3,672,007	3,672,007
Bonds and mortgage-backed certificates payable:			
Due within one year		68,559,063	68,559,063
Due in more than one year	4,811,237	607,393,726	612,204,963
Total liabilities	72,114,613	12,853,552,398	12,925,667,011
NET ASSETS:			
Invested in capital assets	41,711	71,008,014	71,049,725
Restricted for:			
Mortgage loan insurance		61,118,599	61,118,599
Affordable housing programs	50,719,908	247,643,522	298,363,430
Other housing programs		2,566,860	2,566,860
Unrestricted net assets (deficit)	(86,367,782)	2,237,411,190	2,151,043,408
TOTAL NET ASSETS (DEFICIENCY)	$ (35,606,163)	$ 2,619,748,185	$ 2,584,142,022

See notes to basic financial statements.

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO
(A Component Unit of the Commonwealth of Puerto Rico)

STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2011

	Expenses	Program Revenues: Charges for Services - Fees, Commissions, and Others	Program Revenues: Charges for Services - Financing and Investment	Program Revenues: Operating Grants and Contributions	Net Revenues (Expenses) and Changes in Net Assets: Governmental Activities	Net Revenues (Expenses) and Changes in Net Assets: Business-Type Activities	Total
FUNCTIONS/PROGRAMS:							
Governmental activities:							
General government and other	$ 6,155,654	$ -	$ -	$ -	$ (6,155,654)	$ -	$ (6,155,654)
Housing assistance programs	311,950,727		4,690,670	279,608,816	(27,651,241)		(27,651,241)
Total governmental activities	318,106,381		4,690,670	279,608,816	(33,806,895)		(33,806,895)
Business-type activities:							
GDB Operating Fund	409,653,046	14,083,576	486,860,182			91,290,712	91,290,712
Housing Finance Authority	93,503,773	13,321,558	89,325,711			9,143,496	9,143,496
Tourism Development Fund	50,124,842	5,191,098	28,041,675			(16,892,069)	(16,892,069)
Public Finance Corporation	3,990		1,057			(2,933)	(2,933)
Capital Fund	36,828	35,116	1,025			(687)	(687)
Development Fund	10,947,552		(1,433,952)			(12,381,504)	(12,381,504)
Other nonmajor	110,134	2,381,351	4,897			2,276,114	2,276,114
Total business-type activities	564,380,165	35,012,699	602,800,595			73,433,129	73,433,129
Total	$ 882,486,546	$ 35,012,699	$ 607,491,265	$ 279,608,816	(33,806,895)	73,433,129	39,626,234
SPECIAL ITEM—Contribution from Puerto Rico Infrastructure Financing Authority						554,707	554,707
TRANSFERS IN (OUT) — Net					(219,990)	219,990	-
Total special item and transfers					(219,990)	774,697	554,707
CHANGE IN NET ASSETS					(34,026,885)	74,207,826	40,180,941
NET ASSETS — Beginning of year					(1,579,278)	2,545,540,359	2,543,961,081
NET ASSETS (DEFICIENCY) — End of year					$ (35,606,163)	$ 2,619,748,185	$ 2,584,142,022

See notes to basic financial statements.

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO
(A Component Unit of the Commonwealth of Puerto Rico)

BALANCE SHEET — GOVERNMENTAL FUNDS
AS OF JUNE 30, 2011

	HUD Programs	ARRA Funds	Closing Costs Assistance Program	My New Home Program	Other Nonmajor Governmental Funds	Eliminations	Total Governmental Funds
ASSETS:							
Due from other funds	$ -	$ -	$ -	$ -	$ 326,918	$ (303,809)	$ 23,109
Restricted:							
Cash and due from banks	1,910,472				2,283,009		4,193,481
Deposits placed with banks			10,657,011	32,028,000	25,416,487		68,101,498
Due from federal government	1,295,759	11,205,824			8,749,566		21,251,149
Investments and investment contracts					70,164,635		70,164,635
Due from other funds	241,573	276	827,797	3,084,709	16,979,591		21,133,946
Interest and other receivables	3,180		6,625	63,254	174,658		247,717
TOTAL	$ 3,450,984	$ 11,206,100	$ 11,491,433	$ 35,175,963	$ 124,094,864	$ (303,809)	$ 185,115,535
LIABILITIES:							
Due to other funds	$ 1,149,277	$ -	$ -	$ 40,119,127	$ 107,866,977	$ (303,809)	$ 148,831,572
Restricted — accounts payable and accrued liabilities	2,301,707	11,206,100	5,726,850	25,855,146	21,956,743		67,046,546
Deferred revenue					4,576,161	-	4,576,161
Total liabilities	3,450,984	11,206,100	5,726,850	65,974,273	134,399,881	(303,809)	220,454,279
FUND BALANCES (DEFICIT):							
Restricted for affordable housing programs			5,764,583		79,240,402		85,004,985
Unassigned	-	-	-	(30,798,310)	(89,545,419)		(120,343,729)
Total fund balances (deficit)	-	-	5,764,583	(30,798,310)	(10,305,017)	-	(35,338,744)
TOTAL	$ 3,450,984	$ 11,206,100	$ 11,491,433	$ 35,175,963	$ 124,094,864	$ (303,809)	$ 185,115,535

Amounts reported for governmental activities in the statement of net assets are different because:	
Total fund deficit	$ (35,338,744)
Deferred debt issue costs that are recorded as expenditures in governmental funds, but are capitalized in the government-wide financial statements	182,776
Capital assets used in governmental activities are not financial resources and, therefore, are not reported in the funds	41,711
Bonds and notes payable, are not due and payable in the current period and therefore are not reported in the funds	(4,811,237)
Accrued interest payable not due and payable in the current period	(256,830)
Revenues in the statement of activities that do not provide current financial resources are not reported as revenue in the funds	4,576,161
Net deficiency of governmental activities	$ (35,606,163)

See notes to basic financial statements.

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO
(A Component Unit of the Commonwealth of Puerto Rico)

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGE IN FUND BALANCES - GOVERNMENTAL FUNDS
FOR THE YEAR ENDED JUNE 30, 2011

	HUD Programs	ARRA Funds	Closing Costs Assistance Program	My New Home Program	Other Nonmajor Governmental Funds	Total Governmental Funds
REVENUES:						
Commonwealth appropriations for repayment of bonds and housing assistance programs	$ -	$ -	$ 36,774,000	$ -	$ 1,492,536	$ 38,266,536
Intergovernmental — federal government	127,100,197	95,739,443			11,807,876	234,647,516
Interest on investments	9		103,257	774	4,610,704	4,714,744
Net decrease in fair value of investments					(24,074)	(24,074)
Other	24,148		22,701	189,175	1,882,579	2,118,603
Total revenues	127,124,354	95,739,443	36,899,958	189,949	19,769,621	279,723,325
EXPENDITURES:						
Current:						
General government and other	4,980,335				1,175,319	6,155,654
Housing assistance programs	122,144,019	95,739,443	35,931,032	30,988,259	24,612,350	309,415,103
Capital outlays					41,711	41,711
Debt service —						
Interest					2,526,493	2,526,493
Total expenditures	127,124,354	95,739,443	35,931,032	30,988,259	28,355,873	318,138,961
EXCESS (DEFICIENCY) OF REVENUES OVER (UNDER) EXPENDITURES	-	-	968,926	(30,798,310)	(8,586,252)	(38,415,636)
OTHER FINANCING SOURCES (USES):						
Transfers-in					40,342,947	40,342,947
Transfers-out					(40,562,937)	(40,562,937)
Total other financing sources (uses)	-	-	-	-	(219,990)	(219,990)
NET CHANGE IN FUND BALANCES	-	-	968,926	(30,798,310)	(8,806,242)	(38,635,626)
FUND BALANCES (DEFICIT) — Beginning of year			4,795,657		(1,498,775)	3,296,882
FUND BALANCES (DEFICIT) — End of year	$ -	$ -	$ 5,764,583	$ (30,798,310)	$ (10,305,017)	$ (35,338,744)

Amounts reported for governmental activities in the statement of net assets are different because:	
Net change in fund balances - total governmental funds	(38,635,626)
Governmental funds report capital outlays as expenditures; however, in the statement of activities the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital outlays exceeded depreciation in the current period.	41,711
Revenues in the statement of activities that do provide current financial resources and not reported as revenues in the governmental funds.	4,576,161
Governmental funds report the effect of issuance costs when debt is first issued, whereas these costs are deferred and amortized in the statement of activities. This amount is the amortization for the year.	(9,131)
Change in net assets of governmental activities.	$ (34,026,885)

See notes to basic financial statements.

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO
(A Component Unit of the Commonwealth of Puerto Rico)

BALANCE SHEET — ENTERPRISE FUNDS
AS OF JUNE 30, 2011

ASSETS	GDB Operating Fund	Housing Finance Authority	Tourism Development Fund	Public Finance Corporation	Capital Fund	Development Fund	Other Nonmajor	Eliminations	Total Enterprise Funds
CURRENT ASSETS:									
Cash and due from banks	$ 341,723,688	$ 2,523,129	$ 21,885,011	$ 1,039,120	$ -	$11,182,785	$2,475,728	$ (39,038,956)	$ 341,790,505
Federal funds sold	88,850,000								88,850,000
Deposits placed with banks	156,016,947	57,382,535	38,272,670					(32,356,290)	219,315,862
Investments and investment contracts	800,067,569		3,708,800		242,961				804,019,330
Loans receivable, net	986,320,212	5,200,000	8,400,000			8,055,316		(8,400,000)	999,575,528
Accrued interest receivable	233,855,096	1,496,402	1,338,123	87	19	54,432	206	(5,716,652)	231,027,713
Other current receivables	13,733,864	498,551	1,404,102						15,636,517
Other current assets	368,638	4,940							373,578
Due from governmental funds	105,612,612	43,218,960							148,831,572
Restricted:									
Cash and due from banks		7,207,386						(5,783,872)	1,423,514
Deposits placed with banks	400,000,000	422,109,808						(369,063,777)	453,046,031
Investments and investment contracts	564,326,372	1,077,788							565,404,160
Loans receivable, net		528,000							528,000
Accrued interest receivable		2,329,085						(179,513)	2,149,572
Other current receivables		1,907,475							1,907,475
Total current assets	3,690,874,998	545,484,059	75,008,706	1,039,207	242,980	19,292,533	2,475,934	(460,539,060)	3,873,879,357
NONCURRENT ASSETS:									
Restricted:									
Investments and investment contracts	435,792,149	700,143,202						(198,151,692)	937,783,659
Loans receivable, net		34,453,843							34,453,843
Real estate available for sale		1,926,940							1,926,940
Other assets		5,286,518							5,286,518
Investments and investment contracts	2,913,550,162	18,286,389	198,869,775			3,642,563		(163,127,098)	2,971,221,791
Loans receivable, net	7,211,520,610	206,621,055	337,083,379					(393,823,531)	7,361,401,513
Real estate available for sale	125,679,219	962,161							126,641,380
Capital assets:									
Land and other nondepreciable assets	59,299,861								59,299,861
Other capital assets	8,605,180	3,102,973							11,708,153
Other receivables	60,237,906								60,237,906
Other assets	41,446,933	8,880,000	289,784						50,616,717
Total noncurrent assets	10,856,132,020	979,663,081	536,242,938	-	-	3,642,563	-	(755,102,321)	11,620,578,281
TOTAL ASSETS	$14,547,007,018	$1,525,147,140	$611,251,644	$ 1,039,207	$ 242,980	$22,935,096	$2,475,934	$(1,215,641,381)	$15,494,457,638

See notes to basic financial statements.

(Continued)

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO
(A Component Unit of the Commonwealth of Puerto Rico)

BALANCE SHEET — ENTERPRISE FUNDS
AS OF JUNE 30, 2011

LIABILITIES AND NET ASSETS	GDB Operating Fund	Housing Finance Authority	Tourism Development Fund	Public Finance Corporation	Capital Fund	Development Fund	Other Nonmajor	Eliminations	Total
Current liabilities:									
Deposits, principally from the Commonwealth of Puerto Rico and its public entities:									
Demand	$ 3,829,716,026	$ -	$ -	$ -	$ -	$ -	$ -	$ (47,161,507)	$ 3,782,554,519
Certificates of deposit	2,139,888,284							(401,420,067)	1,738,468,217
Certificates of indebtedness	4,300,000								4,300,000
Securities sold under agreements to repurchase	970,818,550								970,818,550
Accrued interest payable	29,270,930	26,845	5,722,254					(5,896,165)	29,123,864
Accounts payable and accrued liabilities	36,874,760	11,573,057	1,207,913	49,960	11,414	4,563	47,848	2,338,679	52,108,194
Allowance for losses on guarantees and letters of credit			2,777,650			1,500,000			4,277,650
Due to governmental funds	21,133,946	23,109							21,157,055
Notes payable	91,138,136		8,400,000					(8,400,000)	91,138,136
Total current liabilities payable from unrestricted assets	7,123,140,632	11,623,011	18,107,817	49,960	11,414	1,504,563	47,848	(460,539,060)	6,693,946,185
Current liabilities payable from restricted assets:									
Accrued interest payable		1,341,647							1,341,647
Accounts payable and accrued liabilities		22,124,221							22,124,221
Bonds and notes payable		68,559,063							68,559,063
Total current liabilities	7,123,140,632	103,647,942	18,107,817	49,960	11,414	1,504,563	47,848	(460,539,060)	6,785,971,116
Noncurrent liabilities:									
Certificates of deposit, principally from the Commonwealth of Puerto Rico and its public entities	230,816,210							(198,151,692)	32,664,518
Allowance for losses on guarantees and letters of credit			20,877,548						20,877,548
Accounts payable and accrued liabilities	5,173,292		1,022,916						6,196,208
Participation agreement payable			26,000,000						26,000,000
Bonds and notes payable	5,391,934,330	2,707,055	391,116,476					(393,823,531)	5,391,934,330
Noncurrent liabilities payable from restricted assets:									
Allowance for losses on mortgage loan insurance		3,672,007							3,672,007
Bonds, notes, and mortgage-backed certificates payable		770,520,824						(163,127,098)	607,393,726
Total noncurrent liabilities	5,627,923,832	776,899,886	439,016,940					(755,102,321)	6,088,738,337
Total liabilities	12,751,064,464	880,547,828	457,124,757	49,960	11,414	1,504,563	47,848	(1,215,641,381)	12,874,709,453
NET ASSETS:									
Invested in capital assets	67,905,041	3,102,973							71,008,014
Restricted for:									
Mortgage loan insurance		61,118,599							61,118,599
Affordable housing programs		247,643,522							247,643,522
Other housing programs		2,566,860							2,566,860
Unrestricted	1,728,037,513	330,167,358	154,126,887	989,247	231,566	21,430,533	2,428,086		2,237,411,190
Total net assets	1,795,942,554	644,599,312	154,126,887	989,247	231,566	21,430,533	2,428,086		2,619,748,185
TOTAL LIABILITIES AND NET ASSETS	$14,547,007,018	$1,525,147,140	$611,251,644	$ 1,039,207	$ 242,980	$22,935,096	$2,475,934	$(1,215,641,381)	$15,494,457,638

See notes to basic financial statements.

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO
(A Component Unit of the Commonwealth of Puerto Rico)

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET ASSETS — ENTERPRISE FUNDS
FOR THE YEAR ENDED JUNE 30, 2011

	GDB Operating Fund	Housing Finance Authority	Tourism Development Fund	Public Finance Corporation	Capital Fund	Development Fund	Other Nonmajor	Total
OPERATING REVENUES:								
Investment income:								
Interest income on federal funds sold	$ 1,355,702	$ -	$ -	$ -	$ -	$ -	$ -	$ 1,355,702
Interest income on deposits placed with banks	351,276	24,334,076	560,040	1,057		17,092	4,897	25,268,438
Interest and dividend income on investments and investment contracts	45,566,123	43,134,124	1,682,506		1,025	320,976		90,704,754
Net increase (decrease) in fair value of investments	33,805,166	7,131,672	14,018,345			(1,772,020)		53,183,163
Total investment income (loss)	81,078,267	74,599,872	16,260,891	1,057	1,025	(1,433,952)	4,897	170,512,057
Interest income on loans receivable:								
Public sector	405,528,470							405,528,470
Private sector	253,445	14,725,839	11,780,784					26,760,068
Total interest income on loans receivable	405,781,915	14,725,839	11,780,784			-		432,288,538
Total investment income (loss) and interest income on loans receivable	486,860,182	89,325,711	28,041,675	1,057	1,025	(1,433,952)	4,897	602,800,595
Noninterest income:								
Fiscal agency fees	5,690,900	170,628						5,861,528
Commitment, guarantee and other service fees	7,860,072	7,919,704	5,142,247					20,922,023
Mortgage loan insurance premiums		3,774,823						3,774,823
Other income	532,604	1,456,403	48,851		35,116		2,381,351	4,454,325
Total noninterest income	14,083,576	13,321,558	5,191,098		35,116		2,381,351	35,012,699
Total operating revenues	500,943,758	102,647,269	33,232,773	1,057	36,141	(1,433,952)	2,386,248	637,813,294
OPERATING EXPENSES:								
Provision (credit) for loan losses	(5,550,286)	7,546,703	31,052,104			9,319,708		42,368,229
Interest expense:								
Deposits	94,023,109							94,023,109
Securities sold under agreements to repurchase	15,602,648							15,602,648
Commercial paper	18,000							18,000
Certificates of indebtedness	20,181							20,181
Bonds, notes and mortgage-backed certificates	255,033,613	56,486,645	14,838,833					326,359,091
Total interest expense	364,697,551	56,486,645	14,838,833					436,023,029
Noninterest expenses:								
Salaries and fringe benefits	23,270,179	12,290,185	120,177				73,093	35,753,634
Depreciation and amortization	1,406,622	1,126,536						2,533,158
Occupancy and equipment costs	3,724,235	2,214,383						5,938,618
Legal and professional fees	3,292,270	3,456,492	1,569,703	3,990	36,015	63,790	21,850	8,444,110
Office and administrative	326,621	965,664	121,027		813			1,414,125
Subsidy and trustee fees	53,435	367,072						420,507
Provision (credit) for losses on guarantees and letters of credit	(1,000,000)		2,370,598			1,496,066		2,866,664
Loss on sale of real estate available for sale		185,036						185,036
Other	3,585,903	8,456,722	52,400			67,988	15,191	12,178,204
Total noninterest expenses	34,659,265	29,062,090	4,233,905	3,990	36,828	1,627,844	110,134	69,734,056
Total operating expenses	393,806,530	93,095,438	50,124,842	3,990	36,828	10,947,552	110,134	548,125,314
OPERATING INCOME (LOSS)	107,137,228	9,551,831	(16,892,069)	(2,933)	(687)	(12,381,504)	2,276,114	89,687,980
NONOPERATING EXPENSES — Contributions to Cooperative Development Investment Trust Fund and others	(15,846,516)	(408,335)						(16,254,851)
SPECIAL ITEM — Contribution from Puerto Rico Infrastructure Financing Authority	554,707							554,707
TRANSFERS-IN		961,032					178,000	1,139,032
TRANSFERS-OUT	(178,000)	(741,042)						(919,042)
CHANGE IN NET ASSETS	91,667,419	9,363,486	(16,892,069)	(2,933)	(687)	(12,381,504)	2,454,114	74,207,826
NET ASSETS — Beginning of year	1,704,275,135	635,235,826	171,018,956	992,180	232,253	33,812,037	(26,028)	2,545,540,359
NET ASSETS — End of year	$1,795,942,554	$644,599,312	$154,126,887	$ 989,247	$ 231,566	$ 21,430,533	$ 2,428,086	$2,619,748,185

See notes to basic financial statements.

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO
(A Component Unit of the Commonwealth of Puerto Rico)

STATEMENT OF CASH FLOWS — ENTERPRISE FUNDS
FOR THE YEAR ENDED JUNE 30, 2011

	GDB Operating Fund	Housing Finance Authority	Tourism Development Fund	Public Finance Corporation	Capital Fund	Development Fund	Other Nonmajor	Eliminations	Total Enterprise Funds
CASH FLOWS FROM OPERATING ACTIVITIES:									
Cash received from interest on housing program loans	$ -	$ 10,766,006	$ -	$ -	$ -	$ -	$ -	$ -	$ 10,766,006
Cash paid for housing program loans originated		(50,468,200)							(50,468,200)
Principal collected on housing program loans		25,569,912							25,569,912
Guarantee fees collected			3,855,638						3,855,638
Payment of guarantees and letters of credit						(2,486,870)			(2,486,870)
Cash received from other operating noninterest revenues	23,627,549	10,040,604	48,853		35,116				33,752,122
Cash payments for other operating noninterest expenses	(30,969,120)	(17,987,321)	(752,056)	(16,380)	(42,672)	(132,149)	(116,327)	1,731,591	(48,284,434)
Cash received from mortgage loans insurance premiums		4,390,197							4,390,197
Due from/to governmental funds	(6,303,598)	(41,083,851)							(47,387,449)
Net cash provided by (used in) operating activities	(13,645,169)	(58,772,653)	3,152,435	(16,380)	(7,556)	(2,619,019)	(116,327)	1,731,591	(70,293,078)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES:									
Contributions to others	(15,846,516)	(408,335)							(16,254,851)
Contributions from Puerto Rico Infrastructure Financing Authorit	554,707								554,707
Transfers in		961,032					178,000		1,139,032
Transfers out	(178,000)	(741,042)							(919,042)
Net increase (decrease) in:									
Deposits	498,641,152							30,200,177	528,841,329
Certificates of deposit	(1,286,602,638)							162,250,819	(1,124,351,819)
Certificates of indebtedness	(7,500,000)								(7,500,000)
Proceeds from issuance of securities sold under agreements to repurchase	4,477,337,335								4,477,337,335
Payment of securities sold under agreements to repurchase	(4,565,353,537)								(4,565,353,537)
Proceeds from issuance of bonds and notes	3,502,889,000	87,571,395	35,572,126					(36,003,520)	3,590,029,001
Repayments of bonds and notes	(1,375,440,000)	(155,825,308)	(7,700,000)					8,919,926	(1,530,045,382)
Payment of debt issue costs	(36,583,443)	(64,149)							(36,647,592)
Interest paid	(343,573,857)	(22,728,406)	(4,112,588)					9,646,014	(360,768,837)
Net cash provided by (used in) noncapital financing activities	848,344,203	(91,234,813)	23,759,538				178,000	175,013,416	956,060,344
CASH FLOWS FROM CAPITAL AND RELATED FINANCING - Purchase of capital assets	$ (708,419)	$ (628,156)	$ -	$ -	$ -	$ -	$ -	$ -	$ (1,336,575)

See notes to basic financial statements.

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO

(A Component Unit of the Commonwealth of Puerto Rico)

STATEMENT OF CASH FLOWS — ENTERPRISE FUNDS
FOR THE YEAR ENDED JUNE 30, 2011

	GDB Operating Fund	Housing Finance Authority	Tourism Development Fund	Public Finance Corporation	Capital Fund	Development Fund	Other Nonmajor	Eliminations	Total Enterprise Funds
CASH FLOWS FROM INVESTING ACTIVITIES:									
Net decrease (increase) in:									
Federal funds sold	242,150,000								242,150,000
Deposits placed with banks	(548,390,398)	41,945,801	39,169,231					(166,232,884)	(633,508,250)
Purchases of investments	(13,923,370,822)	(136,508,708)	(100,165,833)		(35,116)			8,104,417	(14,151,976,062)
Proceeds from sales and redemptions of investments	14,798,740,108	179,971,465	76,030,838		42,610	2,375,000		(4,122,352)	15,053,037,669
Interest and dividends received on investments	25,410,543	67,045,623	1,390,952	1,057	62	339,798	7,305	(11,636,361)	82,558,979
Interest received on other than housing program loans	281,004,198		1,192,932					1,990,347	284,187,477
Origination of other than housing program loans	(4,598,831,424)	(29,203,000)	(55,199,962)			(15,176,272)		36,003,520	(4,662,407,138)
Fees collected on other than housing program loans		8,229,266							8,229,266
Principal collected on other than housing program loans	3,237,462,936		8,780,790					(8,919,926)	3,237,323,800
Proceeds from sale of real estate available for sale	3,125,000	1,333,088							4,458,088
Disbursements for acquisition and improvements to real estate available for sale	(15,019,416)	(4,102,241)							(19,121,657)
Net cash provided by (used in) investing activities	(497,719,275)	128,711,294	(28,801,052)	1,057	7,556	(12,461,474)	7,305	(144,813,239)	(555,067,828)
NET CHANGE IN CASH AND DUE FROM BANKS	336,271,340	(21,924,328)	(1,889,079)	(15,323)		(15,080,493)	68,978	31,931,768	329,362,863
CASH AND DUE FROM BANKS — Beginning of year	5,452,348	31,654,843	23,774,090	1,054,443		26,263,278	2,406,750	(76,754,596)	13,851,156
CASH AND DUE FROM BANKS — End of year	$ 341,723,688	$ 9,730,515	$ 21,885,011	$ 1,039,120	$ -	$11,182,785	$2,475,728	$ (44,822,828)	$ 343,214,019
RECONCILIATION TO ENTERPRISE FUNDS BALANCE SHEET:									
Cash – unrestricted	$ 341,723,688	$ 2,523,129	$ 21,885,011	$ 1,039,120	$ -	$11,182,785	$2,475,728	$ (39,038,956)	$ 341,790,505
Cash – restricted		7,207,386						(5,783,872)	1,423,514
TOTAL CASH AT YEAR END	$ 341,723,688	$ 9,730,515	$ 21,885,011	$ 1,039,120	$ -	$11,182,785	$2,475,728	$ (44,822,828)	$ 343,214,019

See notes to basic financial statements.

(Continued)

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO
(A Component Unit of the Commonwealth of Puerto Rico)

STATEMENT OF CASH FLOWS — ENTERPRISE FUNDS
FOR THE YEAR ENDED JUNE 30, 2011

	GDB Operating Fund	Housing Finance Authority	Tourism Development Fund	Public Finance Corporation	Capital Fund	Development Fund	Other Nonmajor	Eliminations	Total Enterprise Funds
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES:									
Operating income (loss)	$ 107,137,228	$ 9,551,831	$(16,892,069)	$ (2,933)	$ (687)	$ (12,381,504)	$ 2,276,114	$ -	$ 89,687,980
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities:									
Investment income	(47,273,101)	(67,468,200)	(2,242,546)	(1,057)	(1,025)	(338,068)	(4,897)		(117,328,894)
Interest income on other than housing program loans	(405,781,915)		(11,780,784)						(417,562,699)
Capitalized interest on housing program loans		(3,721,006)							(3,721,006)
Interest expense	364,697,551		14,838,833						379,536,384
Provision (credit) for loan losses	(5,550,286)	7,546,703	31,052,104			9,319,708			42,368,229
Provision for losses on guarantees and letters of credit	(1,000,000)		2,370,598			1,496,066			2,866,664
Provision for losses on mortgage loan insurance		3,325,677							3,325,677
Payment of guarantees						(2,486,870)			(2,486,870)
Net decrease (increase) in fair value of investments	(33,805,166)	(7,131,672)	(14,018,345)			1,772,020			(53,183,163)
Provision for losses on real estate available for sale		4,089,470							4,089,470
Provision for losses on other assets	1,307,596	20,000							1,327,596
Loss on sale of real estate available for sale		185,036							185,036
Depreciation and amortization	1,406,622	1,126,536							2,533,158
Interest expense		56,486,645							56,486,645
Origination of housing program loans		(50,468,200)							(50,468,200)
Collections of housing program loans		25,569,912							25,569,912
Changes in operating assets and liabilities									
Interest receivable on housing program loans		(245,002)							(245,002)
Increase in other assets	10,170,718	588,190							10,758,908
Increase (decrease) in other liabilities	1,349,182	2,855,278	(175,356)	(12,390)	(5,844)	(371)	(2,387,544)	1,731,591	3,354,546
Due from/to governmental funds	(6,303,598)	(41,083,851)	-	-	-	-	-	-	(47,387,449)
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	$ (13,645,169)	$(58,772,653)	$ 3,152,435	$ (16,380)	$ (7,556)	$ (2,619,019)	$ (116,327)	$ 1,731,591	$ (70,293,078)

See notes to basic financial statements.

(Continued)

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO
(A Component Unit of the Commonwealth of Puerto Rico)

STATEMENT OF CASH FLOWS — ENTERPRISE FUNDS
FOR THE YEAR ENDED JUNE 30, 2011

	GDB Operating Fund	Housing Finance Authority	Tourism Development Fund	Public Finance Corporation	Capital Fund	Development Fund	Other Nonmajor	Eliminations	Total Enterprise Funds
Noncash investing and noncapital financing activities:									
Accretion of discount on investment securities	$ 12,957,342	$ 12,629,939	$ 864,625	$ -	$ 3,847	$ -	$ -	$ (12,368,600)	$ 14,087,153
Capitalized interest on loans and other	28,142,139	3,721,006	10,557,068					(8,864,142)	33,556,071
Mortgage loans issued not requiring cash disbursement:		29,060,000							29,060,000
Decrease in fair value of real estate held for sale transferred to other receivables	(37,637,417)								(37,637,417)
Transfer of real estate available for sale to capital assets	56,454,861								56,454,861
Accretion of premium (discount) on:									
Deposits	(12,368,600)							12,368,600	
Bonds payable	2,132,926	(32,957,275)	(8,864,142)					21,161,794	(18,526,697)
Increase (decrease) in fair value of investments	33,805,166	7,131,672	14,018,345			(1,772,020)		(12,297,652)	40,885,511
Amortization of bond issue cost (included in interest expense)	20,183,224	943,373							21,126,597
Amortization of deferred loss		309,144							309,144
Transfer of mortgage loans receivable to other real estate held for sale		1,628,792							1,628,792

(Concluded)

See notes to basic financial statements.

1. REPORTING ENTITY

Government Development Bank for Puerto Rico (the "Bank" or "GDB") is a component unit of the Commonwealth of Puerto Rico (the "Commonwealth") created by Act No. 17 of September 23, 1948, as amended. The Bank's principal functions are to act as fiscal agent for the Commonwealth and its public entities and to make loans to public entities and private enterprises, which will further the economic development of Puerto Rico. The charter of the Bank provides for its perpetual existence, and no amendment to the charter, or to any other law of Puerto Rico, shall impair any outstanding obligations or commitments of the Bank. The Bank is exempt from taxation in Puerto Rico. The Bank's charter, as amended, allows the Bank to invest in securities issued by any corporate entity engaged in the economic development of Puerto Rico, as well as to guarantee loans and other obligations incurred by public and private entities.

Pursuant to Act No. 82 of June 16, 2002, which amended the Bank's enabling legislation, the Bank may transfer annually to the general fund of the Commonwealth up to 10% of its net income or $10 million, whichever is greater. Management of the Bank has defined net income as the increase in unrestricted net assets of business-type activities for a fiscal year. The Bank's board of directors approved such definition. The Bank did not make this transfer for the year ended June 30, 2011.

The Bank has the following blended component units: Puerto Rico Housing Finance Authority (the "Housing Finance Authority"), Puerto Rico Tourism Development Fund (the "Tourism Development Fund"), Puerto Rico Development Fund (the "Development Fund"), Puerto Rico Public Finance Corporation (the "Public Finance Corporation"), Government Development Bank for Puerto Rico Capital Fund (the "Capital Fund"), José M. Berrocal Finance and Economics Institute ("JMB Institute"), and Puerto Rico Higher Education Assistance Corporation (the "Education Assistance Corporation"). The balances and transactions of the component units discussed above have been blended with those of the Bank in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) because, while legally separate, they were created and can be dissolved through resolutions of the Bank's board of directors. The board of directors of each of the blended component units is substantially the same as that of the Bank. Financial statements of each major blended component unit may be obtained from the Bank.

The Housing Finance Authority (formerly known as the Puerto Rico Housing Finance Corporation) was created in 1977 to provide public and private housing developers with interim and permanent financing through mortgage loans for the construction, improvement, operation, and maintenance of rental housing for low and moderate-income families. The Housing Finance Authority also issues bonds and notes, the proceeds of which are deposited in separate trusts and generally invested in mortgaged-backed securities collateralized by mortgage loans on properties located in Puerto Rico purchased by low and moderate-income families. The Housing Finance Authority is authorized by the U.S. Department of Housing and Urban Development (HUD) to administer the U.S. Housing Act Section 8 program in Puerto Rico and to act as an approved mortgagor, both for multifamily rental units and for single-family homes. In addition, it is an authorized issuer of Government National Mortgage Association (GNMA) mortgage-backed securities, and is Puerto Rico's State Credit Agency for the Low-Income Housing Tax Credit Program under Section 42 of the U.S. Internal Revenue Code. Effective July 1, 2010, the Housing Finance Authority was also authorized by HUD to administer the HOME Investment Partnerships Program.

The Housing Finance Authority, in conjunction with the Puerto Rico Department of Housing, is the entity responsible for certifying projects under the New Secure Housing Program (known in Spanish as "Nuevo Hogar Seguro"), with the approval of the Federal Emergency Management Agency (FEMA). This program is directed to plan, coordinate, and develop the construction of new housing as a replacement to those destroyed by Hurricane Georges in 1998, and to attend the housing needs of families living in flood zone areas.

The Tourism Development Fund was created in 1993 to promote the hotel and tourism industry of the Commonwealth, primarily through the issuance of letters of credit and guarantees. The Tourism Development Fund is also authorized to make capital investments and provide direct financing to tourism-related projects.

The Development Fund was created in 1977 to expand the sources of financing available for the development of the private sector of the economy of Puerto Rico and to complement the Bank's lending program. The Development Fund may also guarantee obligations of private sector enterprises and invest in their equity securities.

The Public Finance Corporation was created in 1984 to provide the agencies and instrumentalities of the Commonwealth with alternate means of satisfying financial needs. The resolution creating the Public Finance Corporation states that if it were to be dissolved or cease to exist without a successor public entity being appointed, any funds or assets not required for the payment of its bonds or any other obligation, will be transferred to the Secretary of the Department of the Treasury of the Commonwealth (the "Department of the Treasury") for deposit in the Commonwealth's general fund.

The Capital Fund was created in 1992 to expand the investment options available to the Bank and to administer, separately from the Bank's general investment operations, an equity investments process through professional equity investment managers. On May 31, 2010, the board of directors of the Capital Fund authorized the transfer of its investments portfolio of approximately $72 million to the Tourism Development Fund. The transfer was completed on June 30, 2010. The Capital Fund's activities have been reduced significantly after June 30, 2010.

Other nonmajor funds include the JMB Institute and the Education Assistance Corporation. The JMB Institute was created in 2002 to complement the Bank's mission of promoting economic development by providing specialized training on the theory and practice of public finances and economics to talented young professionals in order to attract them to join the public service. The Education Assistance Corporation was created in 1981 to administer the Stafford Loan Program in Puerto Rico and guarantee the payment of student loans granted by financial institutions in Puerto Rico under certain terms and restrictions. The operations of this fund were transferred to a guarantee agency designated by the U.S. Department of Education. The Education Assistance Corporation is currently inactive.

To minimize its risk of loss, the Bank purchases insurance coverage for public liability, hazard, automobile, crime, and bonding as well as workmen's insurance for employees. The selection of the insurer has to be approved by the Public Insurance Office of the Department of the Treasury. Insurance coverage is updated annually to account for changes in operating risk. For the last three years, insurance settlements have not exceeded the amount of coverage.

2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of the Bank conform to accounting principles generally accepted in the United States of America (U.S. GAAP), as applicable to governmental entities. The Bank follows

Governmental Accounting Standards Board (GASB) statements under the hierarchy established by Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, in the preparation of its financial statements. The Bank has elected to apply all Financial Accounting Standards Board's pronouncements issued after November 30, 1989, in accounting and reporting for its enterprise funds and business type activities to the extent they do not conflict with GASB pronouncements.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

Government-Wide and Fund Financial Statements:

Government-Wide Financial Statements — The statement of net assets (deficiency) and the statement of activities report information on all activities of the Bank. The effect of interfund balances has been removed from the government-wide statement of net assets, except for the residual amounts due between governmental and business-type activities. Interfund charges for services among functions of the government-wide statement of activities have not been eliminated. The Bank's activities are distinguished between governmental and business-type activities. Governmental activities generally are financed through intergovernmental revenues and other nonexchange revenues. Business-type activities are financed in whole or in part by fees charged to external parties for goods or services and interest earned on investment securities and loans. Following is a description of the Bank's government-wide financial statements.

The statement of net assets (deficiency) presents the Bank's assets and liabilities, with the difference reported as net assets (deficiency). Net assets are reported in three categories:

- Invested in capital assets, net of any related debt, consists of capital assets, net of accumulated depreciation and amortization and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets.
- Restricted net assets result when constraints placed on net assets use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- Unrestricted net assets (deficiency) consist of net assets (deficiency) that do not meet the definition of the two preceding categories. Unrestricted net assets often are designated, in order to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on use that are imposed by management, but such constraints may be removed or modified.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable within a specific function. Program revenues include: (1) interest income on loans and investments, changes in the fair value of investments, and fees and charges to customers for services rendered or for privileges provided, and (2) grants and contributions that are restricted to meet the operational or capital requirements of a particular function. Other items not meeting the definition of program revenues are reported as general revenues.

Fund Financial Statements — Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts. The financial activities of the Bank that are reported in the accompanying basic financial statements have been classified into governmental and enterprise funds.

Separate financial statements are provided for governmental funds and enterprise funds. Major individual governmental and enterprise funds are reported as separate columns in the fund financial statements, with nonmajor funds being combined into a single column. Fund balances at the beginning of the year are restated to reflect changes in major fund definition. In the case of enterprise funds, each individual blended component unit of the Bank with the exception of JMB Institute and Education Assistance Corporation, which have been grouped as other nonmajor funds, has been reported as a separate major fund in the fund financial statements. In the case of the Housing Finance Authority, all of its activities not classified and reported as governmental funds have been reported as an enterprise fund.

Fund balances for each governmental fund are displayed in the following classifications depicting the relative strength of the spending constraints placed on the purposes for which resources can be used:

- Nonspendable — amounts that cannot be spent because they are either not in a spendable form (such as inventories and prepaid amounts) or are legally or contractually required to be maintained intact.

- Restricted — amounts that can be spent only for specific purposes because of constraints imposed by external providers (such as grantors, bondholders, and higher levels of government), or imposed by constitutional provisions or enabling legislation.

- Committed — amounts that can be spent only for specific purposes determined by a formal action of the government's highest level of decision-making authority.

- Assigned — amounts the government intends to use for specific purposes that do not meet the criteria to be classified as restricted or committed.

- Unassigned — amounts that are available for any purpose.

Measurement Focus, Basis of Accounting, and Financial Statements Presentation:

Government-Wide Financial Statements — The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenues as soon as all eligibility requirements imposed by the provider have been met.

Governmental Funds' Financial Statements — The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Bank considers revenues to be available if they are collected within 120 days after the end of the fiscal year. Principal revenue sources considered susceptible to accrual include federal and Commonwealth funds to be received by the HUD Programs, ARRA Funds and Closing Costs Assistance Program. Other revenues are considered to be measurable and available only when cash is received. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. Modifications to the accrual basis of accounting include:

- Employees' vested annual leave is recorded as expenditure when utilized. The amount of accumulated annual leave unpaid at June 30, 2011 is reported only in the government-wide financial statements.

- Interest on general long-term obligations is generally recognized when paid.

- Debt service principal expenditures and claims and judgments are recorded only when payment is due.

Governmental Funds — The following governmental activities of the Bank are classified as major governmental funds:

- HUD Programs — This special revenue fund accounts for the subsidy to low and moderate-income families for the rental of decent and safe dwellings under the U.S. Housing Act Section 8 programs.

- ARRA Funds — This special revenue fund accounts for funds received under Title XII and Section 1602 of the American Recovery and Reinvestment Act of 2009. Title XII is a grant program that provides funds for capital investments in low-income housing tax credit projects. Section 1602 grants funds to states to finance construction or acquisition and rehabilitation of qualified low-income buildings for low-income housing in lieu of low-income housing tax credits.

- Closing Costs Assistance Program — This special revenue fund accounts for revenues received mainly from appropriations from the Commonwealth to provide subsidies to eligible individuals or families for the purchase of an eligible principal residence.

- My New Home Program — This special revenue fund accounts for revenues provided by Act 122 of August 6, 2010, which assigned to the Housing Finance Authority, for a period of seven years, a portion of no less than 80% of the unreserved monies and other liquid funds abandoned or unclaimed in the financial institutions that will be transferred to the general funds of the Commonwealth.

  The following governmental activities of the Bank are accounted for in other nonmajor governmental funds:

- Affordable Housing Mortgage Subsidy Program (Stages 2, 3, 6, 7, 8, 9, 10 and 11) — These special revenue funds are used to account for the proceeds of specific revenue sources under Stages 2, 3, 6, 7, 8, 9, 10 and 11 of the Affordable Housing Mortgage Subsidy Program (AHMSP) that are legally restricted for expenditures to promote the origination of mortgage loans by financial institutions in the private sector to low and moderate-income families. Under these stages, the Housing Finance Authority provides subsidy for the down payment and/or the principal and interest payments on mortgage loans originated under a predetermined schedule of originations and, in the case of Stages 9, 10, and 11, to acquire such mortgages in the form of mortgage-backed securities issued by the financial institutions. Loans originated, as well as servicing, are kept by the originating financial institution. There was no open schedule of originations under these stages as of June 30, 2011.

- AHMSP Act No. 124 — This special revenue fund accounts for excess subsidy funds as well as accumulated net assets, released periodically from arbitrage structures used to provide housing assistance.

- Affordable Housing Mortgage Subsidy Mortgage-Backed Certificates — This special revenue fund is used to account for specific revenue sources used to provide subsidy for the mortgages underlying the mortgage-backed securities held as collateral for the mortgage-backed certificates issued in fiscal year 2007.

- New Secure Housing Program — This special revenue fund is used to account for federal and local resources directed to plan, coordinate, and develop the construction of new housing units as a replacement for those destroyed by Hurricane Georges in 1998 and to assist with the housing needs of those families living in hazard prone areas.

- HOME Program — Effective July 1, 2010, the Housing Finance Authority was certified by the HUD to administer the HOME Investment Partnerships ("HOME") Program. The objectives of the HOME Program include: (1) expanding the supply of decent and affordable housing, particularly housing for low- and very low-income families; (2) strengthening the abilities of state and local governments to design and implement strategies for achieving adequate supplies of decent, affordable housing; (3) providing financial and technical assistance to participating jurisdictions, including the development of model programs for affordable low-income housing; and (4) extending and strengthening partnerships among all levels of government and the private sector, including for-profit and nonprofit organizations, in the production and operation of affordable housing.

- Protecting Your Home Program — This special revenue fund accounts for mortgage payment subsidy for up to 18 months or $20,000, whichever is lower, and is intended to reduce the amount of home foreclosures among low- and moderate-income families with recent financial difficulties. This loss mitigation program was financed with $20 million of excess funds from previous bond issuances under the AHMSP.

Enterprise Funds' Financial Statements — The financial statements of the enterprise funds are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide statements described above.

Enterprise funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses are those that result from the Bank and its components units providing the services that correspond to their principal ongoing operations. Operating revenues are generated from lending, investing, banking and fiscal agency services, and other related activities. Operating expenses include interest expense, any provision for losses on loans, advances, letters of credit, or guarantees and all general and administrative expenses, among others. Revenues and expenses not meeting these definitions are reported as nonoperating revenues and expenses.

Securities Purchased Under Agreements to Resell — The Bank enters into purchases of securities under agreements to resell. The amounts advanced under these agreements generally represent short-term loans and are reflected as an asset. The securities underlying these agreements are usually held by the broker or his/her agent with whom the agreement is transacted. There were no securities purchased under agreements to resell outstanding at June 30, 2011.

Investments and Investment Contracts — Investments and investment contracts are carried at fair value, except for money market instruments and participating investment contracts with a remaining maturity at the time of purchase of one year or less, and nonparticipating investment contracts (guaranteed investment contracts), which are carried at cost; and investment positions in 2a-7 like external investment pools, which are carried at the pools' share price. Fair value is determined based on quoted market prices and quotations received from independent broker/dealers or pricing service organizations. Realized gains and losses from the sale of investments and unrealized changes in the fair value of outstanding investments are included in net increase (decrease) in fair value of investments.

Loans Receivable and Allowance for Loan Losses — Loans in the enterprise funds are presented at the outstanding unpaid principal balance reduced by an allowance for loan losses. The accrual of interest on loans to the private sector ceases when loans become past due over six months. For loans to public sector entities, the accrual of interest ceases when management determines that all of the following characteristics are present: (a) a loan is six months past due; (b) it has no current source of repayment; (c) it is not covered by a formal commitment from the Commonwealth; and (d) it has no designated collateral or such collateral is insufficient. Once a loan is placed in nonaccrual status, all accrued interest receivable is reversed from interest income. Interest income on nonaccrual loans is thereafter recognized as income only to the extent actually collected. Nonaccrual loans are returned to an accrual status when management has adequate evidence to believe that the loans will be performing as contracted.

The allowance for loan losses is established through provisions recorded in the fund financial statements. This allowance is based on management's evaluation of the risk characteristics of the loan including such factors as the nature of individual credits outstanding, past loss experience, known and inherent risks in the portfolios, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, and general economic conditions. Loan charge-offs are recorded against the allowance when management believes that the collection of the principal is unlikely. Recoveries of amounts previously charged off are credited to the respective allowance. Because of uncertainties inherent in the estimation process, management estimate of credit losses in the outstanding loans receivable portfolios and the related allowance may change in the near future.

Management, considering current information and events regarding the borrowers' ability to repay their obligations, considers a loan to be impaired when it is probable that the Bank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Interest income and cash receipts on impaired loans are accounted for predominantly in the same manner as nonaccrual loans.

Loans considered to be impaired are generally reduced to the present value of expected future cash flows, discounted at the loan's effective interest rate or, as a practical expedient, at the loan's observable market price or the fair value of the collateral if the loan is collateral dependent, by establishing a valuation allowance.

Loans to the Commonwealth of Puerto Rico, its agencies and instrumentalities amounted to approximately $6.0 billion or 38.7% of the Bank's total assets as of June 30, 2011. These loans are expected to be collected from appropriations from, proceeds from bond issuances of, or revenues generated by, the Commonwealth, its agencies and instrumentalities. The Commonwealth's recurring expenditures have exceeded its recurring revenues during the past years and its credit ratings have been lowered. In addition, many of the Commonwealth's agencies and instrumentalities have had losses from operations during the past years. The collectibility of these loans may be affected by budgetary constraints, the fiscal situation, and the credit rating of the Commonwealth of Puerto Rico, its agencies and instrumentalities, and their ability to generate sufficient funds from taxes, charges and/or bond issuances. Continuance of and/or significant negative changes in these factors may affect the ability of the Commonwealth and its agencies and instrumentalities to repay their outstanding loan balances with the Bank and accordingly, may have an adverse impact on the Bank's financial condition, liquidity, funding sources, and results of operations.

Management believes that no losses will be incurred by the Bank with respect to principal and interest on most of its loans to the public sector (including municipalities) and, as a result, no allowance for loan losses is generally established for them. For public sector loans, excluding municipalities, management bases its position in that in the past, the Director of the OMB has included in the budget of the Commonwealth appropriations to assist the Commonwealth and certain public sector corporations, agencies, and instrumentalities in repaying their loans with the Bank. The Legislature of the Commonwealth (the "Legislature") has generally approved these appropriations, and such practice is anticipated to continue in the future. Further, in accordance with Act No. 164 of December 17, 2001, the Bank is no longer allowed to originate loans to any governmental entity for which the source of repayment consists of appropriations from the Commonwealth's general fund without first obtaining the approval of the Legislature, except for (i) loans up to an aggregate amount of $100,000,000 as long as, among other things, the Bank obtains the written approval of the Governor and the Director of OMB, (ii) loans to any financially troubled governmental entity to enable it to honor its debt obligations, and (iii) loans to the Secretary of the Treasury under legislation authorizing the Secretary to borrow funds in anticipation of tax revenues.

In addition, on May 13, 2006, the Legislature enacted Act No. 91 that established the *Dedicated Sales Tax Fund*, known as FIA by the acronym of its Spanish name (the "FIA Fund"). Act No. 91 originally provided that the first one percent of the Commonwealth's share of the sales and consumption tax ("Pledged Sales Tax") will be used to repay certain obligations of the Commonwealth that were outstanding at June 30, 2006, payable to the Bank and the Public Finance Corporation, generally referred to as extra-constitutional debt, including approximately $2.8 billion of loans due by the Commonwealth and certain of its instrumentalities to the Bank at such date. The outstanding balance of such loans amounted to approximately $770.8 million at June 30, 2011.

Act No. 91 was amended by Act No. 291, enacted on December 26, 2006, and by Act No. 56, enacted on July 5, 2007, to create the Puerto Rico Sales Tax Financing Corporation (the "Sales Tax Corporation") as an independent governmental instrumentality that will own and hold the FIA Fund for the purpose of financing the payment, retirement or defeasance of the extra-constitutional debt.

On January 14, 2009, Act No. 91 was amended by Act No. 1 ("Act No. 1") to increase the Pledged Sales Tax to 2% of the Commonwealth's share of the sales and consumption tax. Furthermore, Act No. 1 amended Act No. 91 to allow the use of the proceeds of future bond issuances by the Sales Tax Corporation to, among other, pay principal and/or interest of loans granted by the Bank to the Commonwealth payable from future Commonwealth general obligation bonds and any debt of the Commonwealth outstanding as of December 31, 2008 that did not have a source of repayment or was payable from budgetary appropriations.

Finally, Act No. 7 of March 9, 2009 amended Act No. 91 to increase the Pledged Sales Tax by an additional 0.75% or to 2.75% effective July 1, 2009 which represents 50% of the Commonwealth's share of the sales and consumption tax.

During the fiscal year ended June 30, 2011, the Bank collected interest amounting to approximately $6.6 million on outstanding public sector loans from funds held by the Sales Tax Financing Corporation.

Also, loans granted to finance capital improvement programs of certain public entities are generally repaid from the proceeds of future bond issuances of these public entities or the Commonwealth. The public corporations and the Commonwealth have never defaulted on their respective bonds.

Although management of the Bank believes that no additional losses of principal and interest will be incurred by the Bank with respect to loans outstanding to the public sector at June 30, 2011, there can be no assurance that the director of the OMB will include amounts for loan repayments in the Commonwealth's budget, and that the Legislature will appropriate sufficient funds in the future to cover all amounts due to the Bank by the Commonwealth or public sector entities requiring the Commonwealth's support, or that the proceeds from any future bond issuances by the Sales Tax Corporation or certain public entities which have financed their capital improvement programs with the Bank, will be sufficient to cover the outstanding amount of extra-constitutional or capital improvement program debt at June 30, 2011. The participation of certain public entities in the bond market has been delayed waiting for the credit rating of such entities to improve or for more favorable market conditions. Because of the relationship among the Bank, the public sector entities, the director of the OMB, and the Legislature, the timing and amount of any financial assistance and bond proceeds to be used to repay certain public sector loans cannot be reasonably estimated by the Bank. The Bank, however, has in the past collected the outstanding principal and interest at the contractual rate on loans repaid from Commonwealth's appropriations or bond proceeds. Accordingly, no allowance has been established in the case of public sector loans for any shortfall between the present value of the expected future cash flows and the recorded investment in the loans.

Loans to municipalities amounting to approximately $956 million at June 30, 2011 are collateralized by a pledge of a portion of property tax assessments of each municipality. These loans include bonds and notes issued by Puerto Rico municipalities which are acquired by the Bank as bridge financing until such financings can be packaged and securitized. Subsequently, from time to time, the Bank sells, at par, a selection of these bonds and notes to the Puerto Rico Municipal Finance Agency (MFA), a component unit of the Commonwealth organized to create a capital market to assist municipalities in financing their public improvements programs. These loans, when sold, are pledged to secure the debt service payments for the bonds issued by MFA. In addition, Act. No. 80, enacted on July 29, 2007, provides that a portion of the municipal sales tax will be deposited in special accounts with the Bank for the purpose of granting loans to municipalities. The funds available in such accounts increase the borrowing capacity of the corresponding municipality. As of June 30, 2011, loans to municipalities repayable from these accounts amounted to approximately $559 million.

Allowance for Losses on Guarantees and Letters of Credit — Management of the Bank periodically evaluates the credit risk inherent in the guarantees and letters of credit on the same basis as loans are evaluated. The Bank charges as expense the amount required to cover estimated losses by establishing a specific allowance component for guarantees and letters of credit relating to loans in default, determined on the basis of the estimated future net cash outlays in connection with the related guarantees and letters of credit, and a general component for the risk inherent in the other guarantees and letters of credit outstanding, established as a percentage of the principal amount of the underlying loans, based on the Bank's loss experience on financial guarantees and letters of credit, and management's best judgment.

When a guarantee or letter of credit is honored, the Bank recognizes any disbursement as a nonperforming loan; therefore, no interest is accrued on the principal. After a specific analysis of the provision requirements, the related allowance included in the allowance for guarantees and letters of credit is reclassified to the allowance for loan losses. Any deficiency in the estimated allowance requirement is recorded as an additional provision to the allowance for loan losses.

The concentration of risk in the guarantees and letters of credit issued, predominantly those issued by the Tourism Development Fund (small number of large guarantees, geographical concentration in Puerto Rico, industry concentration in hotel and tourism), as well as other economic factors, compounds the uncertainty in management's estimate of the allowance for losses on guarantees and letters of credit. As a result, the aggregate losses on guarantees and letters of credit ultimately incurred by the Bank may differ from the allowance for losses as reflected in the accompanying basic financial statements, and such differences may be material.

Pursuant to the legislation under which the Tourism Development Fund was created, the executive director of the Tourism Development Fund is required to certify each year to the director of the OMB the amount, if any, that is necessary to reimburse the Tourism Development Fund for disbursements made in the previous year in connection with obligations guaranteed in excess of fees and charges collected on such guarantees ("net disbursements"). On December 16, 2009, Act No. 173 was enacted, which amended the legislation that created the Tourism Development Fund, to modify the definition of net disbursements to include disbursements made by the Tourism Development Fund for (i) loans to third parties, (ii) the acquisition of loan participations, and (iii) the acceleration of maturities of loans, notes, bonds or other type of debt guaranteed by the Tourism Development Fund. In addition, Act No. 173 provides that disbursements shall not be deemed made in the year in which the disbursement occurs but shall be deemed made in the year in which the executive director of the Tourism Development Fund determines that a loss was incurred with respect to a loan, note, bond or debt (such determination being referred to as a "realized loss"). The director of the OMB has to include the amount subject to reimbursement in the general fund budget of the Commonwealth for the following fiscal year for the Legislature's consideration and approval. The Legislature is not obligated to authorize such appropriations. As of June 30, 2011, there were no outstanding claims for reimbursements.

Debt Issue Costs — Debt issue costs are deferred and amortized, as a component of interest expense, over the term of the related debt using the effective interest method, or a systematic and rational method that approximates the interest method. Issuance costs of bonds accounted for in the governmental funds are recorded as expenditures when paid.

Real Estate Available for Sale — Real estate available for sale comprises properties acquired in lieu of payment and through foreclosure proceedings. It also includes loans that are treated as if the underlying collateral had been foreclosed because the Bank has taken possession of the collateral, even though legal foreclosure or repossession proceedings have not taken place. Those properties are carried at the lower of cost or fair value, which is established by a third party professional assessment or based upon an appraisal, minus estimated costs to sell. At the time of acquisition of properties in full or in partial satisfaction of loans, any excess of the loan balance over the fair value of the properties minus estimated costs to sell is charged against the allowance for loan losses. Subsequent declines in the value of real estate available for sale are charged to expenditure/expense. Gain or loss on sale related to real estate available for sale is included within revenues in the accompanying statement of revenues, expenditures and changes in fund balances and within noninterest income in the accompanying statement of revenues, expenses, and changes in net assets.

Allowance for Losses on Mortgage Loan Insurance — The allowance for losses on mortgage loan insurance is based on management's evaluation of potential losses on insurance claims after considering economic conditions, fair value of related property and other pertinent factors. Such amount is, in the opinion of management, adequate to cover estimated future normal mortgage loan insurance losses. Actual losses for mortgage loan insurance are charged and recoveries, if any, are credited to the allowance for losses on mortgage loan insurance. Because of uncertainties inherent in the estimation process, management's estimate of losses in the outstanding mortgage loans insurance portfolio and the related allowance may change in the near future.

Capital Assets — Capital assets, which include premises and equipment, are stated at cost less accumulated depreciation and amortization, and are reported in the business-type activities column in the government-wide financial statements. Capital assets are defined by the Bank as assets that have a cost of $500 or more at the date of acquisition and have an expected useful life of three or more years. Depreciation is charged to operations and included within other noninterest expense, and is computed on the straight-line basis over the estimated useful lives of the depreciable assets. Leasehold improvements are amortized over the terms of the respective leases or the estimated useful lives of the improvements, whichever is shorter. Costs of maintenance and repairs which do not improve or extend the lives of the respective assets are charged to expense as incurred.

Estimated useful lives are as follows:

Building	40 years
Leasehold improvements	Lesser of 10 years or lease term
Information systems	3–5 years
Office furniture and equipment	5 years
Vehicles	5 years

Securities Sold Under Agreements to Repurchase — The Bank enters into sales of securities under agreements to repurchase. These agreements generally represent short-term financings and are reflected as a liability. The securities underlying these agreements are usually held by the broker or his/her agent with whom the agreement is transacted.

Compensated Absences — The employees of the Bank are granted 30 days of vacation and 18 days of sick leave annually. Vacation and sick leave may be accumulated up to a maximum of 72 and 90 days, respectively. In the event of employee resignation, an employee is reimbursed for accumulated vacation and sick leave days up to the maximum allowed. The enterprise fund financial statements and the government-wide financial statements present the cost of accumulated vacation and sick leave as a liability. There are no employees paid by governmental funds.

Deferred Revenues — Deferred revenues at the governmental fund level arise when potential revenues do not meet the available criterion for recognition in the current period. Available is defined as due at June 30 and expected to be collected within 120 days thereafter to pay obligations due at June 30. Deferred revenues at the government-wide level arise only when the Bank receives resources before it has a legal claim to them.

Refundings — Refundings involve the issuance of new debt whose proceeds are used to repay immediately (current refunding) or at a future time (advance refunding) previously issued debt. The difference between the reacquisition price and the net carrying amount of the old debt is deferred and amortized as a component of interest expense over the remaining life of the old debt or the life of the new debt, whichever is shorter. The deferred amount is recorded as an addition to or deduction from the new debt.

No-Commitment Debt — The Housing Finance Authority has issued notes and bonds in connection with the financing of low and moderate-income housing projects. Certain of the obligations issued by the Housing Finance Authority are considered no-commitment debt and are excluded, along with the related assets held in trust, from the accompanying basic financial statements. The Bank, the Housing Finance Authority and the Commonwealth, except for the assets held in trust and earnings thereon, are not liable directly or indirectly for the payment of such obligations.

Certain other collateralized obligations of the Housing Finance Authority are included in the accompanying basic financial statements either because they represent general obligations of the Housing Finance Authority or it maintains effective control over the assets transferred as collateral.

From time to time, the Public Finance Corporation issues bonds, the proceeds of which are used to purchase from the GDB Operating Fund promissory notes of the Commonwealth, and of certain of its instrumentalities and public corporations. The bonds are limited obligations of the Public Finance Corporation and, except to the extent payable from bond proceeds and investments thereon, are payable solely from the pledge and assignment of amounts due on the notes. Principal and interest on the notes are payable solely from legislative appropriations to be made pursuant to acts approved by the Legislature. The underlying notes represent debt of the issuing instrumentalities. The bonds are considered no-commitment debt, and therefore neither the bonds nor the notes purchased with the proceeds therefrom are presented in the accompanying basic financial statements.

Loan Origination Costs and Commitment Fees — GASB No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues*, requires that loan origination and commitment fees and direct origination costs be amortized over the contractual life of the related loan. The Bank generally recognizes commitment fees as income when collected and the related loan origination costs as expense when incurred. In the opinion of management, the difference between the two methods does not have a significant effect on the Bank's financial position and changes in financial position.

Transfers of Receivables — Transfers of receivables are accounted and reported as a sale if the Bank's continuing involvement with those receivable is effectively terminated. This approach distinguishes transfers of receivables that are sales from transfers that are collateralized borrowings.

The Bank's continuing involvement is considered to be effectively terminated if all of the following criteria are met: (i) the transferee's ability to subsequently sell or pledge the receivables is not significantly limited by constraints imposed by the Bank, either in the transfer agreement or through other means, (ii) the Bank does not have the option or ability to unilaterally substitute for or reacquire specific accounts from among the receivables transferred, except in certain limited circumstances, (iii) the sale agreement is not cancelable by either party, including cancellation through payment of a lump sum or transfer of other assets or rights, and (iv) the receivables and the cash resulting from their collection have been isolated from the Bank.

The Bank services loans for investors and receives servicing fees generally based on stipulated percentages of the outstanding principal balance of such loans. Loan servicing fees, late charges, and other miscellaneous fees are recognized as revenues as the related mortgage payments are collected, net of fees due to any third-party servicers. No servicing asset is recognized since fees are considered adequate compensation.

Future Adoption of Accounting Pronouncements — The GASB has issued the following Statements:

- GASB Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employers Plans*, which if effective for periods beginning after June 15, 2011.

- GASB Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, which is effective for periods beginning after December 15, 2011.

- GASB Statements No. 61, *The Financial Reporting Entity: Omnibus – an amendment of GASB Statements No. 14 and No. 34*, which is effective for periods beginning after June 15, 2012.

- GASB Statements No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements,* which is effective for periods beginning after December 15, 2011.

- GASB Statements No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position,* which is effective for periods beginning after December 15, 2011.

- GASB Statements No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions — An Amendment of GASB Statement No. 53,* which is effective for periods beginning after June 15, 2011.

Management is evaluating the impact that these statements will have on the Bank's basic financial statements.

3. CASH AND DUE FROM BANKS, FEDERAL FUNDS SOLD, AND DEPOSITS PLACED WITH BANKS

The table presented below discloses the level of custodial credit risk assumed by the Bank at June 30, 2011. Custodial credit risk is the risk that, in the event of a financial institution failure, the Bank's deposits may not be returned to it. The Commonwealth requires that public funds deposited in commercial banks in Puerto Rico must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury of the Commonwealth. The Bank does not have a formal policy for custodial credit risk for cash accounts opened with commercial banks outside Puerto Rico. These accounts are opened only with well-capitalized financial institutions.

The Bank' policies for deposits placed with banks and federal funds sold establish maximum exposure limits for each institution based on the institution's capital, financial condition and credit rating assigned by nationally recognized rating agencies. Deposits placed with banks of approximately $740.5 million mature within one year. Federal funds sold mature overnight and no collateral is required. As of June 30, 2011, $1,171,971,387 of the depository bank balance of $1,177,222,759 was uninsured and uncollateralized as follows:

	Carrying Amount	Depository Bank Balance	Amount Uninsured and Uncollateralized
Cash and due from banks	$ 347,407,500	$ 347,909,368	$ 342,657,996
Deposits placed with banks	740,463,391	740,463,391	740,463,391
Federal funds sold	88,850,000	88,850,000	88,850,000
Total	$ 1,176,720,891	$ 1,177,222,759	$ 1,171,971,387

Reconciliation to the government-wide statement of net assets (deficiency):

Unrestricted:	
Cash and due from banks	$ 341,790,505
Federal funds sold	88,850,000
Deposits placed with banks	219,315,862
Total unrestricted	649,956,367
Restricted:	
Cash and due from banks	5,616,995
Deposits placed with banks	521,147,529
Total restricted	526,764,524
Total	$ 1,176,720,891

4. INVESTMENTS

The Bank's investment policies allow management to purchase or enter into the following investment instruments:

- U.S. government and agencies obligations
- Certificates of deposit and time deposits
- Bankers' acceptances
- Obligations of the Commonwealth of Puerto Rico, its agencies, municipalities, public corporations, and instrumentalities
- Federal funds sold
- Securities purchased under agreements to resell
- World Bank securities
- Mortgage-backed and asset-backed securities
- Corporate debt, including investment contracts
- External investment pools
- Stock of corporations created under the laws of the United States of America or the Commonwealth of Puerto Rico
- Options, futures, and interest-rate swap agreements for hedging and risk control purposes, as well as for the creation of synthetic products which qualify under any of the foregoing investment categories

- Open-end mutual funds with acceptable underlying assets and rated AAA by Standard & Poor's or its equivalent by Moody's

The Bank's investment policies establish limitations and other guidelines on maturities and amounts to be invested in the aforementioned investment categories and by issuer/counterparty and on exposure by country. In addition, such policies provide guidelines on the institutions with which investment transactions can be entered into. In addition, the investment committee and the board of directors of the Bank will determine, from time to time, other transactions that the Bank may enter into.

The Bank's investment policies provide that investment transactions shall be entered into only with counterparties that are rated BBB+/A-1 or better by Standard & Poor's or equivalent rating by Moody's Investors Service or Fitch Ratings, depending on the type and maturity of the investment and the counterparty to the transaction. Any exceptions must be approved by the Bank's board of directors. The investment policies also provide that purchases and sales of investment securities shall be made using the delivery vs. payment procedures.

The Bank's investment policies also provide that the Asset Liability Management Committee (ALCO) is responsible for implementing and monitoring the Bank's interest rate risk policies and strategies. The ALCO meets on a monthly basis to coordinate and monitor the interest rate risk management of interest sensitive assets and interest sensitive liabilities, including matching of their anticipated level and maturities, consistent with the Bank's liquidity, capital adequacy, risk and profitability goals set by the Bank's board of directors.

The following table summarizes the type and maturities of investments held by the Bank at June 30, 2011. Investments by type in any one issuer representing 5% or more of total investments of either the Bank or its blended component units have been separately disclosed. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Investment Type	Within One Year	After One to Five Years	After Five to Ten Years	After Ten Years	Total
U.S. Treasury bills	$ 843,858,209	$ -	$ -	$ -	$ 843,858,209
U.S. Treasury notes	200,749,558	553,547,664	438,162,500	50,023,438	1,242,483,160
U.S. sponsored agencies notes:					
Federal National Mortgage Association ("FNMA")		25,051,650		1,550,783	26,602,433
Federal Home Loan Bank ("FHLB")	150,005,500	572,646,875			722,652,375
Federal Home Loan Mortgage Corporation ("FHLMC")		76,585,920			76,585,920
Federal Farm Credit Bank ("FFCB")		79,507,335			79,507,335
Mortgage and asset-backed securities:					
Government National Mortgage Association ("GNMA")	79,387	2,797,706	3,258,505	467,070,128	473,205,726
Federal National Mortgage Association ("FNMA")			110,318,422	467,882,745	578,201,167
FHLMC			88,497,892	356,687,331	445,185,223
Other			287,059		287,059
Corporate debt:					
Goldman Sachs	4,000,160				4,000,160
General Electric	708,680	4,110,146			4,818,826
Andrew Mellow Foundation		3,159,600			3,159,600
Walmart Stores		2,116,340			2,116,340
First Puerto Rico Family of Funds	50,000,000				50,000,000
External investment pools—					
Fixed-income securities	123,186,460				123,186,460
PR Housing Bank Portfolio II bonds				4,744,394	4,744,394
Nonparticipating investment contracts:					
American International Group				198,151,692	198,151,692
Other				98,484,022	98,484,022
U.S. Municipal notes	1,418,382	74,073,529	58,599,962	71,186,679	205,278,552
Commonwealth agency bonds	-	3,530,000	-	46,326,069	49,856,069
Total investments	$ 1,374,006,336	$ 1,397,126,765	$ 699,124,340	$ 1,762,107,281	5,232,364,722
External investment pools:					
Equity securities:					
Russell 1000 Growth Common Trust Fund					47,581,657
Global Opportunities Capital Appreciation Fund					14,757,197
Preferred securities / interests:					
Grupo Hima San Pablo					3,642,563
Desarrolladora del Norte					50,000,000
Other					247,436
Total					$ 5,348,593,575
Reconciliation to the government-wide statement of net assets					$ 3,775,241,121
Unrestricted investments and investment contracts					1,573,352,454
Restricted investments and investment contracts					$ 5,348,593,575

Investments in fixed-income external investment pools had an average maturity of less than 60 days; accordingly, they were presented as investments with maturity of less than one year. These investments include $117,362,255 invested in the Puerto Rico Government Investment Trust Fund, a government-sponsored pool, which is administered by the Bank. This pool is subject to regulatory oversight by the Commissioner of Financial Institutions of Puerto Rico. The fair value of the pool is the same as the value of the pool shares.

At June 30, 2011, the total amount of $9,386,086 of the Bank's investment in corporate debt maturing over one year, bear a fixed interest rate. Also, at June 30, 2011, approximately 32% of the Bank's investments in mortgage and asset-backed securities were held by trustees in connection with bonds issued by the Housing Finance Authority, the terms of which generally provide for early redemption of the bonds if the securities are early repaid.

All of the Bank's investments in U.S. Treasury securities and mortgage-backed securities guaranteed by GNMA carry the explicit guarantee of the U.S. government. The credit quality ratings for investments in debt securities, excluding U.S. Treasury securities and mortgage-backed securities guaranteed by GNMA, at June 30, 2011 are as follows:

	Credit Risk				
	Rating				
Securities Type	AAA to A-	BBB	B	Not Rated	Total
U.S. sponsored agencies notes:					
FNMA	$ 26,602,433	$ -	$ -	$ -	$ 26,602,433
FHLB	722,652,375				722,652,375
FHLMC	76,585,920				76,585,920
FFCB	79,507,335				79,507,335
Mortgage-backed and asset-backed securities:					
FNMA	578,201,167				578,201,167
FHLMC	445,185,223				445,185,223
Other	16,861			270,198	287,059
Corporate debt	64,094,926				64,094,926
External investment pools —					
Fixed-income securities	123,186,460				123,186,460
PR Housing Bank Portfolio II bonds	4,744,394				4,744,394
Nonparticipating investment contracts	254,832,428	41,803,286			296,635,714
U.S. municipal notes	205,278,552				205,278,552
Commonwealth agency bonds				49,856,069	49,856,069
Total	$2,580,888,074	$41,803,286	$ -	$50,126,267	$2,672,817,627

The credit quality ratings of nonparticipating investment contracts are based on the credit quality ratings at June 30, 2011 of the counterparties with whom these contracts are entered into. The credit quality ratings of the counterparties should follow the ratings required by the investment policies of the Bank.

As of June 30, 2011, the Bank had pledged investments and investment contracts to secure the following:

Payment of principal and interest on obligations issued by a blended component unit	$ 675,952,789
Securities sold under agreements to repurchase	970,818,550
Certificates of indebtedness	4,300,000

5. LOANS RECEIVABLE AND ALLOWANCE FOR LOAN LOSSES

Loans at June 30, 2011 consist of the outstanding balance of credit facilities granted to the following (in thousands):

	GDB Operating Fund (1)	Tourism Development Fund	Housing Finance Authority	Development Fund	Total
Public corporations and agencies	$6,002,823	$ -	$ -	$ -	$6,002,823
Municipalities	1,792,058				1,792,058
Allowance for loan losses	(4,000)				(4,000)
Total loans to public sector	7,790,881	-	-	-	7,790,881
Private sector	5,000	432,298	302,371	17,375	757,044
Allowance for loan losses	(264)	(86,815)	(35,655)	(9,320)	(132,054)
Deferred origination fees			(19,912)		(19,912)
Total loans to private sector	4,736	345,483	246,804	8,055	605,078
Balance — end of year	$7,795,617	$345,483	$246,804	$8,055	$8,395,959

(1) Excluding loans to component units.

Reconciliation to the government-wide statement of net assets:	
Unrestricted loans receivable — net	$8,360,977
Restricted loans receivable — net	34,982
Total	$8,395,959

For the year ended June 30, 2011, public sector loan originations and collections amounted to $4.6 billion and $3.2 billion, respectively.

Public sector loans amounting to approximately $2.3 billion as of June 30, 2011 were delinquent by 90 days or more or had matured. Public sector loans classified as nonaccrual amounted to approximately $57 million at June 30, 2011. Interest income that would have been recorded if such nonaccrual loans had been accruing in accordance with their original terms was approximately $1.9 million in 2011. Interest collected on these loans during the year ended June 30, 2011 was not material.

At June 30, 2011, loans to public corporations and agencies of the Commonwealth amounting to $6,002,823 were repayable from the following sources (in thousands):

Repayment Source	Amount
Proceeds from future bond issuances of public corporations	$ 1,646,025
Operating revenues of public entities other than the Commonwealth	1,554,059
Legislative appropriations — previously from issuance of Commonwealth's general obligation bonds	1,116,859
Legislative appropriations — previously from FIA Fund	770,799
Legislative appropriations — other	848,239
Other — including funds from federal grants	66,842
Total	$ 6,002,823

During fiscal year 2011, the Bank received $63.1 million and $101.4 million of appropriations to repay principal of and interest on public sector loans whose repayment source was originally from the FIA Fund and from future issuances of Commonwealth's general obligations bonds, respectively. The Commonwealth's general fund budget for fiscal year 2012 includes $65.1 million and $91.5 million of appropriations to repay principal of and interest on public sector loans whose repayment source was originally from the FIA Fund and from future issuances of Commonwealth's general obligations bonds, respectively. These appropriations are based on payment schedules proposed by the Bank, which are based on a period of amortization of 30 years each, at contractual interest rates. The Bank will annually submit to the OMB, to be included in the Commonwealth's budget for legislative approval in each subsequent fiscal year, an amount established in the payment schedules with the terms stated above. The Bank expects that future appropriations will be approved by the Legislature of the Commonwealth to comply with such schedules. However, there can be no assurance that the director of OMB will include an amount for loan repayments in the Commonwealth's budget, and that the Legislature will appropriate sufficient funds in the future to cover all amounts due to the Bank on these loans.

Since one of the Bank's principal functions is to provide financing to the Commonwealth and its instrumentalities, the Bank's loan portfolio includes loans to various departments and agencies of the Commonwealth, to various public corporations, and to municipalities, which represent a significant portion of the Bank's assets. Loans to the Commonwealth and its departments and agencies typically include working capital lines of credit payable from short-term tax and revenue anticipation notes issued by the Commonwealth, interim financing of capital improvements payable from Commonwealth general obligation bonds or revenue bonds issued by the corresponding agency and, in recent years, loans to finance the Commonwealth's budget deficit payable from the FIA Fund, uncollected taxes and annual appropriations made by the Legislature of Puerto Rico. Loans to the public sector, excluding municipalities, amounted to approximately $6.0 billion or 38.7% of the Bank's government-wide total assets at June 30, 2011.

At June 30, 2011, approximately $2.7 billion of the public sector loans are payable from legislative appropriations from, or future tax revenues of, the Commonwealth. Accordingly, the payment of these loans may be affected by budgetary constraints, the fiscal situation and the credit rating of the Commonwealth. Significant negative changes in these factors may have an adverse impact on the Bank's financial condition. From fiscal years 2003 to fiscal year 2010, the Commonwealth's recurring expenditures have exceeded its recurring revenues. These shortfalls were partially covered with loans from the Bank and other nonrecurring revenues. In addition, the Commonwealth has preliminary estimated that its expenditures will exceed its revenues for fiscal year 2011. From fiscal year 2003 to 2008, the Bank granted loans to the Commonwealth aggregating to $1,964 million to cover part of the

Commonwealth's deficit. As of June 30, 2011, the outstanding principal amount of these loans was $227 million.

In addition, at June 30, 2011, approximately $3.3 billion of public sector loans are payable from proceeds from future bond issuances and operating income of public corporations of the Commonwealth. The Bank lends funds to such public corporations for capital improvements and operating needs. The loans for capital improvements generally are construction loans and are repaid from the proceeds of future bond issuances of the respective public corporations. Such loans may, however, also be repaid from the revenues of such public corporations, from loans provided by sources other than the Bank, from federal grants, and from the sale of assets of such public corporations. The amount of outstanding loans from the Bank to the public corporations fluctuates annually, depending upon the capital program needs of the public corporations, the timing and level of their capital expenditures, and their ability to gain access to the long-term capital markets. The participation of certain of these public entities in the bond market has been delayed waiting for the credit rating of such entities to improve or for more favorable market conditions. At June 30, 2011, the Bank has approximately $1.3 billion and $1 billion of loans outstanding due from the Puerto Rico Highways and Transportation Authority and the Puerto Rico Aqueduct and Sewer Authority, representing approximately 71% of the $3.3 billion mentioned above. As explained below, to manage the credit risk of these and other debtors, the Bank has entered into fiscal oversight agreements, whereby the Bank, among other things, imposes conditions on the extensions of credit to these entities and continually monitors their finances. The default by any such and other public sector borrowers on the Bank's loans may have a material adverse effect on the financial condition and operating results of the Bank.

Starting in fiscal year 2010, as part of its risk management activities and as a condition to provide financing support to certain public corporations, GDB has entered into fiscal oversight agreements with such public corporations. The agreements require the public corporations, among other, to implement a comprehensive expense reduction program, including certain fiscal oversight controls, subject to laws and existing agreements of the public corporations, designed to minimize future tariff increases to households and the private sector, and to protect and improve the credit rating of the public corporations, so that the public corporations may obtain adequate financing to fund its capital expenditure requirements and to operate its infrastructure in an efficient and reliable manner and in compliance with applicable laws and regulations. GDB's agreement to provide current financing and any future financing is expressly conditioned upon the public corporations' compliance with the covenants established in the fiscal oversight agreement and GDB's right to monitor and enforce such compliance. These agreements will be in effect until the public corporations have regained a level of financial stability and are able to secure long-term financing that will result in the continued stability of the public corporations' operations and financial condition. As of June 30, 2011, management of the Bank determined that all public corporations and agencies have complied with the material terms and conditions of their respective agreements.

Also, as part of its role of providing financing to the Commonwealth and its instrumentalities to further the economic development of Puerto Rico, and as part of its risk management activities, the Bank is renegotiating and/or restructuring payment terms of the loans to certain governmental entities. Some of the renegotiations/restructurings extend the period for principal repayment but provide for repayment of the contractual interest in accordance with the original terms.

In addition, due mainly to the Commonwealth's financial situation and the unfunded status of the Puerto Rico Government Employee Retirement System, which represents a challenge that could affect Puerto Rico's credit rating, major credit rating agencies, such as Moody's Investors Service ("Moody's") Standards & Poor's Rating Services (S&P), and Fitch, Inc. ("Fitch") have downgraded the Commonwealth's credit ratings during the past years.

However, on March 7, 2011, S&P raised its rating on the Commonwealth unenhanced general obligation bonds to BBB with a stable outlook from BBB- with a positive outlook and assigned such rating to the bonds issued by the Commonwealth. In taking this rating action, S&P stated that the upgrade reflects the Commonwealth's recent revenue performance and continued efforts to achieve fiscal and budgetary balance. S&P noted, however, that other medium-term budget pressures, such as the Commonwealth's retirement benefit obligations, remain a limiting credit factor. S&P's stable outlook is based on the Commonwealth's recent implementation of significant expenditure controls and revenue enhancement measures that could help restore balance within the next two years. S&P also stated that it would raise the rating if, over the upcoming two years, in conjunction with an improvement in the Commonwealth's economic performance, budget controls remain in place and there is continued progress toward achieving balance between ongoing revenues and expenditures as well as in addressing the Commonwealth's unfunded retirement benefit obligations. At June 30, 2011, the credit rating assigned by Moody's, S&P, and Fitch to the general obligation bonds of the Commonwealth was A3 with a negative outlook and on watchlist, BBB with a stable outlook, and BBB+ with a stable outlook, respectively.

Subsequent to year end, on August 8, 2011, Moody's lowered its rating on the Commonwealth's unenhanced general obligation bonds to Baa1 with a negative outlook from A3. This rating action was a result of Moody's review of the Commonwealth's rating, which had been placed on watchlist on May 3, 2011. In taking this rating action, Moody's stated the downgrade reflects the continued financial deterioration of the severely underfunded retirement systems, continued weak economic trend, and weak finances, with a historical trend of funding budget gaps with borrowings. Moody's negative outlook reflects the stress the Commonwealth will face in the next few years as it continues to address the underfunding of the retirement systems from an already weak financial and economic position. The downgrade and negative outlook also affects bonds whose ratings are determined by or linked to that of the Commonwealth, including the Bank's outstanding notes previously issued under an indenture, which were downgraded to Baa1.

Also, on August 8, 2011, S&P reaffirmed its BBB rating of the Commonwealth's unenhanced general obligation bonds.

In an effort to address the Commonwealth's structural budget imbalance, the Legislature enacted Act No. 117 of July 4, 2006 ("Act No. 117"), which amended the Puerto Rico Internal Revenue Code of 1994 to provide, among other things, for a general sales and consumption tax of 5.5% (the "Sales Tax") to be imposed by the Commonwealth. Act No. 117 also eliminated the 5% general excise tax imposed on imported goods and the 3.6% general excise tax on goods manufactured in Puerto Rico, and provided certain income tax reductions to taxpayers. The Sales Tax was effective on November 15, 2006.

Act No. 91 was amended by Act No. 291, enacted on December 26, 2006, and by Act No. 56, enacted on July 6, 2007, to create the Puerto Rico Sales Tax Financing Corporation (the "Sales Tax Corporation") as an independent governmental instrumentality that will own and hold the FIA Fund for the purpose of financing the payment, retirement or defeasance of the extra-constitutional debt. Pursuant to Act No. 91, ownership of the FIA Fund, was transferred to the Sales Tax Corporation.

On January 14, 2009, Act No. 91 was amended by Act No. 1 ("Act No. 1") to increase the Pledged Sales Tax to 2% of the Commonwealth's share of the sales and consumption tax. Furthermore, Act No. 1 amended Act No. 91 to allow the use of the proceeds of future bond issuances by the Sales Tax Corporation to, among other, pay principal and/or interest of loans granted by the Bank to the Commonwealth payable from future Commonwealth general obligation bonds and any debt of the Commonwealth outstanding as of December 31, 2008 that did not have source of repayment or was payable from budgetary appropriations.

Finally, Act No. 7 of March 9, 2009 amended Act No. 91 to increase the Pledged Sales Tax, effective July 1, 2009, by an additional 0.75% or to 2.75%, which represents 50% of the Commonwealth's share of the sales and consumption tax. In addition, Act. No. 7 created an integrated plan for the Commonwealth's fiscal stabilization that includes: (i) operating expense-reduction measures, including various workforce reduction initiatives and a temporary halt of salary increases and other economic benefits included in certain laws and collective bargaining agreements; (ii) tax revenue enforcement measures; (iii) a combination of permanent and temporary tax increases, and (iv) other financial measures, including the increase of the Pledged Sales Tax. During the fiscal year ended June 30, 2011, the Bank collected interest amounting to approximately $6.6 million on outstanding public sector loans from funds held by the Sales Tax Financing Corporation.

Although the Commonwealth is using its best efforts to maximize revenues and reduce expenditures, there can be no assurance that its future revenues will be greater than its expenditures.

Based on previous experience and recent developments, management of the Bank believes that the carrying amount of the loans to the public sector will be collected (including interest at the contractual interest rate), and, accordingly, no additional allowance for loan losses to the public sector is needed at June 30, 2011.

Loans to the private sector include the outstanding principal balance of credit facilities granted by the Bank and the Development Fund to private enterprises in Puerto Rico, the activities of which are deemed to further the economic development of Puerto Rico. They also include the outstanding principal balance of mortgage loans granted to low and moderate-income families for the acquisition of single-family housing units and to developers of low and moderate-income multifamily housing units in Puerto Rico, and direct loans to tourism projects. These credit facilities, net of allowance for loan losses, amounted to approximately $600.3 million at June 30, 2011 of which approximately $246.8 million are mortgage loans for low and moderate-income housing units and approximately $345.5 million are for tourism projects.

Private sector loans classified as nonaccrual amounted to approximately $211 million at June 30, 2011. Interest income that would have been recorded if these loans had been performing in accordance with their original terms was approximately $11 million in 2011. No interest was collected on these loans for the year ended June 30, 2011.

The following is a summary of private sector loans of the enterprise funds considered to be impaired as of June 30, 2011, and the related interest income for the year then ended (in thousands):

	Enterprise Funds				
	GDB Operating Fund	Housing Finance Authority	Tourism Development Fund	Development Fund	Total
Recorded investment in impaired loans:					
Not requiring an allowance for loan losses	$ 129	$ 3,334	$ -	$ -	$ 3,463
Requiring an allowance for loan losses	264	48,253	141,062	16,930	206,509
Total recorded investment in impaired loans	$ 393	$ 51,587	$ 141,062	$ 16,930	$ 209,972
Related allowance for loan losses	$ 264	$ 33,643	$ 76,502	$ 9,387	$ 119,796
Average recorded investment in impaired loans	-	58,781	134,331	8,465	201,577
Interest income recognized on impaired loans	-	562	-	-	562

The following is a summary of the activity in the allowance for loan losses for the year ended June 30, 2011 (in thousands):

	Enterprise Funds				
	GDB Operating Fund	Housing Finance Authority	Tourism Development Fund	Development Fund	Total
Balance — beginning of year	$ 9,814	$ 28,970	$ 55,763	$ -	$ 94,547
Provision (credit) for loan losses	(5,550)	7,547	31,052	9,320	42,369
Transfer to enterprise funds					-
Net charge-offs		(862)			(862)
Balance — end of year	$ 4,264	$ 35,655	$ 86,815	$ 9,320	$ 136,054

6. DUE FROM FEDERAL GOVERNMENT

Under the New Secure Housing Program (the "Program"), the Housing Finance Authority is responsible for administering the Program, including contracting, supervising and paying the designers, inspectors, and legal services needed for the Program. The Housing Finance Authority also provides all the funding for the Program through a $67 million nonrevolving line of credit with the Bank. The Department of Housing is responsible for land acquisitions, auctioning projects, awarding construction contracts, qualifying participants, and selling housing units to eligible participants.

Under the terms of the grant, the construction of, and relocation of participants into new secure housing facilities was to be completed by December 31, 2007. In addition, FEMA would reimburse 75% of the allowable costs of the Program. Funds collected under the Program since its inception amounted to approximately $113 million and are subject to compliance audits under OMB Circular A-133 and federal granting agencies audits.

In April 2007, FEMA discontinued reimbursing the Housing Finance Authority's allowable costs based on the Program's noncompliance with the scheduled dates for construction activities and case management. The Department of Housing requested a one-year extension, up to December 31, 2008, and although original request was denied, FEMA granted such request in 2007.

On June 6, 2008, the Department of Housing requested an additional one-year extension, up to December 31, 2009, for the completion of the construction and relocation of participants into new secure housing facilities. On July 1, 2008, FEMA denied the additional one-year extension. The Department of Housing requested through the Governor's Authorized Representative (GAR) on September 19, 2008, a reconsideration of FEMA's decision not to grant the extension. On December 23, 2008 FEMA granted an extension up to June 30, 2010.

Although significant progress was made through June 30, 2010 in the construction activities and in the case management of the Program, the Housing Finance Authority was not able to fully comply with the terms of the extension granted by FEMA. On September 30, 2011, the Housing Finance Authority provided FEMA and the GAR the program closeout documentation, which is under FEMA's review. Based on this and the fact that no reimbursements have been received from FEMA since April 2007, management has decided to establish an allowance for the $26 million due from the FEMA at June 30, 2011.

The Housing Finance Authority, as a public housing agency, is authorized to administer the U.S. Housing Act Section 8 Programs in Puerto Rico. The revenues and expenses of such federal financial assistance are accounted for as a major governmental fund under the HUD Programs fund. Revenues and expenditures related to the administration of the U.S. Housing Act Section 8 Programs amounted to approximately $127.1 million during the year ended June 30, 2011. This amount includes approximately $4,980,000 of administrative fees for services performed as contract administrator, which are reimbursed by HUD. As of June 30, 2011, the amounts due from federal government under the HUD Programs fund amounted to approximately $1.3 million.

In addition, on February 17, 2009, the American Recovery and Reinvestment Act of 2009 (ARRA) was signed into law in the United States of America. The purpose of ARRA is to jumpstart the nation's ailing economy with the primary focus on creating and saving jobs in the near term and investing in infrastructure that will provide long-term economic benefits. The Housing Finance Authority expended $95.7 million of ARRA program funds during the year ended June 30, 2011, of which $11.2 million are due from the federal government at June 30, 2011.

During 2010, the Housing Finance Authority received from the Department of Housing approximately $1.6 million of cash and approximately $17 thousand in capital assets, as well as liabilities amounting to approximately $1.6 million, that were held by the Department of Housing as the previous administrator of the HOME Program. This transaction did not have an effect on the Housing Finance Authority's 2011 statement of activities and statement of revenues, expenditures, and changes in fund balances – governmental funds.

During the year ended June 30, 2011, the Housing Finance Authority expended $16.6 million of HOME Program funds, of which $8.7 million are due from the federal government as of June 30, 2011. In accordance with the Housing Finance Authority's accounting policies, the Housing Finance Authority has deferred the recognition of revenue of approximately $4.6 million due from the federal government as such amounts are not considered to be available. This amount has been recorded as a deferred revenue in the accompanying balance sheet – governmental funds.

7. REAL ESTATE AVAILABLE FOR SALE

Real estate available for sale at June 30, 2011 consisted of the following:

	GDB Operating Fund	Housing Finance Authority	Total
Residential (1–4 units)	$ -	$ 13,653,479	$ 13,653,479
Commercial	138,800,232		138,800,232
Valuation allowance	(13,121,013)	(10,764,378)	(23,885,391)
Total real estate available for sale	$125,679,219	$ 2,889,101	$128,568,320

Reconciliation to the government-wide statement of net assets (deficiency):

Unrestricted real estate available for sale	$126,641,380
Restricted real estate available for sale	1,926,940
Total	$128,568,320

The following is a summary of the activity in the valuation allowance for the year ended June 30, 2011:

	GDB Operating Fund	Housing Finance Authority	Total
Balance — beginning of year	$ 13,121,013	$ 7,443,470	$ 20,564,483
Provision for possible losses	-	4,089,470	4,089,470
Write-offs	-	(768,562)	(768,562)
Balance — end of year	$ 13,121,013	$ 10,764,378	$ 23,885,391

During fiscal year 2009, the Bank entered into an agreement with an agency of the Commonwealth whereby the Bank received several properties with appraised values (based on appraisals made near the transaction date) of $155.9 million in lieu of payment of a loan whose principal balance and accrued interest receivable amounted to $144.2 million at December 30, 2008. Management of the Bank has subsequently obtained appraisals of the properties, which have resulted in a decrease in the appraised values of certain of such properties, net of estimated selling costs, of approximately $62 million, which have been recorded as a reduction of the carrying value of the properties (included within real estate available for sale in the accompanying statement of net assets) and a receivable from the Commonwealth's agency [included within other receivables in the accompanying statement of net assets (deficiency)]. The interagency agreement provides that the agency of the Commonwealth shall transfer to the Bank additional properties to cover any deficiency in the properties values during a period of five years. In addition, on October 16, 2011, the Bank obtained a commitment from the director of the OMB, whereby OMB commits to pay $7.5 million to the Bank before December 31, 2011 to cover a portion of the outstanding balance at June 30, 2011. In addition, the director of the OMB has committed to include in the Commonwealth's general fund budget, for legislative approval, appropriations of approximately $3.8 million, plus interest at 7%, for the next 15 years to cover the remaining balance. The Legislature is not obligated to authorize such appropriations. Management of the Bank is of the opinion that it will receive properties or cash to cover such deficiency and, accordingly, believes that no valuation allowance on the receivable from the Commonwealth's agency is needed at June 30, 2011.

8. CAPITAL ASSETS

Capital assets activity for the year ended June 30, 2011, was as follows:

Governmental Activities:

	Beginning Balance	Additions	Reductions/ Reclassifications	Ending Balance
Capital assets:				
Information systems	$ -	$ 66,329	$ -	$ 66,329
Office furniture and equipment	-	33,967	-	33,967
Vehicles	-	66,135	-	66,135
Total capital assets	-	166,431	-	166,431
Less accumulated depreciation and amortization for:				
Information systems	-	(35,494)	-	(35,494)
Office furniture and equipment	-	(23,094)	-	(23,094)
Vehicles	-	(66,132)	-	(66,132)
Total accumulated depreciation and amortization	-	(124,720)	-	(124,720)
Capital assets governmental activities — net	$ -	$ 41,711	$ -	41,711

Business Type - Activities

Capital assets not being depreciated — land	Beginning Balance	Additions	Reductions/ Reclassifications	Ending Balance
Land	$ 2,845,000	$ -	$ -	$ 2,845,000
Land under development	-	-	56,454,861	56,454,861
	2,845,000	-	56,454,861	59,299,861
Total capital assets not being depreciated				
Capital assets being depreciated:				
Building	8,988,048	-	-	8,988,048
Leasehold improvements	4,429,170	53,599	(21,058)	4,461,711
Information systems	3,707,774	86,193	(1,762,379)	2,031,588
Office furniture and equipment	2,687,793	49,584	(24,686)	2,712,691
Software	3,522,685	1,147,199	(244,712)	4,425,172
Vehicles	217,119	-	(4)	217,115
Total capital assets being depreciated	23,552,589	1,336,575	(2,052,839)	22,836,325
Less accumulated depreciation and amortization for:				
Building	(2,134,660)	(224,701)	2	(2,359,363)
Leasehold improvements	(1,746,839)	(450,359)	21,058	(2,176,140)
Information systems	(2,468,416)	(513,508)	1,372,096	(1,609,828)
Office furniture and equipment	(1,949,436)	(299,324)	407,975	(1,840,785)
Software	(2,163,973)	(1,034,043)	251,443	(2,946,573)
Vehicles	(184,528)	(11,223)	264	(195,487)
Total accumulated depreciation and amortization	(10,647,852)	(2,533,158)	2,052,838	(11,128,176)
Total capital assets being depreciated — net	12,904,737	(1,196,583)	(1)	11,708,153
Capital assets business type activities — net	$15,749,737	$ (1,196,583)	$ 56,454,860	71,008,014
Total capital assets — net				$ 71,049,725

Land under development represents property owned by the Bank that is being developed for future government benefit. It was transferred from real estate available for sale to capital assets as of June 30, 2011, at cost. Specifically, as part of its functions of furthering the economic development of Puerto Rico, the Bank is developing the infrastructure and public spaces of the "Comunidad Río Bayamón Norte" as per the Master Plan approved by the Puerto Rico Planning Board. The infrastructure development includes the construction of the roads, sidewalks, electric, sanitary and sewer systems and an urban park with recreational area, clubhouse and tennis courts. As part of the development, the Bank is contributing to certain offsite improvements with the Puerto Rico Electric and Power Authority, the Puerto Rico Aqueduct and Sewer Authority and the Puerto Rico Highways and Transportation Authority. The development will have access to Tren Urbano's Jardines Station. Management is evaluating the transfer of these improvements and structures to the corresponding governmental agency for the proper maintenance upon completion of the development.

9. DEPOSITS

Deposits consist predominantly of interest-bearing demand accounts, special government deposit accounts, and time deposits from the Commonwealth, its agencies, instrumentalities, and municipalities. Interest expense on these deposits amounted to approximately $94 million in 2011.

10. SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE

The following is selected information concerning securities sold under agreements to repurchase:

Carrying amount at June 30, 2011	$ 970,818,550
Maximum amount outstanding at any month-end	970,818,550
Average amount outstanding during the year	650,175,776
Weighted average interest rate for the year	2.43%
Weighted average interest rate at year-end	0.13%

The following summarizes the activity of securities sold under agreements to repurchase for the year ended June 30, 2011:

	Beginning Balance	Issuances	Maturities	Ending Balance
GDB Operating Fund	$ 1,058,834,752	$4,477,337,335	$4,565,353,537	$ 970,818,550

All sales of investments under agreements to repurchase are for fixed terms. In investing the proceeds of securities sold under agreements to repurchase, the Bank's policy is for the term to maturity of investments to be on or before the maturity of the related repurchase agreements. At June 30, 2011, the total amount of securities sold under agreements to repurchase mature within one year.

11. CERTIFICATES OF INDEBTEDNESS

Certificates of indebtedness consist of time deposits from corporations that have grants of tax exemptions under the Commonwealth's industrial incentives laws. The following summarizes the certificates of indebtedness activity for the year ended June 30, 2011:

	Beginning Balance	Issuances	Maturities	Ending Balance	Due Within One Year
GDB Operating Fund	$11,800,000	$ -	$ 7,500,000	$ 4,300,000	$4,300,000

At June 30, 2011, certificates of indebtedness amounting to approximately $4.3 million contractually mature during the fiscal year ending June 30, 2012.

12. BONDS, NOTES, AND MORTGAGE-BACKED CERTIFICATES PAYABLE, AND OTHER LIABILITIES

The activity of bonds payable and other borrowed funds for the year ended June 30, 2011 is as follows:

	Beginning Balance	Debt Issued	Debt Paid	Reductions	Ending Balance	Due Within One Year
Governmental activities — Commonwealth appropriation bonds and notes — note payable — AHMSP Stage 7	$4,811,237	$ -	$ -	$ -	$4,811,237	$ -

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Business-type activities:					
GDB Operating Fund:					
Adjustable Refunding Bonds	$ 267,000,000	$ -	$ -	$ 267,000,000	$ -
Senior Notes 2006 Series B	428,655,000		(63,295,000)	365,360,000	62,665,000
Senior Notes 2006 Series C	81,960,000			81,960,000	
Senior Notes 2008 Series A	571,533,000		(571,533,000)		
Senior Notes 2008 Series B	195,467,000		(195,467,000)		
Senior Notes 2009 Series A	250,000,000		(250,000,000)		
Senior Notes 2009 Series B	200,000,000		(200,000,000)		
Senior Notes 2009 Series C	1,013,200,000		(53,427,000)	959,773,000	
Senior Notes 2009 Series D	342,876,000		(41,718,000)	301,158,000	
Senior Notes 2010 Series A		1,448,741,000		1,448,741,000	28,316,000
Senior Notes 2010 Series B		151,259,000		151,259,000	
Senior Notes 2010 Series C		1,086,478,000		1,086,478,000	
Senior Notes 2010 Series D		96,411,000		96,411,000	
Senior Notes 2011 Series A		70,000,000		70,000,000	
Senior Notes 2011 Series B		650,000,000		650,000,000	
Add (deduct) unamortized premium (discount)	7,065,393		(2,132,927)	4,932,466	157,136
Total GDB Operating Fund	3,357,756,393	3,502,889,000	(1,377,572,927)	5,483,072,466	91,138,136
Housing Finance Authority					
Mortgage Trust III	904,333,874		(42,530,000)	861,803,874	42,030,000
Revenue bonds:					
Single Family Mortgage Revenue Bonds — Portfolio IX	107,295,000		(9,145,000)	98,150,000	2,210,000
Single Family Mortgage Revenue Bonds — Portfolio X	73,625,000		(3,350,000)	70,275,000	1,275,000
Single Family Mortgage Revenue Bonds — Portfolio XI	18,910,000		(630,000)	18,280,000	310,000
Homeownership Mortgage Revenue Bonds 2000	47,905,000		(3,700,000)	44,205,000	1,065,000
Homeownership Mortgage Revenue Bonds 2001	50,220,000		(4,720,000)	45,500,000	1,210,000
Homeownership Mortgage Revenue Bonds 2003	23,315,000		(1,460,000)	21,855,000	580,000
Mortgage-Backed Certificates — 2006 Series A	120,259,292		(9,070,382)	111,188,910	19,879,063
Total revenue bonds	441,529,292		(32,075,382)	409,453,910	26,529,063
Subtotal	1,345,863,166		(74,605,382)	1,271,257,784	68,559,063
Notes payable:					
GDB	3,495,586	431,395	(1,219,926)	2,707,055	
Special obligation notes	15,000,000	14,000,000		29,000,000	
Citibank notes		80,000,000	(80,000,000)		
Plus unamortized premium	498,253		(36,004)	462,249	
Less unaccreted discount and deferred amount on refunds	(488,082,569)	(6,860,000)	33,302,423	(461,640,146)	
Total Housing Finance Authority	876,774,436	87,571,395	(122,558,889)	841,786,942	68,559,063
Tourism Development Fund:					
Participation agreement payable	26,000,000			26,000,000	
Notes payable to GDB	362,780,208	44,436,268	(7,700,000)	399,516,476	8,400,000
Total Tourism Development Fund	388,780,208	44,436,268	(7,700,000)	425,516,476	8,400,000
Total	4,623,311,037	3,634,896,663	(1,507,831,816)	6,750,375,884	168,097,199
Less intrafund eliminations	(517,105,240)	(44,867,663)	(3,377,726)	(565,350,629)	(8,400,000)
Total business-type activities	$ 4,106,205,797	$ 3,590,029,000	$ (1,511,209,542)	$ 6,185,025,255	$ 159,697,199

The annual debt service requirements to maturity, including principal and interest, for long-term debt, (excluding notes payable by component units to the Bank) as of June 30, 2011 are as follows:

Years Ending June 30,	GDB Operating Fund Business-Type Activities Principal	Interest	Interest Subsidy (1)	Total
2012	$ 90,981,000	$ 261,859,100	$ (4,984,359)	$ 256,874,741
2013	538,934,000	250,917,106	(4,984,359)	245,932,747
2014	601,727,000	229,344,105	(4,984,359)	224,359,746
2015	1,071,850,000	185,696,752	(4,984,359)	180,712,393
2016	469,065,000	154,119,264	(4,984,359)	149,134,905
2017-2021	2,185,103,000	344,613,780	(24,921,801)	319,691,979
2022-2026	520,480,000	67,699,702	(24,803,957)	42,895,745
Total	$ 5,478,140,000	$ 1,494,249,809	$ (74,647,553)	$ 1,419,602,256

(1) The GDB Senior Notes Series 2010 B and 2010 D were issued as Build America Bonds. The Bank will receive a subsidy payment from the federal government equal to 35% of the amount of each interest payment.

Years Ending June 30,	Housing Finance Authority Governmental Activities Principal	Governmental Activities Interest	Business-Type Activities Principal	Business-Type Activities Interest
2012	$ -	$ 261,554	$ 68,559,063	$ 4,846,999
2013		201,452	57,267,066	4,151,196
2014	95,757	217,922	54,392,294	3,717,371
2015	89,306	215,785	50,536,769	3,306,565
2016	107,858	208,628	49,693,737	2,926,059
2017-2021	554,872	913,724	244,359,480	13,532,646
2022-2026	851,237	731,534	594,191,519	12,289,458
2027-2031	3,112,207	422,339	89,758,935	7,512,229
2032-2036			70,950,433	4,866,472
2037-2040			20,548,488	1,440,264
Total	$4,811,237	$3,172,938	$1,300,257,784	$ 58,589,259

Years Ending June 30,	Tourism Development Fund (1) Business-Type Activities Principal	Interest
2012	$ -	$ 730,600
2013		730,600
2014		730,600
2015		730,600
2016		730,600
2017-2019	26,000,000	1,461,200
Total	$26,000,000	$5,114,200

(1) Debt service requirements of this variable-rate debt assume that the interest rate effective at June 30, 2011 remains the same throughout the term of the debt.

Governmental Activities — Bonds and notes payable by governmental activities as of June 30, 2011 consist of the following:

Description and Maturity Date	Interest Rate	Amount Outstanding
Note payable Affordable Housing Mortgage Subsidy Program Stage 7 — due on July 1, 2014 and each July 1, thereafter to July 1, 2031	4.10%–5.25%	$4,811,237

Note Payable to Puerto Rico Public Finance Corporation — On December 27, 2001, the Housing Finance Authority entered into a loan agreement (the "Note") with the GDB Operating Fund to refinance the Affordable Housing Mortgage Subsidy Program Stage 7 note payable (the "Old Note") of the Housing Bank, as authorized by Act No. 164 of December 17, 2001. The Public Finance Corporation acquired and restructured the Note through the issuance of its Commonwealth appropriations bonds ("PFC Bonds"). The PFC Bonds were issued under a trust indenture whereby the Public Finance Corporation pledged and sold the Note, along with other notes under Act No. 164, to certain trustees and created a first lien on the revenues of the notes sold. The notes payable to the Public Finance Corporation were originally composed of a loan granted by the Bank, which, pursuant to Act No. 164 of December 17, 2001, the Public Finance Corporation acquired and restructured through the issuance of Commonwealth appropriation bonds. These bonds were issued under trust indenture agreements whereby the Public Finance Corporation pledged the notes to certain trustees and created a first lien on the pledged revenue (consisting of annual Commonwealth appropriations earmarked to repay these notes) for the benefit of the bondholders.

During June 2004, the Public Finance Corporation advance refunded a portion of certain of its outstanding Commonwealth appropriation bonds issued in 2001 under Act No. 164 of December 17, 2001. The Housing Finance Authority recognizes a mirror effect of this advance refunding by the Public Finance Corporation in its own notes payable in proportion to the portion of the Housing Finance Authority's notes payable included in the Public Finance Corporation refunding. The aggregate debt service requirements of the refunding and unrefunded notes will be funded with annual appropriations from the Commonwealth.

The outstanding balance of this Note at June 30, 2011 was $4,811,237 and matures on July 1, 2031. Interest on the unpaid principal amount of the Note is equal to the applicable percentage of the aggregate interest payable on the Public Finance Corporation Bonds. Applicable percentage is the percentage representing the proportion of the amount paid by Public Finance Corporation on the PFC Bonds serviced by the Note to the aggregate amount paid by Public Finance Corporation on all the PFC Bonds issued by Public Finance Corporation under Act No. 164.

Business-Type Activities — Bonds, notes and mortgage-backed certificates payable of business-type activities consist of the following:

Description and Maturity Date	Interest Rate		Carrying Amount
Remarketed Refunding Bonds —December 1, 2015	4.75%	$	267,000,000
GDB Senior Notes :			
Series 2006 B — Each December 1 until December 1, 2017	5.00		368,832,386
Series 2006 C — January 1, 2015	5.25		83,420,080
Series 2009 C — Each February 1 from 2011 to 2022	2.50–6.00		959,773,000
Series 2009 D — Each February 1 from 2011 to 2022	2.50–6.00		301,158,000
Series 2010 A — Each August 1 from 2011 to 2020	2.00–5.50		1,448,741,000
Series 2010 B — August 1, 2025	5.75		151,259,000
Series 2010 C — Each August 1 from 2012 to 2019	3.00–5.40		1,086,478,000
Series 2010 D — August 1, 2025	5.75		96,411,000
Series 2011 A — April 1, 2014	3.9		70,000,000
Series 2011 B — May 1, 2014 and May 1, 2016	3.67–4.704		650,000,000
Mortgage Trust III:			
Each July 1 and January 1 until July 1, 2011	Zero Coupon		21,250,000
Each July 1 and January 1 until January 1, 2021	Zero Coupon		241,014,876
Single Family Mortgage Revenue Bonds — Portfolio IX — Each December 1 and June 1 until December 1, 2012	4.85%–5.60%		98,150,000
Single Family Mortgage Revenue Bonds – Portfolio X — Each December and June 1 until December 1, 2037	4.60%–5.65%		70,275,000
Single Family Mortgage Revenue Bonds — Portfolio XI — Each December 1 and June 1 until December 1, 2039	3.460%–5.45%		18,280,000
Homeownership Mortgage Revenue Bonds 2000 Series — Each June 1 and December 1 until December 1, 2032	4.65%–5.20%		44,205,000
Homeownership Mortgage Revenue Bonds 2001 Series:			
Each December 1 until December 1, 2012	4.60%-4.70%		2,495,000
June 1, 2013, and each December 1 and June 1 thereafter until December 1, 2033	5.30%–5.50%		43,005,000
Homeownership Mortgage Revenue Bonds 2003 Series:			
Each December 1 until December 1, 2013	3.80%–4.00%		1,805,000
June 1, 2013, and each December 1 and June 1 thereafter to December 1, 2033	4.375%–4.875%		20,050,000
Mortgage-Backed Certificates, 2006 Series A — Principal and interest payable monthly from September 29, 2006 to August 29, 2030	2.955%–6.560%		99,641,122
Special Obligation Notes, 2010 Series A and B — November 1, 2040	6.96%-6.974%		15,781,791
Total		$	6,159,025,255

GDB Senior Notes, 2010 Series A — On July 29, 2010, the Bank issued $1,448,741,000 of Senior Notes, 2010 Series A (the "2010 Series A Notes"). The 2010 Series A Notes consist of term notes maturing on various dates from August 1, 2011 to August 1, 2020, and carrying fixed interest rates ranging from 2.00% to 5.50%, payable monthly on the first day of each month. The 2010 Series A Notes are subject to redemption prior to maturity at the option of the Bank, either in whole or in part (and if in part, in such order of maturity as directed by the Bank), at a price equal to the principal amount to be redeemed plus accrued interest to the date of redemption, without premium, on August 1, 2011 and on any date thereafter, subject to at least 20 days prior notice.

GDB Senior Notes, 2010 Series B — On July 29, 2010, the Bank issued $151,259,000 of Senior Notes, 2010 Series B (the "2010 Series B Notes"). The 2010 Series B Notes consist of term notes maturing on August 1, 2025, and carrying a fixed interest rate of 5.75 %, payable quarterly on each February 1, May 1, August 1 and November 1. Upon compliance with certain requirements of the U.S. Internal Revenue Code, the Bank will receive a subsidy payment from the federal government equal to 35% of the amount of each interest payment of the Notes. The 2010 Series B Notes are subject to redemption prior to maturity at the option of the Bank, either in whole or in part, at a price equal to the principal amount to be redeemed plus accrued interest to the date of redemption, without premium, on August 1, 2011 and on any date thereafter, subject to at least 20 days prior notice.

GDB Senior Notes, 2010 Series C — On August 24, 2010, the Bank issued $1,086,478,000 of Senior Notes, 2010 Series C (the "2010 Series C Notes"). The 2010 Series C Notes consist of term notes maturing on various dates from August 1, 2012 to August 1, 2019, and carrying fixed interest rates ranging from 3.00% to 5.40%, payable monthly on the first day of each month. The 2010 Series C Notes are subject to redemption prior to maturity at the option of the Bank, either in whole or in part (and if in part, in such order of maturity as directed by the Bank), at a price equal to the principal amount to be redeemed plus accrued interest to the date of redemption, without premium, on September 1, 2011 and on any date thereafter, subject to at least 20 days prior notice.

GDB Senior Notes, 2010 Series D — On August 24, 2010, the Bank issued $96,411,000 of Senior Notes, 2010 Series D (the "2010 Series D Notes"). The 2010 Series D Notes consist of term notes maturing on August 1, 2025, and carrying a fixed interest rate of 5.75 %, payable quarterly on each February 1, May 1, August 1 and November 1. Upon compliance with certain requirements of the U.S. Internal Revenue Code, the Bank will receive a subsidy payment from the federal government equal to 35% of the amount of each interest payment of the Notes. The 2010 Series D Notes are subject to redemption prior to maturity at the option of the Bank, either in whole or in part, at a price equal to the principal amount to be redeemed plus accrued interest to the date of redemption, without premium, on September 1, 2011 and on any date thereafter, subject to at least 20 days prior notice.

GDB Senior Notes, 2011 Series A — On March 2, 2011, the Bank issued $70,000,000 of Senior Notes, 2011 Series A (the "2011 Series A Notes"). The 2011 Series A Notes consist of term notes maturing on April 1, 2014, and carrying a fixed interest rate of 3.90%, payable monthly on the first day of each month.

GDB Senior Notes, 2011 Series B — On May 26, 2011, the Bank issued $650,000,000 of Senior Notes, 2011 Series B (the "2011 Series B Notes"). The 2011 Series B Notes consist of term notes maturing on May 1, 2014 and May 1, 2016, and carrying fixed interest rates ranging from 3.670% to 4.704%, payable semi-annually arrears on the first day of May and November. The 2011 Series B Notes are subject to redemption prior to maturity at the option of the Bank, either in whole or in part (and if in part, in such order of maturity as directed by the Bank), at a price equal to the greater of the principal amount to be redeemed or the sum of the present value of the remaining schedule payments of principal and interest to the maturity date of the 2011 Series B Notes to be redeemed, subject to at least 30 days prior notice.

Special Obligation Notes, 2010 Series A and B — On October 22, 2009 and November 10, 2010, the Housing Finance Authority issued $15,000,000 and $14,000,000 respectively, of Special Obligation Notes, 2010 Series A and 2010 Series B, respectively. These notes are collateralized by certain second mortgage loans originated under the Home Purchase Stimulus Program. The notes will be repaid from collections of principal and interest of the underlying collateral, net of servicing and guarantee fees. The second mortgage loans are guaranteed by the Housing Finance Authority's Act No. 87 insurance fund.

Participation Agreement Payable — On April 10, 2006, the Tourism Development Fund entered into a debt restructuring agreement with Hotel Dorado, S.E. (the "Hotel") whereby the Tourism Development Fund, as guarantor of the Hotel's outstanding bonds, accelerated the payment of the bonds in exchange for a note receivable of $26 million (the "Note") from the Hotel. In addition, on April 10, 2006, the Tourism Development Fund entered into a participation agreement with a financial institution whereby the Tourism Development Fund transferred a 100% participation (the "Participation") in the Note.

The Participation is subject to recourse and the Tourism Development Fund is obligated to purchase the loan from the financial institution upon the occurrence and during the continuance of an event of default under the participation agreement. The participation agreement also stipulates that the financial institution cannot sell, pledge, transfer, assign or dispose of the Participation without the Tourism Development Fund's consent. Accordingly, the Tourism Development Fund has recorded the Note as part of loans receivable and has recorded a participation agreement payable (i.e. a collateralized borrowing) in the accompanying statement of net assets (deficiency) and balance sheet — enterprise funds.

The Participation bears a variable interest rate based on the three-month LIBOR plus 2.50%, until maturity. Interest is payable on a quarterly basis. In August 2008, The Tourism Development Fund agreed to extend the maturity to July 1, 2018 and approved a conditional-commitment to provide a guarantee for a permanent loan to be provided by the financial institution upon completion of the construction of some amenities and subject to compliance with certain conditions. The outstanding principal balance of the Note and the corresponding participation agreement payable amounted to $26 million as of June 30, 2011.

The activity for noncurrent accounts payable and accrued liabilities during the year ended June 30, 2011 follows:

Balance — beginning of period	$ 7,283,627
Additions	766,699
Reductions	(2,877,034)
Balance — end of period	$ 5,173,292

The activity for compensated absences included within accounts payable and accrued liabilities during the year ended June 30, 2011 follows:

	Beginning Balance	Provision	Reductions	Ending Balance	Due Within One Year
Vacation	$2,725,603	$2,339,445	$2,684,075	$2,380,973	$ 2,344,696
Sickness	2,677,182	1,419,170	1,818,652	2,277,700	1,547,278
Total	$5,402,785	$3,758,615	$4,502,727	$4,658,673	$ 3,891,974

Compensated absences are available to be liquidated by the employees during the year.

13. RESTRICTED NET ASSETS — MORTGAGE LOAN INSURANCE FUND

The Mortgage Loan Insurance fund was created by Act No. 87 of June 25, 1965, as amended, known as the *Mortgage Loan Insurance*. This act provides mortgage credit insurance to low- and moderate-income families on loans originated by the Housing Finance Authority and other financial institutions. This activity can be increased through legislative appropriations, if and when needed, and derives its revenue from premiums charged to the borrowers, interest on investments, and sales of properties acquired through foreclosure. The Housing Finance Authority manages the risk of loss of its mortgage loan insurance activities by providing its insurance program only to financial institutions that (1) maintain certain defined minimum capital, (2) are qualified based on experience and resources, (3) perform certain collection efforts, and (4) comply with established procedures and requirements. In addition, the Housing Finance Authority requires certain loan-to-value ratios on loans insured and recording of the collateral in the property registry of the Commonwealth.

During the year ended June 30, 2008, the Housing Finance Authority created the Puerto Rico Housing Administration program, known in Spanish as "FHA Boricua," expanding requirements and parameters under the existing act. The program allows citizens, paying an annual insurance premium, to originate mortgage loans with up to a 98% loan-to-value ratio. The program insures participating lending institutions in events of foreclosure. The program is financed through annual insurance premiums, commitment and transaction fees, and proceeds from any sale of foreclosed real estate. The program also requires participants to comply with various eligibility requirements.

The Commonwealth guarantees up to $75 million of the principal insured by the mortgage loan insurance program. As of June 30, 2011, the mortgage loan insurance program covered loans aggregating to approximately $566 million.

The regulations adopted by the Housing Finance Authority require the establishment of adequate reserves to guarantee the solvency of the Mortgage Loan Insurance Fund. At June 30, 2011, the Housing Finance Authority had restricted net assets for such purposes of approximately $61.1 million and an estimated liability for losses on mortgage loan insurance of approximately $3.7 million.

The summary of the activity in the allowance for losses on mortgage loan insurance for the year ended June 30, 2011, is as follows:

Balance — beginning of year	$ 346,330
Provision for losses on mortgage loan insurance	3,325,677
Claims paid	(3,064,766)
Foreclosed real estate acquired from insured financial institutions	3,064,766
Balance — end of year	$ 3,672,007

14. TERMINATION BENEFITS

On October 13, 2010, the Bank announced to its employees a voluntary termination plan (the "Plan") based on Act No. 70 enacted on July 2, 2010. The Plan was approved by the Bank's board of directors on October 6, 2010. Act No. 70 provides that eligible employees may retire from employment with the Commonwealth in exchange for an early pension, an economic incentive and other benefits. The Plan only applied to employees who were ten years or less from retirement in accordance with their applicable retirement plans as of December 31, 2010. The Plan approved by the Bank's board of directors provides the following:

- The employee will receive an annuity of fifty percent of salary in effect at September 30, 2010. The Bank is responsible for the payment of the annuity in addition to the related employee and employer contributions to the Retirement System for a maximum period of ten years.
- The employee will receive an economic incentive of six month's salary. This incentive is exempt from income taxes as established by Act No. 70.
- The employee will receive the benefits of health and dental insurance for a period of one year.

The total amount of employees that were voluntarily separated from employment was five. Total cost related to these termination benefits was $2.6 million. Employee and employer contributions to the Retirement System and the employee annuity for the applicable period were discounted based on the average interest rate of unpledged investments. As of June 30, 2011, the total liability related to this plan was approximately $2.2 million.

15. FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK

In the normal course of business, the Bank is party to transactions involving financial instruments with off-balance-sheet risk to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit, and financial guarantees. These instruments involve, to varying degrees, elements of credit risk in excess of amounts recognized in the accompanying statement of net assets and fund balance sheets. These off-balance-sheet risks are managed and monitored in manners similar to those used for on-balance-sheet risks. The Bank's exposures to credit loss for lending commitments, financial guarantees, and letters of credit are represented by the contractual amount of those transactions.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank, as applicable, evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained upon extension of credit is based on management's credit evaluation of the counterparty. Collateral held varies but may include property, plant, and equipment, and income-producing commercial properties. Standby letters of credit and financial guarantees are written conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

At June 30, 2011, the off-balance-sheet risks consisted of the following (in thousands):

Financial instruments whose credit risk is represented by contractual amounts:

Financial guarantees:	
Public sector	$ 52,000
Private sector	357,864
Total	$ 409,864
Standby letters of credit — Public sector	$ 674,429
Commitments to extend credit:	
Public sector	$ 2,418,998
Private sector	51,000
Total	$ 2,469,998

Following is the activity of the allowance for losses on guarantees and letters of credit for the year ended June 30, 2011:

	Beginning Balance	Provision (Credit)	Payments / Reductions	Ending Balance	Due Within One Year
GDB Operating Fund	$ 1,000,000	$ (1,000,000)	$ -	$ -	$ -
Tourism Development Fund	21,284,600	2,370,598	-	23,655,198	-
Development Fund	2,490,804	1,496,066	2,486,870	1,500,000	1,500,000
Total	$24,775,404	$ 2,866,664	$2,486,870	$25,155,198	$ 1,500,000

16. RETIREMENT SYSTEM

Defined Benefit Pension Plan — The Employees' Retirement System of the Government of the Commonwealth of Puerto Rico (the "Retirement System"), created pursuant to Act No. 447 of May 15, 1951, as amended, is a cost-sharing, multiple-employer, defined benefit pension plan sponsored by and reported as a component unit of the Commonwealth. All regular employees of the Bank hired before January 1, 2000 and less than 55 years of age at the date of employment became members of the Retirement System as a condition of their employment. No benefits are payable if the participant receives a refund of their accumulated contributions.

The Retirement System provides retirement, death, and disability benefits pursuant to legislation enacted by the Legislature. Retirement benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after 10 years of plan participation. Disability benefits are available to members for occupational and nonoccupational disabilities. However, a member must have at least 10 years of service to receive nonoccupational disability benefits.

Members who have attained 55 years of age and have completed at least 25 years of creditable service, or members who have attained 58 years of age and have completed 10 years of creditable service, are entitled to an annual benefit payable monthly for life. The amount of the annuity shall be 1.5% of the average compensation, as defined, multiplied by the number of years of creditable service up to 20 years, plus 2% of the average compensation, as defined, multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than $200 per month.

Participants who have completed 30 years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained 55 years of age will receive 65% of the average compensation, as defined; otherwise, they will receive 75% of the average compensation, as defined.

Commonwealth's legislation requires employees to contribute 5.775% of the first $550 of their monthly gross salary and 8.275% for the excess over $550 of monthly gross salary. The Bank is required by the same statute to contribute 9.275% of each participant's gross salary. On July 6, 2011, Act No. 116 was approved to increase the employer's contribution for each participant. Starting on July 1, 2011, the employer's contribution will be 10.275% and will increase annually by 1.00% until June 30, 2016. Effective July 1, 2016, the employer's contribution will increase by 1.25% annually, until reaching 20.525%.

Defined Contribution Plan — The Legislature enacted Act No. 305 on September 24, 1999, which amended Act No. 447 to establish, among other things, a defined contribution savings plan program (the "Program") to be administered by the Retirement System. All regular employees hired for the first time on or after January 1, 2000, and former employees who participated in the defined benefit pension plan, received a refund of their contributions, and were rehired on or after January 1, 2000, become members of the Program as a condition to their employment. In addition, employees who at December 31, 1999 were participants of the defined benefit pension plan had the option, up to March 31, 2000, to irrevocably transfer their prior contributions to the defined benefit pension plan plus interest thereon to the Program.

Act No. 305 requires employees to contribute 8.275% of their monthly gross salary to the Program. Employees may elect to increase their contribution up to 10% of their monthly gross salary. Employee contributions are credited to individual accounts established under the Program. Participants have three options to invest their contributions to the Program. Investment income is credited to the participant's account semiannually.

The Bank is required by Act No. 305 to contribute 9.275% of each participant's gross salary. The Retirement System will use these contributions to increase its asset level and reduce the unfunded status of the defined benefit pension plan. On July 6, 2011, Act. No. 116 was approved to increase the employer's contribution for each participant. Starting on July 1, 2011, the employer's contribution will be 10.275% and will increase annually by 1.00% until June 30, 2016. Effective July 1, 2016, the employer's contribution will increase by 1.25% annually, until reaching 20.525%.

Upon retirement, the balance in each participant's account will be used to purchase an annuity contract, which will provide for a monthly benefit during the participant's life and 50% of such benefit to the participant's spouse in case of the participant's death. Participants with a balance of $10,000 or less at retirement will receive a lump-sum payment. In case of death, the balance in each participant's account will be paid in a lump sum to the participant's beneficiaries. Participants have the option of receiving a lump sum or purchasing an annuity contract in case of permanent disability.

Total employee contributions for the defined benefit pension plan and the defined contribution plan during the year ended June 30, 2011 amounted to approximately $719,000 and $827,000 respectively. The Bank's contributions during the years ended June 30, 2011, 2010, and 2009 amounted to approximately $1,731,000, $1,910,000, and $1,946,000, respectively. These amounts represented 100% of the required contribution for the corresponding year. Individual information for each option is not available since the allocation is performed by the Retirement System itself.

Additional information on the Retirement System is provided in its stand alone financial statements for the year ended June 30, 2011, a copy of which can be obtained from the Employees' Retirement System of the Commonwealth of Puerto Rico, P.O. Box 42004, San Juan PR 00940-2004.

17. COMMITMENTS AND CONTINGENCIES

Lease Commitments — The Bank leases office and storage space from the governmental and private sectors. Principally, office space is leased under a short-term operating lease agreement that renews automatically every year, if it is not canceled by any of the parties before the beginning of each year. The storage space agreement expires in July 2016. In addition, during fiscal year 2010, the Bank entered into a lease agreement with the Puerto Rico Industrial Development Company (PRIDCO) for office space in PRIDCO's New York Office. This agreement expires in 2022.

The Housing Finance Authority entered into a 30 year lease agreement with the Puerto Rico Department of Housing (PRDH) to rent office space expiring in 2037. During the term of the lease, the Housing Finance Authority will pay an annual rent of $1.5 million. The agreed upon rent includes parking spaces, maintenance and security services in common areas. PRDH will be responsible for the payment of utilities in exchange for an additional payment of $350,000 payable in a lump sum on or before August 31st of each year.

Rent charged to operations in fiscal year 2011 amounted to approximately $2.7 million. At June 30, 2011, the minimum annual future rentals under noncancelable leases are approximately as follows:

Year Ending June 30,	Amount
2012	$ 2,932,000
2013	2,943,000
2014	2,949,000
2015	2,957,000
2016	2,964,000
Thereafter	54,812,000
Total	$69,557,000

Cooperative Development Investment Fund — On August 18, 2002, the Legislature approved Law No. 198, which creates the Cooperative Development Investment Fund. The purpose of this fund is to promote the development of cooperative entities. This fund will be capitalized through contributions to be provided by the Bank up to $25 million to be matched by cooperative entities. As of June 30, 2011, the Bank has contributed $16.9 million to the Cooperative Development Investment Fund, $673,000 of which were contributed during the year ended June 30, 2011.

Other Risks Related to Mortgage Loans Servicing and Insurance Activities — Certain loan portfolios of the Housing Finance Authority are administered by private servicers who are required to maintain an error and omissions insurance policy. The Housing Finance Authority has a program to manage the risk of loss on its mortgage loan lending and insurance activities.

Loan Guarantees — The Development Fund has entered into an agreement (the "Agreement") with Economic Development Bank for Puerto Rico (EDB) whereby the Development Fund would guarantee a portion of loans granted by EDB under a government program named The Key for Your Business (the "Program"). Under the Agreement, the Development Fund would assign $15 million of its capital for the program. The Development Fund guarantees one-third of the outstanding principal balance of each loan plus accrued interest and certain other charges. The Development Fund charges one percent of the loan amount as guarantee fee and no loan can exceed $50,000. At June 30, 2011, the outstanding balance of loans guaranteed amounted to approximately $14.2 million and the allowance for losses on guarantees amounted to by the Development Fund approximately $1.5 million.

Custodial Activities of Enterprise Funds — At June 30, 2011, the Housing Finance Authority was custodian of approximately $212,000 in restricted funds of the former "*Corporación de Renovación Urbana y Vivienda*" (CRUV). As of June 30, 2011, such funds are deposited with the Bank. These funds are not owned by the Housing Finance Authority's enterprise funds and thus are not reflected in the accompanying basic financial statements.

Loan Sales and Securitization Activities — On July 13, 1992, the Housing Finance Authority entered into an agreement to securitize approximately $20.7 million of mortgage loans into a FNMA certificate. The Housing Finance Authority agreed to repurchase, at a price of par plus accrued interest, each and every mortgage loan backing up such security certificate that become delinquent for 120 days or more. As of June 30, 2011, the aggregate outstanding principal balance of the loans pooled into the FNMA certificate amounted to approximately $545,295.

Mortgage Loan Servicing Activities — The Housing Finance Authority acts as servicer for a number of mortgage loans owned by other investors. The servicing is generally subcontracted to a third party. As of June 30, 2011, the principal balance of the mortgage loans serviced for others is approximately as follows:

Popular Mortgage, Inc.	$ 37,609
R-G Mortgage, Inc.	1,439,434
CRUV or its successor without guaranteed mortgage loan payments	42,929
Total	$1,519,972

HOME Program — The U.S. Office of Inspector General (OIG) has performed various examinations of the HOME Program covering fiscal years ended prior to July 1, 2010. These examinations covered the periods in which the HOME Program was under the administration of the Department of Housing. These examinations identified instances of noncompliance with terms and conditions of the grant agreements, applicable federal law, and the HOME Program's regulations, including but not limited to the expenditure of resources for eligible purposes. OIG identified in its examinations disallowed costs amounting to approximately of $18.3 million. The Housing Finance Authority's management is of the opinion that these disallowed costs are a liability of the Department of Housing and, therefore, the Housing Finance Authority has not recorded a contingency in its basic financial statements.

Litigation — The Bank and certain if its component units are defendants in several lawsuits arising out of the normal course of business. Management, based on advice of legal counsel, is of the opinion that the ultimate liability, if any, resulting from these pending proceedings will not have a material adverse effect on the financial position and results of operations of the Bank or its component units.

18. NO-COMMITMENT DEBT AND PROGRAMS SPONSORED BY THE HOUSING FINANCE AUTHORITY

The Public Finance Corporation has issued approximately $5.9 billion of Commonwealth appropriation bonds (the "Bonds") maturing at various dates through 2032. The proceeds of the Bonds, except for approximately $1.7 billion, were used to provide the necessary funds to purchase from the Bank separate promissory notes of the Department of the Treasury of the Commonwealth and certain of its instrumentalities and public corporations (the "Promissory Notes"). The $1.7 billion referred to above were used to refund a portion of certain bonds issued by the Public Finance Corporation (also no-commitment debt) between fiscal years 1995 and 2005. The outstanding balance of the Bonds at June 30, 2011 amounted to approximately $1.6 billion.

The Bonds are limited obligations of the Public Finance Corporation and, except to the extent payable from bond proceeds and investment earnings thereon, will be payable solely from a pledge and assignment of amounts due under the Promissory Notes. Principal and interest on the Promissory Notes are payable solely from legislative appropriations to be made pursuant to acts approved by the Legislature of the Commonwealth. These acts provide that the Commonwealth shall honor the payment of principal and interest on the Promissory Notes, and that the Director of the OMB shall include in the budget of the Commonwealth submitted to the Legislature the amounts necessary to pay the principal and interest on the Notes. The underlying Promissory Notes represent debt of the issuing instrumentalities (all part of the Commonwealth or its component units), and, for purposes of the Public Finance Corporation, the Bonds are considered no-commitment debt. Neither the Bonds nor the Notes purchased with the proceeds therefrom are presented in the accompanying basic financial statements.

Certain bonds of the Housing Finance Authority are considered no-commitment debt as more fully described in Note 2. At June 30, 2011, there were restricted assets held in trust by others, outstanding obligations, fund balances, and excess of fund expenses over revenues, net of transfers (all of which are excluded from the accompanying basic financial statements), as indicated below (unaudited):

Restricted assets	$	1,804,410
Restricted liabilities (no-commitment debt)		1,804,410
Restricted fund balance	$	-
Excess of fund expenses over revenues	$	1,033,159

In December 2003, the Housing Finance Authority issued $663 million in Capital Fund Program Bonds Series 2003 to lend the proceeds thereof to the Public Housing Administration (PHA), a governmental instrumentality of the Commonwealth. PHA utilized such funds for improvements to various public housing projects in the Commonwealth. The Capital Fund Program Bonds Series 2003 are limited obligations of the Housing Finance Authority, which will be paid solely from an annual allocation of public housing capital funds when received from the U.S. Department of Housing and Urban Development and other funds available under the bonds indenture. Accordingly, these bonds are considered no-commitment debt and are not presented in the accompanying basic financial statements. The outstanding balance of these bonds amounted to $179,945,000 million at June 30, 2011.

On August 1, 2008, the Housing Finance Authority issued the Capital Fund Modernization Program Subordinate Bonds amounting to $384,475,000 and the Housing Revenue Bonds amounting to $100,000,000. The proceeds from the issuance were mainly used to finance a loan to a limited liability company (the "LLC") and pay the costs of issuance. The $384,475,000 bonds are limited obligations of the Housing Finance Authority, payable primarily by a pledge and assignment of federal housing assistance payments made available by the U.S. Department of Housing and Urban Development, with an outstanding balance of $343,840,000 at June 30, 2011. The $100,000,000 bonds are also limited obligations of the Housing Finance Authority, payable from amounts deposited in escrow accounts with a trustee and the proceeds of a loan to be made by the Housing Finance Authority to the LLC using moneys received as a grant from the Department of Housing of Puerto Rico. Payment of principal of the Housing Revenue Bonds is also secured by an irrevocable standby letter of credit issued by the Bank. These bonds are considered no-commitment debt and, accordingly, are excluded, along with the related assets held in trust, from the Housing Finance Authority's financial statements.

On February 23, 2009, the Housing Finance Authority entered into an agreement with the Department of Housing of the Commonwealth whereby a limited liability company was incorporated by the name of Puerto Rico Community Development Fund, LLC (PRCDF). PRCDF is a community development entity (CDE). A CDE is any duly organized entity treated as a domestic corporation or partnership for federal income tax purposes that: (a) has a primary mission of serving or providing investment capital for low-income communities or low-income persons; (b) maintains accountability to residents of low-income communities through their representation on any governing board of the entity or any advisory board to the entity; and (c) has been certified as a CDE by the CDFI Fund of the U.S. Department of Treasury. On March 2, 2009, in order to carry out its mission, PRCDF requested New Markets Tax Credits (NMTC). The NMTC Program permits taxpayers to receive a credit against Federal income taxes for making qualified equity investments in designated Community Development Entities. PRCDF received a $45 million NMTC allocation related to 2009.

19. CONTRIBUTION FROM PUERTO RICO INFRASTRUCTURE FINANCING AUTHORITY

On January 14, 2009, the Legislature enacted Act No. 3 to, among other; authorize the Puerto Rico Infrastructure Financing Authority, an affiliate of the Bank, to sell securities deposited at a corpus account, the proceeds of which would be used, among other, to make a contribution to the Bank. Approximately $555 thousand were contributed by the Puerto Rico Infrastructure Financing Authority to the Bank during fiscal year 2011.

20. ESTIMATED FAIR VALUE OF FINANCIAL INSTRUMENTS

For a significant portion of the Bank's financial instruments (principally loans and deposits) fair values are not readily available since there are no available trading markets. Accordingly, fair values can only be derived or estimated using valuation techniques, such as present-valuing estimated future cash flows using discount rates, which reflect the risk involved, and other related factors. Minor changes in assumptions or estimation methodologies may have a material effect on the results derived therefrom.

The fair values reflected below are indicative of the interest rate environment as of June 30, 2011 and do not take into consideration the effects of interest rate fluctuations. In different interest rate scenarios, fair value results can differ significantly. Furthermore, actual prepayments may vary significantly from those estimated resulting in materially different fair values.

The difference between the carrying value and the estimated fair value may not be realized, since, in many of the cases, the Bank intends to hold the financial instruments until maturity, or because the financial instruments are restricted. Comparability of fair values among financial institutions is not likely, due to the wide range of permitted valuation techniques and numerous estimates that must be made in the absence of secondary market prices.

The following methods and assumptions were used by the Bank in estimating fair values of the financial instruments for which it is practicable to estimate such values:

- Short-term financial instruments, such as cash and due from banks, federal funds sold, deposits placed with banks, certificates of deposit, due from federal government, repurchase agreements, certificates of indebtedness, and accrued interest receivable and payable have been valued at the carrying amounts reflected in the statement of net assets, as these are reasonable estimates of fair value given the relatively short period of time between origination of the instruments and their expected realization.

- Financial instruments that are primarily traded in secondary markets, such as most investments, were valued using either quoted market prices or quotations received from independent brokers/dealers or pricing service organizations.

- Financial instruments that are not generally traded, such as long-term deposits placed with banks, investment contracts, long-term certificates of deposit, and bonds, notes and mortgage-backed certificates issued with fixed interest rates, were fair valued using the present values of estimated future cash flows at the appropriate discount rates. Bonds and other borrowings issued with interest rates floating within certain ranges were fair valued at their outstanding principal balance. The fair value of liabilities with no defined maturities, such as demand deposits, was reported as the amounts payable upon demand.

- Loans, participation agreement payable, commitments to extend credit, financial guarantees and standby letters of credit to the private sector are mostly industrial development, tourism development, and low-cost housing development projects. For these types of loans and commitments, there is no secondary market, and the actual future cash flows may vary significantly as compared to the cash flows projected under the agreements, due to the degree of risk. Accordingly, management has opted not to disclose the fair value of these financial instruments, as such information may not be estimated with reasonable precision.

- Disclosure of the fair value of loans, commitments to extend credit, standby letters of credit, and financial guarantees relating to instrumentalities of the Commonwealth is omitted, as these agreements are with component units of the Commonwealth.

The following table presents the carrying amounts and estimated fair values of the Bank's financial instruments at June 30, 2011 (in millions):

Financial assets:		
Cash and due from banks	$ 347	$ 347
Federal funds sold	89	89
Deposits placed with banks	740	740
Due from federal government	21	21
Investments and investment contracts	5,349	5,483
Accrued interest receivable and other receivables	237	237
Financial liabilities:		
Demand deposits	3,783	3,783
Certificates of deposit	1,771	1,775
Certificates of indebtedness	4	4
Securities sold under agreements to repurchase	971	971
Accounts payable and accrued liabilities	149	149
Accrued interest payable	31	31
Bonds, notes, mortgage-backed vertificates and participation agreement payable	6,190	6,355

21. INTERFUND BALANCES AND TRANSFERS

The following table is a summary of the interfund balances as of June 30, 2011 between governmental funds and enterprise funds:

Receivable by	Payable by	Purpose	Amount
Governmental fund:	Enterprise fund:		
Other nonmajor funds (New Secure Housing Program)	GDB Operating Fund	Demand deposits and accrued interest	$ 270,014
HUD Programs	GDB Operating Fund	Demand deposits and accrued interest	241,573
Other nonmajor funds (AHMSP Act No. 124)	GDB Operating Fund	Investment agreements and accrued interest	564,063
Other nonmajor funds (AHMSP Act No. 124)	GDB Operating Fund	Demand deposits and accrued interest	674,611
Other nonmajor funds (AHMSP-Stage 7)	GDB Operating Fund	Demand deposits and and accrued interest	97,565
Other nonmajor funds (AHMSP-Stage 8)	GDB Operating Fund	Investment agreements and accrued interest	15,373,338
ARRA Funds	GDB Operating Fund	Demand deposits	276
Closing Costs Assistance Program	GDB Operating Fund	Demand deposits and accrued interest	827,797
My New Home Program	GDB Operating Fund	Demand deposits and accrued interest	3,084,709
Subtotal and balance carried forward			21,133,946

(Continued)

The summary of the interfund balances as of June 30, 2011 between government funds is as follows:

Receivable by	Payable by	Purpose	Amount
Balance brought forward			$ 21,133,946
Governmental fund:	Enterprise fund:		
Other nonmajor funds (New Secure Housing Program)	Housing Finance Authority	Reimbursement of expenditures	20,179
Other nonmajor funds (AHMSP Act. No. 124)	Housing Finance Authority	Reimbursement of expenditures	2,930
Sub total			23,109
Total			$ 21,157,055
Enterprise fund:	Governmental fund:		
GDB Operating Fund	Other nonmajor funds (New Secure Housing Program)	Loans payable and accrued interest	(52,684,188)
GDB Operating Fund	Other nonmajor funds (AHMSP-Stage 7)	Loans payable and accrued interest	(39,281,780)
GDB Operating Fund	Other nonmajor funds (AHMSP-Stage 10)	Loans payable and accrued interest	(13,646,644)
Housing Finance Authority	Other nonmajor funds (AHMSP-Stage 7)	Reimbursement of expenditures	(1,217,841)
Housing Finance Authority	Other nonmajor funds (New Secure Housing Program)	Reimbursement of expenditures	(54,117)
Housing Finance Authority	HUD Programs	Reimbursement of expenditures	(1,149,277)
Housing Finance Authority	My New Home Program	Reimbursement of expenditures	(40,119,127)
Housing Finance Authority	HOME Programs	Reimbursement of expenditures	(678,598)
Total			(148,831,572)
Total internal balances — net			$ (127,674,517)

(Continued)

The summary of interfund balances of June 30, 2011, among governmental funds, is as follows:

Receivable by	Payable by	Purpose	Amount
Governmental fund:	Governmental fund:		
Other nonmajor funds (Home Secured Program)	Other nonmajor funds (AHMSP Act No. 124)	Reimbursement of expenditures	$ 303,809

The summary of interfund balances of June 30, 2011, among enterprise funds, is as follows:

Receivable by	Payable by	Purpose	Amount
Enterprise funds:	Enterprise funds:		
Housing Finance Authority	GDB Operating Fund	Demand deposits and accrued interest	$ 8,241,502
Development Fund	GDB Operating Fund	Demand deposits and accrued interest	11,183,720
Tourism Development Fund	GDB Operating Fund	Demand deposits and accrued interest	21,886,826
Public Finance Corporation	GDB Operating Fund	Demand deposits and accrued interest	1,039,206
Other nonmajor (Education Assistance Corporation)	GDB Operating Fund	Demand deposits and accrued interest	2,381,351
Other nonmajor (JMB Institute)	GDB Operating Fund	Demand deposits and accrued interest	94,583
Housing Finance Authority	GDB Operating Fund	Certificates of deposit and accrued interest	396,767,044
Tourism Development Fund	GDB Operating Fund	Certificates of deposit and accrued interest	4,856,417
Housing Finance Authority	GDB Operating Fund	Guaranteed investment contracts and accrued interest	198,151,692
GDB Operating Fund	Housing Finance Authority	Bonds payable	163,127,098
GDB Operating Fund	Tourism Development Fund	Loans receivable and accrued interest	405,178,042
GDB Operating Fund	Housing Finance Authority	Loan receivable and accrued interest	2,733,900
Total balance among enterprise funds eliminated			$ 1,215,641,381

(Concluded)

The following table is a summary of interfund transfers for the year ended June 30, 2011:

Transfer Out	Transfer In	Transfer for	Amount
Governmental funds: Other nonmajor funds (AHMSP Stage 11)	Governmental funds: Other nonmajor funds (AHMSP Act No. 124)	Release of excess funds	$ 19,601,834
Other nonmajor funds (AHMSP Act No. 124)	Other nonmajor funds (Secured Your Home Program)	Contribution	20,000,000
Other nonmajor funds (AHMSP Stage 7)	Other nonmajor funds (AHMSP Act Stage 6)	Contribution	71
Enterprise Funds:	Governmental Funds:		
Housing Finance Authority	Other nonmajor funds (AHMSP Mortgage Backed Certificates)	Subsidy payments	741,042
Governmental funds: Other nonmajor funds (AHMSP Mortgage-backed certificates)	Enterprise funds: Housing Finance Authority	Debt service payments	305,231
Other nonmajor funds (AHSMP Stage 9)	Housing Finance Authority	Contribution	467,146
Other nonmajor funds (AHMSP-Stage 10)	Housing Finance Authority	Debt service payments	187,896
Other nonmajor funds (AHMSP- Stage 11)	Housing Finance Authority	Debt service payments	759
Enterprise funds: GDB Operating Fund	Enterprise funds: Other nonmajor funds (JMB Institute)	Contribution	178,000

22. FUND BALANCE DEFICIT

The following governmental funds reflect a deficit at June 30, 2011: My New Home Program, AHMSP Stage 7, AHMSP Stage 10, HOME Program and New Secure Housing Program for the amount of $30.8 million, $20.3 million, $8.8 million, $4.2 million and $55.8 million, respectively. The deficit of the My New Home Program, AHMSP Stage 7and AHMSP Stage 10 is due to the amounts borrowed by the Housing Finance Authority from the Bank that were used to provide housing subsidies. The deficit of the New Secure Housing Program is due to discontinued reimbursement of the Housing Finance Authority's allowable costs. The Housing Finance Authority expects to cover these deficits through contributions from the Commonwealth.

23. SUBSEQUENT EVENTS

Subsequent events were evaluated through December 1, 2011, the date the financial statements were available to be issued, to determine if any such events should either be recognized or disclosed in the 2011 financial statements.

On July 1, 2011, the Bank refunded $400 million of its then outstanding Senior Notes Series 2009 C and Series 2009 D.

GDB Senior Notes 2011 — On September 13, 2011, the Bank issued $450 million of Senior Notes, 2011 Series C. The Senior Notes, 2011 Series C mature on October 15, 2012 bearing fixed interest rate of 1.00%. Interest on the Senior Notes, 2011 Series C will be payable on maturity. The Bank used the proceeds to provide a loan to the Secretary of the Treasury of Puerto Rico for the purpose of managing intra-year cash flow needs of the Commonwealth during fiscal year 2012.

On October 5, 2011, the Bank issued $295 million of Senior Notes, 2011 Series D. The Senior Notes, 2011 Series D mature on November 8, 2012 bearing fixed interest rate of 1.00%. The Bank used the proceeds to provide a loan to the Secretary of the Treasury of Puerto Rico for the purpose of managing intra-year cash flow needs of the Commonwealth during fiscal year 2012.

On October 11, 2011, the Bank issued $150 million of Senior Notes, 2011 Series E. The Senior Notes, 2011 Series E mature on April 11, 2012 bearing fixed interest rate of 1.85%. Interest on the Senior Notes, 2011 Series E will be payable on a monthly basis. The Bank used the proceeds for general corporate purposes, including, but not limited to, increasing its investment portfolio, making loans and purchasing obligation of the Commonwealth and its public corporations, instrumentalities and municipalities.

On November 7, 2011, the Bank issued $400 million of Senior Notes, 2011 Series F. The Senior Notes, 2011 Series F mature on January 8, 2013 bearing fixed interest rate of 1.750%. Interest on the Senior Notes, 2011 Series F will be payable on maturity. The Bank used the proceeds for general corporate purposes, including, but not limited to, increasing its investment portfolio, making loans and purchasing obligation of the Commonwealth and its public corporations, instrumentalities and municipalities.

Housing Finance Authority

Special Obligation Notes, 2011 Series A — On October 4, 2011, the Housing Finance Authority issued $18 million of its Special Obligation Notes, 2011 Series A (the "2011 Notes") at an aggregate discounted price of $9,180,000. The 2011 Notes will be collateralized by certain second mortgages originated under the Home Purchase Stimulus Program and will be repaid from collections of principal and interest of the underlying collateral. The second mortgage loans will be guaranteed by the Housing Finance Authority's Act No. 87 insurance.

Restructuring of Mortgage Trust III, Collateralized Mortgage Obligations, Series A — In July 2011, the Housing Finance Authority restructured approximately $425 million face amount of Mortgage Trust III bonds and obtained $60 million of cash from the related collateral. The restructuring took place as follows: 1) tender offer amounting to approximately $144 million (including expenses related to the transaction) to acquire and cancel bonds with a carrying amount of approximately $112 million, and 2) purchase AAA securities amounting to approximately $160 million to establish an escrow for the payment through maturity of bonds with a carrying amount of approximately $129 million.

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GT GreenbergTraurig

[Closing Date]

Puerto Rico Infrastructure Financing Authority
San Juan, Puerto Rico

Re: $340,000,000 Puerto Rico Infrastructure Financing Authority Revenue Bonds (Ports Authority Project), Series 2011A (Federally Taxable) (the "Series A Bonds"), $192,830,000 Puerto Rico Infrastructure Financing Authority Revenue Bonds (Ports Authority Project), Series 2011B (Non-AMT) (the "Series B Bonds"), and $136,385,000 Puerto Rico Infrastructure Financing Authority Revenue Bonds (Ports Authority Project), Series 2011C (AMT) (the "Series C Bonds")

Gentlemen:

We have acted as bond counsel to the Puerto Rico Infrastructure Financing Authority (the "Authority") in connection with the issuance of the above-captioned Series A Bonds, Series B Bonds and Series C Bonds (collectively, the "Bonds"). In such capacity we have examined Act No. 44 of the Legislature of Puerto Rico, approved June 21, 1988, as amended (the "Act"), and such other law and such certified proceedings and other documents as we have deemed necessary to rending this opinion, including the Loan and Trust Agreement, dated as of December 1, 2011 (the "Trust Agreement"), by and among the Authority, the Puerto Rico Ports Authority (the "Borrower"), and The Bank of New York Mellon, as Trustee (the "Trustee"), and the resolution adopted by the Authority on October 19, 2011 authorizing the issuance of the Bonds (the "Resolution"). Terms used in this opinion and not otherwise defined herein have the same meanings assigned to them in the Trust Agreement.

The Bonds are issued pursuant to the Act, the Trust Agreement, and the Resolution. Pursuant to the Trust Agreement, the Authority is lending the proceeds of the Bonds to the Borrower for the purposes of financing and refinancing the Project (as defined in the Agreement.) Under the Trust Agreement, the Borrower has covenanted to make payments to the Authority to be used to pay when due the principal of and premium (if any) and interest on the Bonds, as well as other payments required under the Trust Agreement (collectively, the "Revenues"). Under the Trust Agreement, the Authority has pledged and assigned its rights in and to the Agreement and the Revenues (except certain rights to indemnification, reimbursements, and administrative fees) to the Trustee, as security for the Bonds. The Bonds are payable solely from the Revenues, including from drawings on a Letter of Credit issued by Government Development Bank for Puerto Rico to the Trustee, for the account of the Borrower.

We note that various issues concerning the legal existence of the Borrower, the power of the Borrower to carry out the Project and to enter into and perform its obligations under the Trust

Agreement, the authorization, execution and delivery of the Trust Agreement by the Borrower and the extent to which the Trust Agreement is binding upon the Borrower are addressed in an opinion of Greenberg Traurig, LLP, counsel to the Borrower, provided to the Authority, and we express no opinion herein with respect to those issues.

Regarding questions of fact material to our opinion, we have relied on representations of the Authority and the Borrower contained in the Trust Agreement, and the certified proceedings and other certifications of public officials and others furnished to us, including certifications furnished to us by or on behalf of the Borrower, without undertaking to verify the same by independent investigation.

Based on the foregoing, we are of opinion that, under existing law:

1. The Authority is validly existing as a public corporation and instrumentality of the Commonwealth of Puerto Rico with the power to enter into and perform its obligations under the Trust Agreement and to issue the Bonds.

2. The Trust Agreement has been duly authorized, executed, and delivered by the Authority, and is a valid and binding obligation of the Authority enforceable against the Authority in accordance with its terms. The Trust Agreement creates a valid lien on the Revenues and on the rights of the Authority to receive Revenues under the Trust Agreement (except certain rights to indemnification, reimbursements, and administrative fees).

3. The Bonds have been duly authorized and executed by the Authority, and are legal, valid and binding limited obligations of the Authority, payable solely from the Revenues.

4. Under the provisions of the Acts of Congress now in force and under existing regulations, rulings and court decisions, (i) interest on the Series B Bonds is excluded from gross income for federal income tax purposes, (ii) interest on the Series C Bonds is excluded from gross income for federal income tax purposes, except for interest on any Series C Bond for any period during which such Series C Bond is held by a "substantial user" of the facilities financed by the Series C Bonds, or a "related person" within the meaning of Section 147(a) of the Internal Revenue Code of 1986, as amended (the "Code"), (iii) interest on the Series A Bonds is not excluded from gross income for federal income tax purposes and so will be fully subject to federal income taxation, and (iv) the Bonds and the interest thereon are exempt from state, Commonwealth of Puerto Rico, and local income taxation.

Interest on the Series B Bonds will not be an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations; however such interest will be taken into account in determining adjusted current earnings for purposes of computing the alternative minimum tax imposed on certain corporations. Interest on the Series C Bonds is an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations. The Code contains other provisions that could result in tax consequences, upon which we express no opinion, as a result of (i) ownership of Bonds, or (ii) the inclusion in certain computations of interest that is excluded from gross income.

The opinion set forth in this paragraph 4 is subject to the condition that the Authority and the Borrower comply with all requirements of the Code that must be satisfied subsequent to the issuance of the Series B Bonds and the Series C Bonds (collectively, the "Tax-Exempt Bonds") in order that interest thereon be, and continue to be, excludable from the gross income of the owners thereof for federal income tax purposes. The Authority and the Borrower have covenanted to comply with all such requirements, to the extent permitted by the Constitution and laws of the Commonwealth of Puerto Rico, so that interest on the Tax-Exempt Bonds will remain exempt from federal income taxes to which they are not subject on the date of issuance of the Tax-Exempt Bonds. We are not aware of any provisions of the Constitution or laws of the Commonwealth of Puerto Rico which would prevent the Authority or the Borrower from complying with the requirements of the Code. Failure to comply with certain of such requirements may cause interest on the Tax-Exempt Bonds to be included in gross income for federal income tax purposes retroactively to the date of the issuance of the Tax-Exempt Bonds.

The rights of the owner of the Bonds and the enforceability of the Bonds and the Trust Agreement are limited by bankruptcy, insolvency, reorganization, moratorium, and other similar laws affecting creditors' rights generally, and by equitable principles, whether considered at law or in equity.

The opinions expressed herein are for the benefit of the addressee only and may not be quoted, circulated, assigned or delivered to any other person or for any other purpose without our prior written consent. The opinions expressed herein are based on an analysis of existing laws and court decisions on or prior to the date hereof. Such opinions may be adversely affected by actions taken or events occurring, including a change in law, regulation or ruling (or in the application or official interpretation of any law, regulation or ruling) after the date hereof. We have not undertaken to determine, or to inform any person, whether such actions are taken or such events occur, and we have no obligation to update this opinion in light of such actions or events.

Respectfully submitted,

Greenberg Traurig, LLP

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APPENDIX G

FERRAIUOLI LLC

[Closing Date]

Puerto Rico Infrastructure Financing Authority
San Juan, Puerto Rico

Re: $340,000,000 Puerto Rico Infrastructure Financing Authority Revenue Bonds (Ports Authority Project), Series 2011A (Federally Taxable) (the "Series A Bonds")

Ladies and Gentlemen:

We have acted as Special Tax Counsel to the Puerto Rico Infrastructure Financing Authority (the "Authority") in connection with the issuance of the above-captioned Series A Bonds (the "Bonds"). In such capacity we have examined Act No. 44 of the Legislature of Puerto Rico, approved June 21, 1988, as amended (the "Act"), and such other law and such certified proceedings and other documents as we have deemed necessary to provide this opinion, including the Loan and Trust Agreement, dated as of December 1, 2011 (the "Loan and Trust Agreement"), by and among the Authority, the Puerto Rico Ports Authority (the "Borrower"), and The Bank of New York Mellon, as Trustee (the "Trustee"), and the resolution adopted by the Authority on October 19, 2011 authorizing the issuance of the Bonds (the "Resolution"). Terms used in this opinion and not otherwise defined herein have the same meanings assigned to them in the Loan and Trust Agreement.

The Bonds are issued pursuant to the Act, the Loan and Trust Agreement, and the Resolution. Pursuant to the Loan and Trust Agreement, the Authority is lending the proceeds of the Bonds to the Borrower for the purposes of financing and refinancing the Project (as defined in the Loan and Trust Agreement). Under the Loan and Trust Agreement, the Borrower has covenanted to make payments to the Authority to be used to pay when due the principal of, premium (if any) and interest on the Bonds, as well as other payments required under the Loan and Trust Agreement (collectively, the "Revenues"). Under the Loan and Trust Agreement, the Authority has pledged and assigned its rights in and to the Loan and Trust Agreement and the Revenues (except certain rights to indemnification, reimbursements, and administrative fees) to the Trustee, as security for the Bonds. The Bonds are payable solely from the Revenues, including from drawings on a Letter of Credit issued by Government Development Bank for Puerto Rico to the Trustee, for the account of the Borrower.

We are not opining as to the legality, validity or enforceability of the Bonds. Accordingly, the following opinions are based on the assumption that the Bonds have been duly authorized and executed by the Authority, and are legal, valid and binding obligations of the Authority.

From such examination, and assumption and based on the provision of the laws of Puerto Rico and the United States as now in force, and having regard to legal questions we deem relevant, we are of the opinion that:

1. In accordance to Section 1031.02(a)(3)(B) of the Internal Revenue Code for a New Puerto Rico, Act No. 1 of the Legislature of Puerto Rico, approved January 31, 2011, as amended by Act 232 of December 11, 2011 (the PR Code"), and Article 20(b) of the Act, interest on the Bonds and any gain realized from the sale or exchange thereof is exempt from the income tax imposed by Sections 1021.02, 1022.01 and 1022.02 of the PR Code.

2. In accordance to Section 1022.04(b)(2) of the PR Code, interest on the Bonds is excluded from the "adjusted net book income" of a corporation for purposes of computing the alternative minimum tax imposed by Section 1022.03(a) of the PR Code.

3. In accordance to Section 1021.02(a)(2)(A)(i) of the PR Code, the "alternative basic tax taxable income" of an individual does not include interest on the Bonds for purposes of determining the Puerto Rico alternative basic tax imposed by Section 1021.02(a)(1) of the PR Code.

4. The Bonds will be considered an obligation of an instrumentality of the Government of Puerto Rico for purposes of: (i) the non-recognition of gain rules of Section 1034.04(f)(2)(A) of the PR Code applicable to certain involuntary conversions; and (ii) Section 1022.05(g) of the PR Code, which provides an exemption from the surtax imposed by Section 1022.05(a) of the PR Code for corporations that have a certain percentage of their net income invested in obligations of instrumentalities of the Government of Puerto Rico and certain other investments.

5. Interest on the Bonds is exempt from Puerto Rico municipal license taxes under Section 9(25) of the Puerto Rico Municipal License Tax Act of 1974, as amended.

6. The Bonds are exempt from Puerto Rico personal property tax pursuant to the Act, Section 3.11 of the Puerto Rico Municipal Property Tax Act of 1991, as amended, and Section 3 of the Puerto Rican Federal Relations Act.

7. The Bonds are exempt from Puerto Rico (i) gift tax with respect to donors who are residents of Puerto Rico at the time the gift is made and (ii) estate tax with respect to estates of decedents who are residents of Puerto Rico at the time of death and who acquired their United States citizenship solely by reason of birth or residence in Puerto Rico.

8. Interest on the Series 2011A Bonds constitutes "industrial development income" under Section 2(j) of the Puerto Rico Industrial Incentives Act of 1963, as amended, the Puerto Rico Industrial Incentives Act of 1978, as amended, the Puerto Rico Tax Incentives Act of 1987, as amended, and the Puerto Rico Tax Incentives Act of 1998 , as amended (collectively,

the “Acts”), when received by a holder of a grant of tax exemption issued under any of the Acts that acquired the Series 2011A Bonds with “eligible funds,” as such term is defined in the Acts.

The PR Code provides rules for “amortizable bond premium” that an owner of a Bond should refer to in the event that the amount payable at maturity or earliest redemption of the Bonds is less than such owner’s basis in the Bonds.

The PR Code does not contain any provisions regarding the treatment of the excess of a Bond’s redemption price at maturity over its initial issue price (original issue discount). Under the administrative practice followed by the Puerto Rico Treasury Department with respect to the repealed Puerto Rico Internal Revenue Code of 1994, as amended, original issue discount was treated as interest.

Prospective owners of the Bonds should be aware that, pursuant to Sections 1033.17(a)(5), 1033.17 (a)(10) and 1033.17(f) of the PR Code, ownership of the Bonds may, under certain circumstances, result in a disallowance, for Puerto Rico income tax purposes, of interest expense and other expenses related to an investment in the Bonds.

IRS Circular 230 Disclosure: The following tax discussion is not intended or written to be used, and cannot be used by any taxpayer, for purposes of avoiding penalties that may be imposed on a taxpayer by the Internal Revenue Service. This tax discussion was written in connection with the promotion or marketing of the Bonds. Each prospective purchaser of the Bonds should seek tax advice from an independent tax advisor based on its particular circumstances.

Based upon the provisions of the United States Internal Revenue Code of 1986, as amended (the “US Code”), now in force and the rules and regulations thereunder, it is our opinion that:

1. Interest or original issue discount on the Bonds owned by an individual is excludable from the gross income of the individual thereof for United States federal income tax purposes under Section 933 of the US Code if (a) the individual is a bona fide resident of Puerto Rico during the entire taxable year in which such interest or original discount is to be recognized for purposes of the US Code and (b) such interest or original issue discount is not, and is not treated as, income effectively connected with, or attributable to, the conduct of a trade or business within the United States by such individual under the US Code.

2. Interest or original issue discount on the Bonds derived by a corporation organized under the laws of Puerto Rico is not subject to United States federal income tax under the US Code if: (a) such interest or original issue discount is not, and is not treated as, income effectively connected with, or attributable to, the conduct of a trade or business in the United States by such corporation under the US Code; (b) such corporation is not a controlled foreign corporation or a passive foreign investment company under the US Code; and (c) such corporation is not treated as a domestic corporation for purposes of the US Code.

3. United States taxpayers, other than individuals who comply with the requirements set forth below, may be subject to federal income tax on any gain realized upon sale of the Bonds. Pursuant to Notice 89-40, issued by the United States Internal Revenue Service on March 27, 1989, and the regulations issued under Section 937 of the US Code, the gain from the sale of the Bonds by an individual that is not a resident of the United States under Section 865(g) of the US Code and who is a bona fide resident of Puerto Rico will constitute Puerto Rico source income, and therefore will qualify for exclusion from gross income under Section 933 of the US Code, provided (i) said Bonds do not constitute inventory in the hands of such seller, (ii) such gain is not attributable to an office or fixed place of business of the individual located outside Puerto Rico, and (iii) the individual has been a bona fide resident of Puerto Rico for the shorter of (1) the full period during which the individual has owned the Bonds or (2) each of the ten years preceding the year of the sale. In the case the individual is a bona fide resident of Puerto Rico for the tax year for which the source of income must be determined and the individual was a United States citizen or resident (other than a bona fide resident of Puerto Rico) for any of the ten years preceding said year, the individual may elect to treat as gain from sources within Puerto Rico the portion of the gain attributable to the individual's holding period in Puerto Rico.

Prospective owners of the Bonds should consult their tax advisors with respect to the precise determination of the Puerto Rico and United States federal tax consequences arising from ownership or disposition of the Bonds.

This opinion is limited to the above, and we do not express any other opinion regarding the Puerto Rico or United States federal tax consequences arising from ownership or disposition of the Bonds.

The opinions expressed herein are for the benefit of the addressee only and may not be quoted, circulated, assigned or delivered to any other person or for any other purpose without our prior written consent. The opinions expressed herein are based on an analysis of existing laws and court decisions on or prior to the date hereof. Such opinions may be adversely affected by actions taken or events occurring, including a change in law, regulation or ruling (or in the application or official interpretation of any law, regulation or ruling) after the date hereof. We have not undertaken to determine, or to inform any person, whether such actions are taken or such events occur, and we have no obligation to update this opinion in light of such actions or events.

Respectfully submitted,

Ferraiuoli LLC

APPENDIX H: Table of Discount Bonds and Premium Bonds

Table of Discount Bonds and Premium Bonds

	Series	2011B	2011B	2011B	2011B	2011B	2011B	2011B	2011B	2011B	2011B	2011B	2011B	2011B
	Maturity (12/15)	**2014**	**2015**	**2016**	**2017**	**2018**	**2021**	**2022**	**2022**	**2023**	**2024**	**2025**	**2026**	**2026**
	Coupon	4.000%	5.000%	3.000%	5.000%	4.000%	4.000%	4.250%	5.000%	4.500%	4.625%	5.000%	5.250%	6.000%
	Orig Yield	2.380%	2.760%	2.950%	3.170%	3.440%	4.060%	4.330%	4.33%*	4.49%*	4.700%	4.86%*	4.98%*	4.77%*
	Orig Price	104.608	108.355	100.228	109.872	103.440	99.510	99.306	105.374	100.077	99.276	101.093	102.098	109.662
Redemption Date and Price	6/15/2012	103.909	107.424	100.209	109.170	103.236	99.530	99.330	105.173	100.076	99.297	101.055	102.023	109.308
	12/15/2012	103.145	106.407	100.187	108.400	103.012	99.551	99.356	104.950	100.073	99.318	101.010	101.939	108.915
	6/15/2013	102.373	105.375	100.165	107.618	102.784	99.572	99.382	104.722	100.070	99.339	100.965	101.852	108.513
	12/15/2013	101.591	104.329	100.142	106.824	102.552	99.593	99.408	104.489	100.066	99.361	100.918	101.763	108.101
	6/15/2014	100.800	103.269	100.119	106.017	102.316	99.615	99.436	104.251	100.063	99.384	100.871	101.672	107.679
	12/15/2014	100.000	102.194	100.096	105.197	102.076	99.637	99.463	104.008	100.059	99.407	100.822	101.579	107.247

* Yield to December 15, 2021 optional redemption date at a redemption price of 100%.

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APPENDIX I

COMMONWEALTH OF PUERTO RICO
Financial Information and Operating Data Report
December 6, 2011

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COMMONWEALTH OF PUERTO RICO
Financial Information and Operating Data Report
December 6, 2011

INTRODUCTION

General

The financial and operating information about the Commonwealth of Puerto Rico (the "Commonwealth" or "Puerto Rico") included in this Report has been updated as of June 30, 2011, except as otherwise provided herein. The Commonwealth's fiscal year runs from July 1 through June 30 of the following year. References in this Report to a particular fiscal year are to the year in which such fiscal year ends.

Forward-Looking Statements

The information included in this Report contains certain "forward-looking" statements. These forward-looking statements may relate to the Commonwealth's fiscal and economic condition, economic performance, plans, and objectives. All statements contained herein that are not clearly historical in nature are forward-looking, and the words "anticipates," "believes," "continues," "expects," "estimates," "intends," "aims," "projects," and similar expressions, and future or conditional verbs such as "will," "would," "should," "could," "might," "can," "may," or similar expressions, are generally intended to identify forward-looking statements.

These statements are not guarantees of future performance and involve certain risks, uncertainties, estimates, and assumptions by the Commonwealth that are difficult to predict. The economic and financial condition of the Commonwealth is affected by various financial, social, economic, environmental, and political factors. These factors can be very complex, may vary from one fiscal year to the next, and are frequently the result of actions taken or not taken, not only by the Commonwealth and its agencies and instrumentalities, but also by entities such as the government of the United States of America or other nations that are not under the control of the Commonwealth. Because of the uncertainty and unpredictability of these factors, their impact cannot, as a practical matter, be included in the assumptions underlying the Commonwealth's projections.

The projections set forth in this Report were not prepared with a view toward complying with the guidelines established by the American Institute of Certified Public Accountants with respect to prospective financial information, but, in the view of the Commonwealth's responsible officers, were prepared on a reasonable basis, reflect the best currently available estimates and judgments, and present, to the best of such officers' knowledge and belief, the expected course of action and the expected future financial performance of the Commonwealth. However, this information is not fact and should not be relied upon as being necessarily indicative of future results, and readers of this Report are cautioned not to place undue reliance on the prospective financial information. Neither the Commonwealth's independent auditors, nor any other independent auditors, have compiled, examined, or performed any procedures with respect to the prospective financial information contained herein, nor have they expressed any opinion or any other form of assurance on such information or its achievability and disclaim any association with the prospective financial information. Neither the Commonwealth's independent auditors, nor any other independent auditors, have been consulted in connection with the preparation of the prospective financial information set forth in this Report, which is solely the product of the Commonwealth, and the independent auditors assume no responsibility for its content.

Overview of Economic and Fiscal Condition

Economic Condition

Puerto Rico's economy is currently in a recession that began in the fourth quarter of fiscal year 2006. Although Puerto Rico's economy is closely linked to the United States economy, in recent fiscal years the performance of the Puerto Rico economy has not been consistent with the performance of the United States economy. For fiscal years 2007, 2008, 2009 and 2010 Puerto Rico's real gross national product decreased by 1.2%, 2.9%, 4.0% and 3.8%, respectively, while the United States real gross domestic product grew at a rate of 1.8% and 2.7% during fiscal years 2007 and 2008, respectively, contracted during fiscal year 2009 at a rate of 3.0%, and grew by 0.9% in fiscal year 2010. According to the Puerto Rico Planning Board's (the "Planning Board") latest projections made in March 2011, which take into account the preliminary results for fiscal year 2010, the economic impact of the disbursement of funds from the American Recovery and Reinvestment Act of 2009 ("ARRA"), and other economic factors, it is projected that the real gross national product for fiscal year 2011 contracted by 1.0%. The real gross national product for fiscal year 2012, however, is forecasted to grow by 0.7%.

Fiscal Condition

Fiscal Imbalance. Since 2000, the Commonwealth has faced a number of fiscal challenges, including an imbalance between its General Fund total revenues and expenditures. The imbalance reached its highest level in fiscal year 2009, when the deficit was $3.306 billion, consisting of the difference between total revenues from non-financing sources of $7.583 billion and total expenditures of $10.890 billion. The following table shows total revenues from non-financing sources (which are revenues from taxes, licenses and other internal or external sources received by virtue of existing laws, but excluding proceeds from financings), total expenditures (including debt service payments) and the ensuing imbalance for the last three fiscal years. Total revenues from non-financing sources, as shown in the table, includes revenues from temporary revenue raising measures taken by the Commonwealth to address this fiscal imbalance, some of which are described in "Fiscal Stabilization and Economic Reconstruction" under THE ECONOMY below. Such temporary revenues should not be considered "recurring" revenues beyond the applicable period of such measures. Similarly, total expenditures, as shown in the table, includes expenditures of a non-recurring nature as a result of the implementation of various expense-reduction measures also described in "Fiscal Stabilization and Economic Reconstruction" under THE ECONOMY below. Accordingly, the amount of the Commonwealth's so called "structural deficit," or the difference between recurring government revenues and recurring expenditures, may differ from the amount of the deficit shown below. Depending on the assumptions made as to what should be considered "recurring" for purposes of this computation, such difference may be significant.

Deficit
Fiscal Years ended June 30,
(in millions)

	Total Revenues[1]	Total Expenditures	Deficit
2009	7,583	10,890	(3,306)
2010	7,593	10,369[3]	(2,775)
2011[2]	8,063	9,792[3]	(1,729)

(1) Excludes General Fund revenues attributable to the electronic and traditional lotteries in the amount of $126.7 million, $122.8 million and $101.9 million for fiscal years 2009, 2010 and 2011, respectively.

(2) Preliminary, unaudited numbers.

(3) Includes debt service of $677.4 million and $638.7 million for fiscal years 2010 and 2011, respectively, on the Commonwealth's general obligation bonds and guaranteed bonds of Public Buildings Authority that was refinanced through the issuance of refunding bonds.

Source: 2009-2010: Commonwealth of Puerto Rico Comprehensive Annual Financial Report — Statement of Revenues and Expenditures — Budget and Actual — Budget Basis — General Fund.
2011: Department of the Treasury.

Prior to fiscal year 2009, the Commonwealth bridged such deficit through the use of non-recurring measures, such as borrowing from Government Development Bank for Puerto Rico ("Government Development Bank" or "GDB" ") or in the bond market, postponing the payment of various government expenses, such as payments to suppliers and utilities providers, and other one time measures such as the use of derivatives and borrowings collateralized with government owned real estate and uncollected General Fund revenues.

In January 2009, the Government of Puerto Rico (the "Government") began to implement a multi-year plan designed to achieve fiscal balance, restore sustainable economic growth and safeguard the investment-grade ratings of the Commonwealth bonds. This plan included certain expense reduction measures that, together with various temporary and permanent revenue raising measures, have allowed the government to reduce the deficit. These measures are briefly discussed below and are discussed in greater detail in "Fiscal Stabilization and Economic Reconstruction" under THE ECONOMY.

As shown in the table above, during the last three fiscal years, the Commonwealth has been able to reduce the deficit by both increasing its revenues and reducing its expenditures. The Commonwealth's ability to continue reducing the deficit will depend in part on its ability to continue increasing revenues and reducing expenditures, which in turn depends on a number of factors, including improvements in general economic conditions.

Fiscal Stabilization Plan. The fiscal stabilization plan, which was generally contained in Act No. 7 of March 9, 2009, as amended ("Act 7"), sought to achieve budgetary balance, while addressing expected fiscal deficits in the intervening years through the implementation of a number of initiatives, including: (i) a gradual operating expense-reduction plan through reduction of operating expenses, including payroll, which is the main component of government expenditures, and the reorganization of the Executive Branch; (ii) a combination of temporary and permanent revenue raising measures, coupled with additional tax enforcement measures; and (iii) certain financial measures.

The Government estimates that the fiscal stabilization plan's operating expense reduction measures have resulted in annual savings of approximately $837 million, and that the tax revenue enforcement measures, and the temporary and permanent revenue raising measures have resulted in additional revenues of $420 million during fiscal year 2011.

The principal financial measure taken has been a bond issuance program through the Puerto Rico Sales Tax Financing Corporation ("COFINA" by its Spanish-language acronym), to which the Commonwealth allocated a portion of its sales and use tax. The proceeds from the COFINA bond issuance program (such proceeds are deposited in an account (referred to herein as the "Stabilization Fund") managed by GDB) have been used to repay existing government debt (including debts with GDB), finance government operating expenses for fiscal years 2008 through 2011 (and will be used in fiscal year 2012 to cover government expenses included in the government's annual budget for such fiscal year), including costs related to the implementation of a workforce reduction plan, and fund an economic stimulus plan, as described below. During fiscal years 2009 and 2010, COFINA issued approximately $5.6 billion and $3.6 billion, respectively, of revenue bonds payable from sales and use tax collections transferred to COFINA. During fiscal year 2012, COFINA expects to issue approximately $2 billion of revenue bonds payable from sales and use tax collections transferred to COFINA, the proceeds of which will be mainly used to finance a portion of the government's operating expenses for fiscal year 2012, refund outstanding debt obligations payable from Commonwealth appropriations, and refund certain outstanding COFINA bonds.

Another financial measure taken has been the restructuring of a portion of the debt service on the Commonwealth's general obligation bonds and on bonds of the Public Buildings Authority ("PBA") that are guaranteed by the Commonwealth and are payable from Commonwealth budget appropriations. During fiscal year 2010, the Commonwealth refinanced $512.9 million of interest accrued during such fiscal year on the Commonwealth's general obligation bonds and $164.5 million of interest accrued during such fiscal year on PBA bonds. During fiscal year 2011, the Commonwealth refinanced $490.9 million of interest accrued during such fiscal year and principal due on July 1, 2011 on the Commonwealth's general obligation bonds. During fiscal year 2011, PBA also used a line of credit from GDB to make payments of approximately $147.8 million of interest accrued during such fiscal year on its Commonwealth guaranteed bonds, which line of credit was refinanced with the proceeds of a series of Commonwealth guaranteed bonds issued by PBA.

During fiscal year 2012, the Government expects to refinance approximately $537.4 million of principal due in and interest to accrue during such fiscal year on the Commonwealth's general obligation bonds and approximately $153.8 million of interest to accrue during such fiscal year on Commonwealth guaranteed PBA bonds.

The fiscal stabilization plan is discussed in more detail in "Fiscal Stabilization and Economic Reconstruction" under THE ECONOMY.

Results for Fiscal Year 2009. General Fund total revenues for fiscal year 2009 were $7.583 billion (this amount excludes approximately $126.7 million of revenues attributable to the electronic and traditional lotteries, which for accounting purposes are included in the Commonwealth's audited financial statements as a separate fund from the General Fund), representing a decrease of $775.5 million, or 9.3%, from fiscal year 2008. Total expenditures for fiscal year 2009 were $10.890 billion (consisting of $9.927 billion of total expenditures and $962 million of other uses) representing an increase of approximately $1.402 billion, or 14.8%, from original budgeted expenditures and exceeded General Fund total revenues (excluding other financing sources) by $3.306 billion, or 43.6%.

During fiscal year 2009, the Government faced an aggregate cash shortfall of $1.153 billion that, when added to the General Fund deficit, represented approximately $4.459 billion in excess expenditures and cash shortfall. The difference between General Fund revenues and total expenditures for fiscal year 2009 was principally paid from proceeds of COFINA bond issues and the restructuring of the corpus account of the Puerto Rico Infrastructure Financing Authority ("PRIFA") pursuant to the fiscal stabilization plan. See "Fiscal Stabilization and Economic Reconstruction – Fiscal Stabilization Plan" under THE ECONOMY.

Results for Fiscal Year 2010. General Fund total revenues for fiscal year 2010 were $7.593 billion (this amount excludes approximately $122.8 million of revenues attributable to the electronic and traditional lotteries, which for accounting purposes are included in the Commonwealth's audited financial statements as a separate fund from the General Fund), representing an increase of $9.8 million from fiscal year 2009 revenues. The principal changes in sources of revenues from fiscal year 2009 included a decrease in the sales and use tax received by the General Fund of $256.8 million due to the assignment to COFINA of an additional 1.75% of the 5.5% Commonwealth sales and use tax. This decrease in the amount of sales and use taxes allocated to the General Fund was fully offset, however, by increases in property taxes and excise taxes on cigarettes and alcoholic beverages of approximately $227.8 million and $60.5 million, respectively, as a result of the temporary and permanent revenue raising measures implemented as part of the Commonwealth's fiscal stabilization plan. Revenues from income taxes for fiscal year 2010 were approximately the same as in fiscal year 2009, reflecting the continuing impact of the ongoing economic recession.

Total expenditures for fiscal year 2010 were $10.369 billion (which included $173 million of expenditures related to a Government local stimulus program described below in "Fiscal Stabilization and Economic Reconstruction – Economic Reconstruction Plan" under THE ECONOMY), consisting of (i) $9.640 billion of total expenditures and (ii) $728 million of other financing uses. Total expenditures of $10.369 billion exceeded General Fund total revenues (excluding other financing sources) by $2.775 billion, or 36.6%. Excluding the debt service amounts that were refinanced, total expenditures for fiscal year 2010 were approximately $9.691 billion and exceeded General Fund total revenues (excluding other financing sources) by $2.098 billion, or 27.6%. The difference between revenues and expenses for fiscal year 2010 was covered principally by proceeds from a COFINA bond issue.

Preliminary Results for Fiscal Year 2011. Preliminary General Fund total revenues for fiscal year 2011 (from July 1, 2010 to June 30, 2011) were $8.165 billion (this amount includes approximately $101.9 million of revenues attributable to the electronic and traditional lotteries), an increase of $449.3 million, or 5.8%, from $7.716 billion of total revenues for the same period in the prior fiscal year (this amount includes approximately $122.8 million of revenues attributable to the electronic and traditional lotteries), and an increase of $31 million from the revised estimate of total revenues, which took into account the effect of the tax reform discussed below under "Tax Reform."

The increase in General Fund total revenues is mainly due to an increase of $170.1 million in tax withholdings from non-residents and the collection of $677.8 million as a result of the new temporary excise tax and the expansion of the taxation of certain foreign persons adopted as Act No. 154 of October 25, 2010, as amended ("Act 154") as part of the tax reform (discussed below under "Tax Reform"). This increase was partially offset by a decrease of $407 million and $18.5 million in collections from income tax on individuals and entertainment machine licenses, respectively. The decrease in individual income taxes is due to the tax relief provided to individual taxpayers as part of the tax reform and to current economic conditions. The Government had expected that the decrease in General Fund net revenues as a result of the tax relief provided to taxpayers as part of the tax reform would be offset by the temporary excise tax imposed on certain foreign persons by Act 154. For fiscal year 2011, the first five monthly excise tax payments (from February through June 2011) amounted to $677.6 million, which was consistent with the Government's projection of collections from the excise tax. The Government's expectations with respect to the impact of the tax reform on fiscal year 2011 revenues were met.

Preliminary General Fund total expenses for fiscal year 2011 amounted to $9.153 billion, which excludes $638.7 million of debt service amounts that were refinanced, and exceeded General Fund total revenues (excluding other financing sources) by $988 million, or 12.1%. The difference between preliminary revenues and expenses for fiscal year 2011 was covered principally by proceeds from a COFINA bond issue and proceeds of bonds issued to refinance debt service payments.

Budget for Fiscal Year 2012. On July 1, 2011, the Governor signed the Commonwealth's central government budget for fiscal year 2012. The adopted budget provides for General Fund total revenues of $9.260 billion. The budgeted General Fund revenue of $9.260 billion includes estimated revenues of $8.650 billion and $610.0 million in additional revenues from proceeds of COFINA bond issues.

The principal changes in General Fund revenues under the fiscal year 2012 budget compared to the fiscal year 2011 budget are accounted for mainly by the projected collections from the new temporary excise tax under Act 154 (up $969.0 million), sales and use taxes (up $125.0 million), non-resident withholding taxes (up $29 million), alcoholic beverage taxes (up $9.0 million), and projected decreases in excise taxes on motor vehicles and accessories (down $8.0 million), corporate income tax (down $51.0 million), federal excise taxes on offshore shipments (down $66.0 million), property taxes (down $162 million) and personal income taxes (down $239.0 million).

The fiscal year 2012 budget provides for total expenditures of $9.260 billion, consisting of General Fund expenditures of $8.650 billion and additional expenditures of $610 million that are expected to be covered from proceeds of COFINA bond issues. The fiscal year 2012 budgeted expenditures exclude certain debt service payments on the Commonwealth's general obligation bonds and Commonwealth guaranteed PBA bonds which are expected to be refinanced during fiscal year 2012. See "Fiscal Stabilization Plan" above. The budgeted total expenditures for fiscal year 2012 are $110 million, or 1.2%, higher than budgeted total expenditures of $9.150 billion for fiscal year 2011, and $1.109 billion, or 10.7%, lower than total expenditures of $10.369 billion for fiscal year 2010.

The principal changes in General Fund expenditures by program in the fiscal year 2012 budget compared to the fiscal year 2011 budget are mainly due to increases in public safety and protection (up $80.1 million), education (up $131.4 million), economic development (up $106.4 million), transportation (up $10.2 million), special pension contributions (up $85.8 million), contribution to municipalities (up $28.5 million), and decreases in general obligation bonds debt service (down $21.5 million), welfare (down $22.0 million), health (down $209.2 million), and governmental management (down $51.2 million).

Budgeted expenditures and capital improvements for the central government of all budgetary funds total $15.9 billion, a decrease of $142.9 million from fiscal year 2011 budgeted appropriations.

Preliminary Results for the First Three Months of Fiscal Year 2012 and Projected Fiscal Year 2012 Deficit. Preliminary General Fund revenues for the first three months of fiscal year 2012 (from July 1, 2011 to September 30, 2011) were $1.696 billion, an increase of $129.3 million, or 8.25%, from $1.567 billion of revenues for the same period in the prior fiscal year and a decrease of $33.3 million, or 1.9%, from the revised estimate of revenues of $1.729 billion made in September 2011. The increase in General Fund revenues for the first three months of fiscal year 2012, compared to the same period in the prior fiscal year, is mainly due to the collections of $478 million from the new temporary excise tax under Act 154, which was not in effect during the first three months of fiscal year 2011. This increase was partially offset by a decrease in collections from individual and corporate income taxes of $115 million and $75 million, respectively.

Preliminary General Fund total expenses (on a cash basis) for the first three months of fiscal year 2012 amounted to $1.858 billion, which is $13.5 million, or 1%, lower than $1.872 billion of budgeted expenditures for the same period. The lower expenditures are mainly due to timing differences in disbursements for general government expenditures of $29.4 million, safety and protection of $6.3 million and welfare of $4.5 million. These lower expenditures were partially offset by increased expenditures in health of $26 million and transportation and communication of $2.4 million. The difference between preliminary revenues and expenditures for the first three months of fiscal year 2012 was covered principally by funds on deposit in the Stabilization Fund and the issuance of tax revenue anticipation notes by the Commonwealth.

The deficit for fiscal year 2012 is projected to be approximately $610 million, which excludes approximately $691.2 million of debt service payments on Commonwealth general obligation bonds and Commonwealth guaranteed PBA bonds that will be refinanced. In addition, the Office of Management and Budget ("OMB") has indicated that the sectors of health and safety carry risk of budget overruns for fiscal year 2012 as they are undergoing operational changes that were not considered during the preparation of the budget for that fiscal year.

Unfunded Pension and Non-Pension Post-Employment Benefit Obligations and Funding Shortfalls of the Retirement Systems.

One of the challenges every administration has faced during the past 20 years is how to address the growing unfunded pension benefit obligations and funding shortfalls of the three Government retirement systems (the Employees Retirement System, the Teachers Retirement System and the Judiciary Retirement System) that are funded principally with budget appropriations from the Commonwealth's General Fund. As of June 30, 2010, the date of the latest actuarial valuations of the retirement systems, the unfunded actuarial accrued liability (including basic and system administered benefits) for the Employees Retirement System, the Teachers Retirement System and the Judiciary Retirement System was $17.8 billion, $7.1 billion and $283 million, respectively, and the funded ratios were 8.5%, 23.9% and 16.4%, respectively.

Based on current employer and member contributions to the retirement systems, the unfunded actuarial accrued liability will continue to increase significantly, with a corresponding decrease in the funded ratio, since the annual contributions are not sufficient to fund pension benefits, and thus, are also insufficient to amortize the unfunded actuarial accrued liability. Because annual benefit payments and administrative expenses of the retirement systems have been significantly larger than annual employer and member contributions, the retirement systems have been forced to use investment income, borrowings and sale of investment portfolio assets to cover funding shortfalls. The funding shortfall (basic system benefits, administrative expenses and debt service in excess of contributions) for fiscal year 2011 for the Employees Retirement System, the Teachers Retirement System and the Judiciary Retirement System was approximately $693 million, $268 million and $6.5 million, respectively. For fiscal year 2012, the funding shortfall is expected to be $741 million, $287 million and $8.5 million, respectively. As a result, the assets of the retirement systems are expected to continue to decline.

Based on the assumptions used in the latest actuarial valuations, including the expected continued funding shortfalls: (i) the Employees Retirement System, the largest of the three retirement systems, would deplete its net assets (total assets less liabilities, including the principal amount of certain pension obligation bonds) by fiscal year 2014 and its gross assets by fiscal year 2019; (ii) the Teachers Retirement System would deplete its net and gross assets by fiscal year 2020; and (iii) the Judiciary Retirement System would deplete its net and gross assets by fiscal year 2018. The estimated years for depletion of the assets could vary depending on how actual results differ from the assumptions used in the actuarial valuations, as well as based on any future changes to the contribution and benefits structures of the retirement systems. As a result of the increases in employer contributions to the Employees Retirement System and the Teachers Retirement System adopted in July 2011, as described below, the Administrator of the Retirement Systems projects that the period before depletion of the assets of these two systems will be extended by three to four years.

Since the Commonwealth and other participating employers are ultimately responsible for any funding deficiency in the three retirement systems, the depletion of the assets available to cover retirement benefits will require the Commonwealth and other participating employers to cover annual funding deficiencies. It is estimated that the Commonwealth would be responsible for approximately 74% of the combined annual funding deficiency of the three retirement systems, with the balance being the responsibility of the municipalities and participating public corporations.

The Commonwealth also provides non-pension post-employment benefits that consist of a medical insurance plan contribution. These benefits, which amounted to $114.2 million for fiscal year 2010 and $123.4 million for fiscal year 2011, are funded on a pay-as-you-go basis from the General Fund and are valued using actuarial principles similar to the way that pension benefits are calculated. Based on the latest actuarial valuations, as of June 30, 2010, the aggregate unfunded actuarial accrued liability of these benefits for the three retirement systems was $2.3 billion.

Because of its multi-year fiscal imbalances previously mentioned, the Commonwealth has been unable and is currently unable to make the actuarially recommended contributions to the retirement systems. If the Commonwealth fails to take action in the short-term to address the retirement systems' funding deficiency, the continued use of investment assets to pay benefits as a result of funding shortfalls and the resulting depletion of assets could adversely affect the ability of the retirement systems to meet the rates of return assumed in the actuarial valuations, which could in turn result in an earlier depletion of the retirement systems' assets and a significant increase in the unfunded actuarial accrued liability. Ultimately, since the Commonwealth's General Fund is required to cover a significant amount of the funding deficiency, the Commonwealth would have difficulty funding the annual required contributions unless it implements significant reforms to the retirement systems, obtains additional revenues, or takes other budgetary measures. For more information regarding the retirement systems, see RETIREMENT SYSTEMS.

In order to address the growing unfunded pension and non-pension benefit obligations and funding shortfalls of the three Government retirement systems, in February 2010, the Governor established a special commission to make recommendations for improving the financial solvency of the retirement systems. The special commission submitted a report to the Governor on October 21, 2010.

As a result of the special commission's report and the Government's analysis, the Governor submitted two bills to the Legislative Assembly to address in part the retirement systems' financial condition. One of such bills was enacted as Act No. 96 of June 16, 2011 ("Act 96"). On June 23, 2011, in accordance with Act 96, $162.5 million of funds on deposit in the Corpus Account of the Puerto Rico Infrastructure Development Fund (the "Corpus Account")"), which is under the custody and control of the Puerto Rico Infrastructure Financing Authority ("PRIFA")(see "Infrastructure Financing Authority" under PUBLIC CORPORATIONS for a description of the Corpus Account), were contributed to the Employees Retirement System and invested in capital appreciation bonds issued by COFINA maturing annually on August 1, 2043 through 2048 and accreting interest at a rate of 7%. The principal amount of the COFINA bonds will grow to an aggregate amount of approximately $1.65 billion at their maturity dates.

The second bill submitted by the Governor was enacted as Act No. 114 of July 5, 2011 ("Act 114") and Act No. 116 of July 6, 2011 ("Act 116"). These Acts provide an increase in employer contributions to the Employee Retirement System and the Teachers Retirement System of 1% of covered payroll in each of the next five fiscal years and by 1.25% of covered payroll in each of the following five fiscal years. As a result of these increases, the Employee Retirement System and the Teachers Retirement System would receive approximately $36 million and $14 million, respectively, in additional employer contributions during fiscal year 2012, and the additional employer contributions are projected to increase gradually each fiscal year (by an average aggregate increase of $71 million per fiscal year) to approximately $494 million and $195 million, respectively, by fiscal year 2021. The additional employer contributions for fiscal year 2012 have been included in the approved budget for such fiscal year. With respect to the increases in the employer contributions corresponding to the municipalities, Act 116 provides that the increases for fiscal years 2012, 2013 and 2014 will be paid for by the Commonwealth from the General Fund budget, representing approximately $6.3 million, $12.8 million and $19.7 million in fiscal years 2012, 2013 and 2014, respectively.

In addition to these measures, on August 8, 2011, the Board of Trustees of the Employees Retirement System adopted a new regulation regarding the rules relating to the concession of personal loans to its members, which, among other changes, lowers the maximum amount of those loans from $15,000 to $5,000. This change is expected to improve gradually the Employees Retirement System's liquidity.

Economic Reconstruction Plan

In fiscal year 2009, the Government began to implement a short-term economic reconstruction plan. The cornerstone of this plan was the implementation of federal and local economic stimulus programs. The Commonwealth was awarded approximately $6.8 billion in stimulus funds under the ARRA program, which was enacted by the U.S. government to stimulate the U.S. economy in the wake of the global economic downturn. Approximately $3.3 billion of the ARRA funds is allocated for consumer and taxpayer relief and the remainder will be used to expand unemployment and other social welfare benefits, and spending in education, healthcare and infrastructure, among others. As of October 14, 2011, the Commonwealth had disbursed $5.5 billion in ARRA funds, or 78.8%, of awarded funds.

The Government has complemented the federal stimulus package with additional short and medium-term supplemental stimulus measures that seek to address local economic challenges and provide investment in strategic areas. These measures included a local $500 million economic stimulus plan to supplement the federal plan.

Economic Development Plan

The Government has also developed the Strategic Model for a New Economy, which is a comprehensive long-term economic development plan aimed at improving Puerto Rico's overall competitiveness and business environment and increasing private-sector participation in the Puerto Rico economy. As part of this plan, the Government enacted Act No. 161 of December 1, 2009, which overhauled the permitting and licensing process in Puerto Rico in order to provide for a leaner and more efficient process that fosters economic development. The Government also enacted Acts No. 82 and 83 of July 19, 2010, which provided a new energy policy that seeks to lower energy costs and reduce energy-price volatility by reducing Puerto Rico's dependence on fuel oil and the promotion of diverse, renewable-energy technologies. Moreover, the

Government adopted a comprehensive tax reform (described below) that takes into account the Commonwealth's current financial situation. See "Tax Reform" below.

In addition, to further stimulate economic development and cope with the fiscal crisis, on June 8, 2009, the Legislative Assembly approved Act No. 29 establishing a clear public policy and legal framework for the establishment of public-private partnerships ("PPP") to finance and develop infrastructure projects and operate and manage certain public assets. During fiscal year 2010, the Government engaged various financial advisors to assist it in the evaluation and procurement of various projects in the energy, transportation, water and public school infrastructure sectors. During the fourth quarter of fiscal year 2010, the Government published desirability studies for four public-private partnership priority projects and commenced procurement for such projects. As of September 30, 2011, the Government had completed the concession of toll roads PR-22 and PR-5 and had short-listed proponents for the procurement process leading to the award of an administrative concession of the Luis Muñoz Marín International Airport and school infrastructure projects.

The Government has also identified strategic initiatives to promote economic growth in various sectors of the economy where the Commonwealth has competitive advantages and several strategic/regional projects aimed at fostering balanced economic development throughout the Island. These projects, some of which are ongoing, include tourism and urban redevelopment projects.

The fiscal stabilization plan, the economic reconstruction plan, and the long-term economic development plan are described in further detail below in "Fiscal Stabilization and Economic Reconstruction" under THE ECONOMY.

Tax Reform

In February 2010, the Governor established a committee to review the Commonwealth's income tax system and propose a comprehensive tax reform directed at promoting economic growth and job creation within the framework of preserving the administration's path towards achieving fiscal stability. The committee presented its findings to the Governor and, on October 25, 2010, the Governor announced that he was submitting to the Legislative Assembly various bills in order to implement the tax reform.

The tax reform was intended to be revenue positive. It consisted of two phases focused on providing tax relief to individuals and corporations, promoting economic development and job creation, simplifying the tax system and reducing tax evasion through enhanced tax compliance measures. The first phase, enacted as Act No. 171 of November 15, 2010, was expected to provide individual and corporate taxpayers with aggregate savings of $309 million for taxable year 2010. The second phase, enacted as Act No. 1 of January 31, 2011 ("Act 1 of 2011"), was projected to provide individual and corporate taxpayers aggregate annual average savings of $1.2 billion for the next six taxable years, commencing in taxable year 2011. Consistent with the objective of maintaining the path towards fiscal stability, the tax relief provisions applicable to individuals and corporations for taxable years 2014 through 2016 become effective only if (i) OMB certifies that the administration's expense control target has been met, (ii) the Treasury Department certifies that the General Fund revenue target has been met and (iii) the Planning Board certifies a year-over-year target increase in gross domestic product. See "Major Sources of General Fund Revenues—Tax Reform" under PUERTO RICO TAXES, OTHER REVENUES AND EXPENDITURES for a summary of the principal provisions of the tax reform.

As part of structuring the tax reform, the Government utilized a group of economic consultants to project its impact on tax revenues through the use of dynamic economic models adjusted to the Commonwealth's specific economic conditions. The Government also conducted its own internal analyses of such impact. Based on these analyses, the Government expects that the reduction in income tax revenues resulting from the implementation of the tax reform should be fully offset by the additional revenues produced by (i) enhanced tax compliance measures, (ii) the elimination of certain incentives and tax credits, (iii) a new temporary excise tax imposed on a controlled group member's acquisition from another group member of certain personal property manufactured or produced in Puerto Rico and certain services performed in Puerto Rico (at a declining rate from 4% for 2011 to 1% for 2016), and (iv) an expansion of taxation rules that characterize certain income of non-resident corporations, partnerships and individuals as effectively connected with the conduct of a trade or business in Puerto Rico and therefore subject to Puerto Rico income tax. The temporary excise tax and the expansion of the taxation of certain foreign persons were adopted by Act 154. In circumstances in which the temporary excise tax applies, the expansion of the taxation of nonresident individuals, foreign corporations and foreign partnerships does not apply. The other revenue enhancement measures, which are part of the second phase of the tax reform, are included in Act 1 of 2011. On December 29, 2010, the Treasury Department adopted regulations that provide certain tax credits against the temporary excise tax that lessen its impact on affected taxpayers subject to the temporary excise tax. These regulations became effective on January 1, 2011. The regulations address implementation and interpretation issues and include provisions regarding certain applicable credits against the tax subject to maintaining a baseline employment and other conditions. The Government estimates that this excise tax will affect foreign corporations or partnerships that are principally engaged in the manufacturing of pharmaceuticals and electronics. The Government expects to raise approximately $1.4 billion from the excise tax during the first year of implementation of Act 154 and $5.6 billion for the six-year period that the excise tax is in place.

The first monthly excise tax payment was due in February 2011. The collections for the first nine monthly excise tax payments (from February through October 2011) were $1.325 billion. These amounts are consistent with the Government's projection of collections from the excise tax.

Based on its analysis, the Government believes that the revenue projections from the taxes imposed by Act 154 are reasonable. However, since such taxes only became effective on January 1, 2011, there can be no assurance that the revenues therefrom, together with the other revenue enhancement measures included in the tax reform, will be sufficient to fully offset the reduction in income tax revenues expected from other aspects of the tax reform.

In connection with the expansion of the taxation of foreign persons by Act 154, the Government obtained a legal opinion regarding the creditability of the excise tax for U.S. federal income tax purposes. The opinion concludes that this excise tax should be creditable against U.S. federal income tax. That conclusion was based in part upon a determination that the expansion of the taxation of foreign persons and the imposition of the excise tax more likely than not satisfy the constitutional requirements of due process and the Commerce Clause of the United States Constitution, for reasons discussed therein. It is the position of the Government that the excise tax is a tax imposed in substitution of the generally imposed income tax and that, as such, under Section 903 of the United States Internal Revenue Code of 1986, as amended, U.S. taxpayers can claim a foreign tax credit for amounts paid.

On March 30, 2011, the United States Internal Revenue Service (the "IRS") issued Notice 2011-29 addressing the creditability of the new excise tax imposed by Act 154. Notice 2011-29 provides that the provisions of the new Puerto Rico excise tax are novel and the determination of its creditability requires the resolution of a number of legal and factual issues. Pending the resolution of those issues, the IRS will not challenge a taxpayer's position that the excise tax is a tax in lieu of an income tax under Section 903. The IRS also provided that any change in the foregoing tax credit treatment of the excise tax after resolution of the pending issues will be prospective and will apply to excise tax paid or accrued after the date that further guidance is issued.

Act 154 has not been challenged in court. Consequently, no court has passed on the constitutionality of Act 154. There can be no assurance that its constitutionality will not be challenged and that, if challenged, the courts will uphold Act 154. To the extent a court determines that the imposition of the excise tax or the expansion of the income tax or both are unconstitutional, the Government's revenues may be materially adversely affected.

For a summary of the principal provisions of the tax reform, the expansion of the income tax source rules to certain nonresident alien individuals, foreign corporations and foreign partnerships, and the new temporary excise tax, see "Major Sources of General Fund Revenues — Tax Reform" and "Major Sources of General Fund Revenues — Income Taxes," respectively, under PUERTO RICO TAXES, OTHER REVENUES AND EXPENDITURES.

Ratings of Commonwealth General Obligation Bonds

On August 8, 2011, Moody's Investors Service ("Moody's") lowered its rating on the Commonwealth unenhanced general obligation bonds to "Baa1" with a negative outlook from "A3". This rating action was a result of Moody's review of the Commonwealth's rating, which had been placed on watchlist on May 3, 2011. In taking this rating action, Moody's stated the downgrade reflects the continued financial deterioration of the severely underfunded retirement systems, continued weak economic trend, and weak finances, with a historical trend of funding budget gaps with borrowings. Moody's negative outlook reflects the stress the Commonwealth will face in the next few years as it continues to address the underfunding of the retirement systems from an already weak financial and economic position. On April 19, 2010, Moody's had rated the Commonwealth's unenhanced general obligation debt "A3," which was three gradations above the previous "Baa3" rating, as a result of its recalibration of certain U.S. municipal bond issues and issuers.

On August 8, 2011, Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc. ("S&P"), reaffirmed its "BBB" rating of the Commonwealth's unenhanced general obligation bonds. On March 7, 2011, S&P had raised its rating on the Commonwealth's unenhanced general obligation bonds to "BBB" with a stable outlook from "BBB–" with a positive outlook. In taking this rating action, S&P stated the upgrade reflects the Commonwealth's recent revenue performance and continued efforts to achieve fiscal and budgetary balance. S&P noted, however, that other medium-term budget pressures, such as the Commonwealth's retirement benefit obligations, remain a limiting credit factor. S&P's stable outlook is based on the Commonwealth's recent implementation of significant expenditure controls and revenue enhancement measures that could help restore balance within the next two years. S&P also stated that it would raise the rating if over the upcoming two years, in conjunction with an improvement in the Commonwealth's economic performance, budget controls remain in place and there is continued progress toward achieving balance between ongoing revenues and expenditures as well as in addressing the Commonwealth's unfunded retirement benefit obligations.

On January 19, 2011, Fitch, Inc. ("Fitch") assigned a "BBB+" rating to the Commonwealth's general obligation and appropriation debt with a stable outlook. In assigning the rating, Fitch stated that, while it recognized the Commonwealth's historic budget deficits, overestimation of revenues, reliance on borrowings to meet budgetary gaps, and the low level of pension funding, the successful implementation of the dramatic steps taken by the government to restructure fiscal operations and stimulate the economy was a positive credit factor.

Geographic Location and Demographic Trends

Puerto Rico, the fourth largest of the Caribbean islands, is located approximately 1,600 miles southeast of New York City. It is approximately 100 miles long and 35 miles wide.

According to the United States Census Bureau, the population of Puerto Rico was 3,725,789 in 2010, compared to 3,808,610 in 2000. The population of San Juan, the island's capital and largest city, was 381,931 in 2010 compared to 434,374 in 2000.

Relationship with the United States

Puerto Rico's constitutional status is that of a territory of the United States, and, pursuant to the territorial clause of the U.S. Constitution, the ultimate source of power over Puerto Rico is the U.S. Congress.

Puerto Rico came under United States sovereignty pursuant to the Treaty of Paris, signed on December 10, 1898, which ended the Spanish-American War. Puerto Ricans have been citizens of the United States since 1917. In 1950, after a long evolution toward greater self-government, Congress enacted Public Law 600, which provided that the existing political, economic and fiscal relationship between Puerto Rico and the United States would remain the same, but Puerto Rico would be authorized to draft and approve its own Constitution, guaranteeing a republican form of government. The Constitution was drafted by a popularly elected constitutional convention, approved in a special referendum by the people of Puerto Rico, amended and ratified by the U.S. Congress, and subsequently approved by the President of the United States.

The Commonwealth exercises virtually the same control over its internal affairs as do the 50 states. It differs from the states, however, in its relationship with the federal government.

The people of Puerto Rico are citizens of the United States but do not vote in national elections. They are represented in Congress by a Resident Commissioner that has a voice in the House of Representatives but no vote (except in House committees and sub-committees to which he belongs). Most federal taxes, except those such as Social Security taxes, are not levied in Puerto Rico. No federal income tax is collected from Puerto Rico residents on income earned in Puerto Rico, except for certain federal employees who are subject to taxes on their salaries. Income earned by Puerto Rico residents from sources outside of Puerto Rico, however, is subject to federal income tax.

The official languages of Puerto Rico are Spanish and English.

Governmental Structure

The Constitution of Puerto Rico provides for the separation of powers of the executive, legislative, and judicial branches of government. The Governor is elected every four years. The Legislative Assembly consists of a Senate and a House of Representatives, the members of which are elected for four-year terms. The highest court within the local jurisdiction is the Supreme Court of Puerto Rico. Decisions of the Supreme Court of Puerto Rico may be appealed to the Supreme Court of the United States under the same conditions as decisions from state courts. Puerto Rico constitutes a District in the federal judiciary and has its own United States District Court. Decisions of this court may be appealed to the United States Court of Appeals for the First Circuit and from there to the Supreme Court of the United States.

Governmental responsibilities assumed by the central government of the Commonwealth are similar in nature to those of the various state governments. In addition, the central government assumes responsibility for local police and fire protection, education, public health and welfare programs, and economic development.

Principal Officers Responsible for Fiscal Matters

Luis G. Fortuño was sworn in as Governor of Puerto Rico on January 2, 2009. From 2005 until becoming Governor, Mr. Fortuño was Puerto Rico's elected Resident Commissioner in the U.S. House of Representatives. Mr. Fortuño was an attorney in private practice from 1985 to 1993, and again from 1997 to 2003. Mr. Fortuño was the Executive Director of the Tourism Company from 1993 to 1996. From 1994 to 1996, Mr. Fortuño served as the first Secretary of the Department of Economic Development and Commerce. Mr. Fortuño holds a Bachelor's Degree from the Edmund A. Walsh School of Foreign Service at Georgetown University and a Juris Doctor from the University of Virginia School of Law.

Jesús F. Méndez was designated Secretary of the Department of the Treasury (the "Treasury Department") on January 7, 2011 and confirmed by the Senate of Puerto Rico on January 24, 2011. Prior to his appointment, Mr. Méndez served as Executive Vice President and Director of Administration, Operation and Controllership of GDB and as Executive Director of PBA. From 2005 to 2008, Mr. Méndez held the position of President and Chief Executive Officer of Tresamici Management, Inc., a closely held corporation dedicated to the administration of assisted living facilities. From 1996 to 2004, he held several senior management positions within Banco Santander S.A. operating entities in Puerto Rico, including

President of Santander Asset Management and First Senior Vice President and Trust Officer of Banco Santander Puerto Rico and Managing Director of Santander Securities Corporation. Prior to joining Santander Securities, Mr. Méndez served as Chief Financial Officer and Managing Director of BP Capital Markets. He also worked for Credit Suisse First Boston (Puerto Rico, Inc.) as Vice President and Deloitte & Touche as Senior Auditor. In addition, Mr. Méndez also held the position of Assistant Bank Examiner at the Federal Deposit Insurance Corporation in New York City. Mr. Méndez has a Bachelor's Degree in Business Administration from the University of Puerto Rico and is a Certified Public Accountant.

Juan Carlos Pavía was appointed Director of OMB on February 16, 2011. Prior to his appointment as Director of OMB, Mr. Pavía was Executive Vice President and Fiscal Agent of GDB as well as Executive Director of the Fiscal Stabilization and Reconstruction Board, where he was responsible for the compliance, oversight and economic studies areas of GDB. Before being named Executive Vice President and Fiscal Agent of GDB, he was a senior advisor to the President of GDB and Deputy Advisor to the Governor. Prior to entering public service, Mr. Pavía was employed in the commercial banking field. Mr. Pavía earned a bachelor's degree in Business Administration from The George Washington University in Washington D.C.

Juan Carlos Batlle was appointed President of GDB effective March 2, 2011. Prior to his appointment, Mr. Batlle served 14 years as a top executive for Santander Group in Puerto Rico. As part of the Investment Banking Group of Santander Securities Corporation, he served consecutively as Assistant Vice President in 1999, Vice President in 2001, and Senior Vice President and Director in 2003. In 2005, Mr. Batlle was named First Senior Vice President of Banco Santander Puerto Rico and President and Chief Executive Officer of Santander Asset Management Corporation. In 2008, Mr. Batlle was named Managing Director of Santander Securities Corporation. Prior to joining Santander in 1997, Mr. Batlle was employed by Popular Securities, Inc. Mr. Batlle has also been a member of the Boards of Directors of Santander Securities Corporation, Santander Asset Management Corporation and the First Puerto Rico Family of Funds. In addition, he has been a member of the Boards of Directors of the Puerto Rico Tourism Company, the Convention Center District Authority and the Hotel Development Corporation. He holds a degree in Economics from the College of Literature, Science and the Arts of the University of Michigan.

Political Trends

For many years there have been two major views in Puerto Rico with respect to Puerto Rico's relationship with the United States: one favoring statehood, represented by the New Progressive Party, and the other favoring the existing commonwealth status, represented by the Popular Democratic Party. The following table shows the percentages of the total votes received by the gubernatorial candidates of the various parties in the last five elections. While the electoral choices of Puerto Rico's voters are not based solely on party preferences regarding Puerto Rico's relationship with the United States, candidates who support a continuing relationship between Puerto Rico and the United States have prevailed in elections for many years.

	1992	1996	2000	2004	2008
New Progressive Party	49.9%	51.1%	45.7%	48.2%	52.8%
Popular Democratic Party	45.9%	44.5%	48.6%	48.4%	41.3%
Puerto Rico Independence Party	4.2%	3.8%	5.2%	2.7%	2.0%
Others, Blank or Void	-	0.5%	0.5%	0.6%	3.9%

With the results of the 2008 election, the New Progressive Party gained control of the Executive Branch and retained control of the Legislative Branch. The current membership of the Senate and House of Representatives by political party is as follows:

	Senate	House
New Progressive Party	21	37
Popular Democratic Party	8	17
Total	29	54

The next general election (gubernatorial, municipal, and legislative) in Puerto Rico will be held in November 2012.

THE ECONOMY

General

The Commonwealth in the past has established policies and programs directed principally at developing the manufacturing and service sectors and expanding and modernizing the Commonwealth's infrastructure. Domestic and foreign investments have historically been stimulated by selective tax exemptions, development loans, and other financial and tax incentives. Infrastructure expansion and modernization have been to a large extent financed by bonds and notes issued by the Commonwealth, its public corporations, and municipalities. Economic progress has been aided by significant increases in the levels of education and occupational skills of the population.

Puerto Rico's economy experienced a considerable transformation during the second half of the twentieth century, from an agriculture economy to an industrial one. Factors contributing to this transformation included government-sponsored economic development programs, increases in the level of federal transfer payments, and the relatively low cost of borrowing. In some years, these factors were aided by a significant rise in construction investment driven by infrastructure projects, private investment, primarily in housing, and relatively low oil prices. Nevertheless, the significant oil price increases experienced from January 2002 to June 2008, the continuous contraction of the manufacturing sector, and the budgetary pressures on government finances triggered a general contraction in the economy.

Puerto Rico's economy is currently in a recession that began in the fourth quarter of fiscal year 2006, a fiscal year in which the real gross national product grew by only 0.5% and the government was shut-down during the first two weeks of May. For fiscal years 2008 and 2009, the real gross national product contracted by 2.9% and 4.0%, respectively. For fiscal year 2010, preliminary reports indicate that the real gross national product contracted by 3.8%. The

Planning Board projects a decrease in real gross national product of 1.0% for fiscal year 2011 and an increase of 0.7% for fiscal year 2012.

Nominal personal income, both aggregate and per capita, has shown a positive average growth rate from 1947 to 2010. In fiscal year 2010, aggregate personal income was $60.4 billion ($50.0 billion at 2005 prices) and personal income per capita was $15,203 ($12,592 in 2005 prices). Personal income includes transfer payments to individuals in Puerto Rico under various social programs. Total U.S. federal transfer payments to individuals amounted to $16.0 billion in fiscal year 2010 ($14.0 billion in fiscal year 2009). Entitlements for previously performed services or resulting from contributions to programs such as Social Security, Veterans' Benefits, Medicare, and U.S. Civil Service retirement pensions were $10.4 billion, or 65% of the transfer payments to individuals in fiscal year 2010 ($9.8 billion, or 70.1%, in fiscal year 2009). The remainder of the federal transfers to individuals is represented by grants, mostly concentrated in the Nutritional Assistance Program (Food Stamps) and Pell Grant scholarships (higher education).

Total average annual employment (as measured by the Puerto Rico Department of Labor and Human Resources Household Employment Survey, known as the "Household Survey") decreased during the last decade. From fiscal year 2000 to fiscal year 2010, total employment decreased at an average annual rate of 0.4%, from 1,150,291 to 1,102,680. A reduction in total employment began in the fourth quarter of fiscal year 2006 and has continued consistently through fiscal year 2011 due to the current recession and the fiscal adjustment measures.

The dominant sectors of the Puerto Rico economy in terms of production and income are manufacturing and services. The manufacturing sector has undergone fundamental changes over the years as a result of increased emphasis on higher-wage, high-technology industries, such as pharmaceuticals, biotechnology, computers, microprocessors, professional and scientific instruments, and certain high technology machinery and equipment. The service sector, which includes finance, insurance, real estate, wholesale and retail trade, transportation, communications and public utilities, and other services, plays a major role in the economy. It ranks second to manufacturing in contribution to gross domestic product and leads all sectors in providing employment.

The following table shows the gross national product for the five fiscal years ended June 30, 2010.

Commonwealth of Puerto Rico
Gross National Product
Fiscal Years Ended June 30,

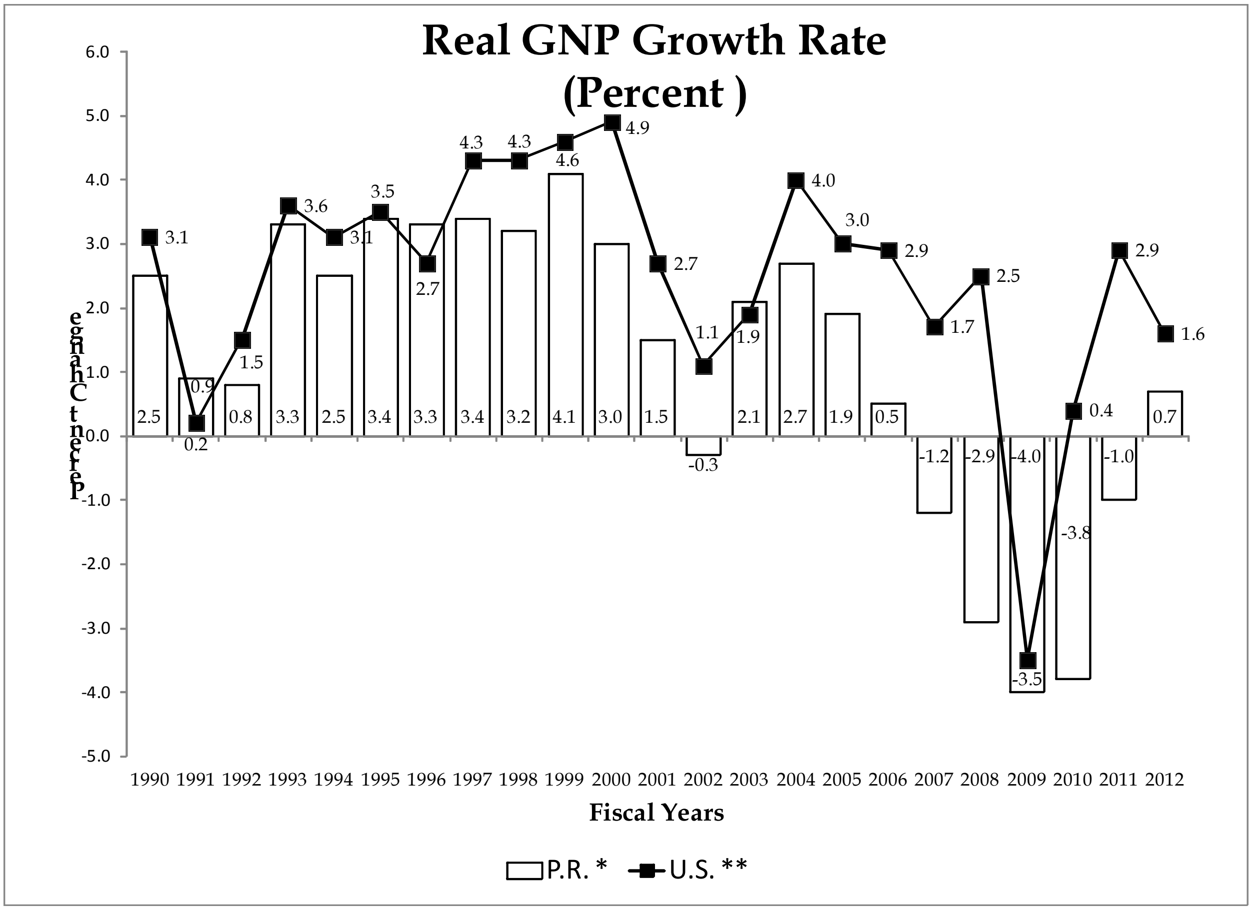
	2006	2007	2008	2009	2010 (1)
Gross national product – $ millions(2)	$56,732	$59,521	$61,665	$62,678	$63,292
Real gross national product – $ millions (2005 prices)	$54,027	$53,400	$51,832	$49,775	$47,898
Annual percentage increase (decrease) in real gross national product (2005 prices)	0.5%	(1.2)%	(2.9)%	(4.0)%	(3.8)%
U.S. annual percentage increase in real gross national product (2005 prices)	2.9%	1.7%	2.5%	(3.5)%	0.4%

(1) Preliminary.
(2) In current dollars.

Sources: Puerto Rico Planning Board and IHS-Global Insight.

The economy of Puerto Rico is closely linked to the United States economy, as most of the external factors that affect the Puerto Rico economy (other than oil prices) are determined by the policies and performance of the mainland economy. These external factors include exports, direct investment, the amount of federal transfer payments, the level of interest rates, the rate of inflation, and tourist expenditures. During fiscal year 2010, approximately 68.1% of Puerto Rico's exports went to the United States mainland, which was also the source of approximately 53.3% of Puerto Rico's imports. In fiscal year 2010, Puerto Rico experienced a positive merchandise trade balance of $22.4 billion.

The following graph compares the growth rate of real gross national product for the Puerto Rico and U.S. economies since fiscal year 1990, and the forecast of the growth rate for fiscal years 2011 and 2012.



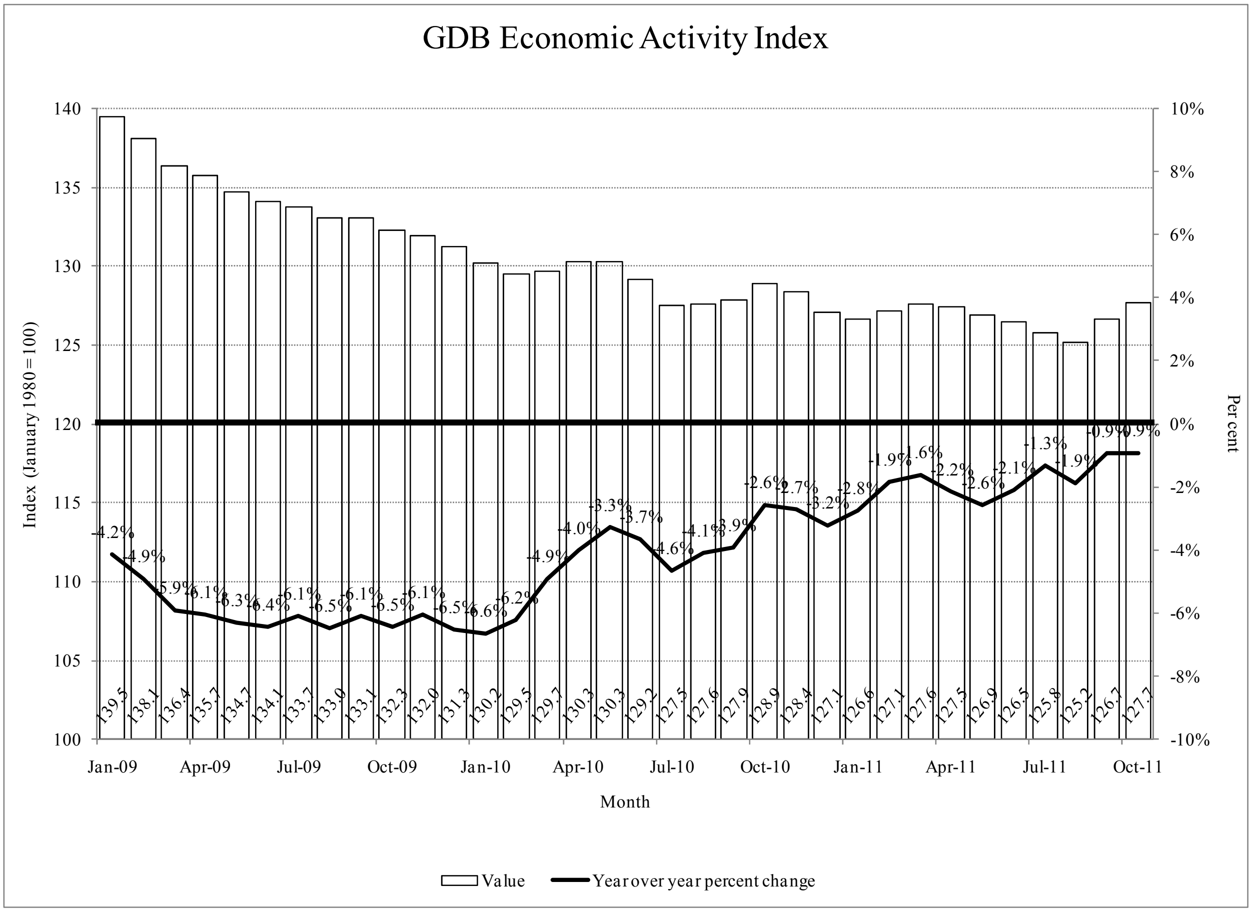
Sources: Puerto Rico Planning Board & IHS-Global Insight.

* Estimate for Puerto Rico from the Puerto Rico Planning Board (Mar-2011).
** Estimate for U.S. from IHS-Global Insight (Oct-2011).

Since the 1950s, the Planning Board has prepared a complete set of macroeconomic measures like those prepared for the United States by the Bureau of Economic Analysis ("BEA") of the Department of Commerce, as part of the National Income and Product Accounts ("NIPA"). In contrast with the BEA, which computes the economic accounts on a quarterly basis, the Planning Board computes Puerto Rico's NIPA on an annual basis. Like the BEA, the Planning Board revises its statistics on a regular basis. The Planning Board classifies its statistics as preliminary until they are revised and made final in conjunction with the release of new data each year. Thus, all macroeconomic accounts for fiscal year 2010 shown in this Report are preliminary until the revised figures for fiscal year 2010 and the preliminary figures of fiscal year 2011 are released and the forecast for fiscal year 2012 is revised.

Certain information regarding current economic activity, however, is available in the form of the Government Development Bank – Economic Activity Index (the "EAI"), a coincident indicator of ongoing economic activity. This index, shown in the following table and published by GDB since October 2009, is composed of several variables (total payroll employment based on the Establishment Survey, total electric power consumption, cement sales and consumption of gasoline) that highly correlate to Puerto Rico's real gross national product. The average contraction rate of the index for fiscal year 2011 was 2.9%, after a reduction of 5.6% for fiscal year 2010. For the first quarter of fiscal year 2012, this index decreased by 1.2%.

The month of September 2011, however, reflected the smallest year-over-year reduction in the EAI since October 2006.



Economic Forecast for Fiscal Years 2011 and 2012

On March 2011, the Planning Board released its revised gross national product forecast for fiscal year 2011 and its gross national product forecast for fiscal year 2012. The Planning Board revised its gross national product forecast for fiscal year 2011 from a projected growth of 0.4% to a contraction of 1.0%, both in constant dollars. The Planning Board's revised forecast for fiscal year 2011 took into account the estimated effects on the Puerto Rico economy of the Government's fiscal stabilization plan, the impact of the initial phase of the tax reform, the disbursement of funds from ARRA, the continuation of the fiscal stabilization plan, and the activity expected to be generated from the Government's local stimulus package. The revised forecast also considered the effect on the Puerto Rico economy of general and global economic conditions, the U.S. economy, the volatility of oil prices, interest rates and the behavior of local exports, including expenditures by visitors. The Planning Board's forecast for fiscal year 2012 projects an increase in gross national product of 0.7% in constant dollars. The Planning Board's forecast for fiscal year 2012 took into account the estimated effect of the projected growth of the U.S. economy, tourism activity, personal consumption expenditures, federal transfers to individuals and the acceleration of investment in construction due to the Government's local stimulus package and the establishment of public-private partnerships. It also took into account the disbursement of the remaining ARRA funds, and the continuation of the implementation of the tax reform.

Fiscal Year 2010

The Planning Board's preliminary reports on the performance of the Puerto Rico economy for fiscal year 2010 indicate that real gross national product decreased 3.8% (an increase of 1.0% in current dollars) over fiscal year 2009. Nominal gross national product was \$63.3 billion in fiscal year 2010 (\$47.9 billion in 2005 prices), compared to \$62.7 billion in fiscal year 2009 (\$49.8 billion in 2005 prices). Aggregate personal income increased from \$58.6 billion in fiscal year 2009 (\$49.8 billion in 2005 prices) to \$60.4 billion in fiscal year 2010 (\$50.0 billion in 2005 prices), and personal income per capita increased from \$14,786 in fiscal year 2009 (\$12,558 in 2005 prices) to \$15,203 in fiscal year 2010 (\$12,592 in 2005 prices).

According to the Household Survey, total employment for fiscal year 2010 averaged 1,102,700, a decrease of 65,500, or 5.6%, from the previous fiscal year. The unemployment rate for fiscal year 2010 was 16.0%, an increase from 13.4% for fiscal year 2009.

Among the variables contributing to the decrease in gross national product was the continuous contraction of the manufacturing and construction sectors. Due to the Commonwealth's dependence on oil for power generation and gasoline (in spite of its recent improvements in power-production diversification), the high level of oil prices accounted for an increased outflow of local income in fiscal year 2008, when the average price of the West Texas Intermediate oil barrel (WTI) increased by 53.1% to reach an average of \$97.0/bbl. Although the situation improved significantly during fiscal year 2009, with a decline of 28.1% in the price of the WTI, oil prices remained at relatively high levels, at an average of \$69.7/bbl, and the impact of the increases of previous years were still felt in fiscal year 2009. Nevertheless, during fiscal year 2010, the average price of the WTI increased by 7.9% to \$75.2/bbl, which put more pressure on internal demand. On the other hand, the continuation of the difficulties associated with the financial crisis kept short-term interest rates at historically low levels, but this did not translate into a significant improvement in the construction sector due to the high level of inventory of residential housing units.

Fiscal Year 2009

The Planning Board's reports on the performance of the Puerto Rico economy for fiscal year 2009 indicate that real gross national product decreased 4.0% (an increase of 1.6% in current dollars) over fiscal year 2008. Nominal gross national product was \$62.7 billion in fiscal year 2009 (\$49.8 billion in 2005 prices), compared to \$61.7 billion in fiscal year 2008 (\$51.8 billion in 2005 prices). Aggregate personal income increased from \$56.1 billion in fiscal year 2008 (\$49.6 billion in 2005 prices) to \$58.6 billion in fiscal year 2009 (\$49.7 billion in 2005 prices), and personal income per capita increased from \$14,217 in fiscal year 2008 (\$12,557 in 2005 prices) to \$14,786 in fiscal year 2009 (\$12,558 in 2005 prices).

According to the Household Survey, total employment for fiscal year 2009 averaged 1,168,200, a decrease of 4.1% compared to 1,217,500 for fiscal year 2008. At the same time, the unemployment rate for fiscal year 2009 was 13.4%, an increase from 11% for fiscal year 2008.

Among the variables contributing to the decrease in gross national product were the continuous contraction of the manufacturing and construction sectors, as well as the corresponding contraction of U.S. economic activity. Furthermore, the decline in Puerto Rico's gross national product was not offset by the federal tax rebates due to the high levels of oil prices during fiscal year 2008. The dramatic increase to record levels in the price of oil and its derivatives (such as gasoline) during that period served to reduce the income available for other purchases and, thereby, negatively affected domestic demand. Due to the Commonwealth's dependence on oil for power generation and gasoline (in spite of its recent improvements in power-production diversification), the high level of oil prices accounted for an increased outflow of local income in fiscal year 2008. The global financial crisis promoted lower interest rates that were reflected in the local market, but those rates did not improve the conditions in the construction sector.

Fiscal Stabilization and Economic Reconstruction

In January 2009, the Government began to implement a multi-year Fiscal Stabilization Plan (the "Fiscal Plan") and Economic Reconstruction Plan (the "Economic Plan") that sought to achieve fiscal balance and restore economic growth. The Fiscal Plan was central to safeguarding the Commonwealth's investment-grade credit rating and restoring Puerto Rico's economic growth and development.

In addition, the administration designed and began to implement the *Strategic Model for a New Economy*, a series of economic development initiatives which aim to enhance Puerto Rico's competitiveness and strengthen specific industry sectors. These economic development initiatives were intended to support the prospects of long-term and sustainable growth.

Fiscal Stabilization Plan

The Fiscal Plan had three main objectives: (i) stabilize the short-term fiscal situation, (ii) safeguard and strengthen the Commonwealth's investment-grade credit rating, and (iii) achieve budgetary balance. The Fiscal Plan, which was generally contained in Act 7, included operating expense-reduction measures, tax revenue enforcement measures, temporary and permanent revenue raising measures, and financial measures, as discussed below.

Expense Reduction Measures. A significant portion of Puerto Rico's budget deficit is attributable to the accumulated effect of high operating expenses in the government. The Fiscal Plan sought to reduce the government's recurring expense base to make it consistent with the level of government revenues. The Fiscal Plan established a government-wide operating expense-reduction program aimed at reducing operating expenses, including payroll.

Payroll expense is the most significant component of the government's recurring expense base. The reduction in payroll expenses contemplated by the Fiscal Plan was implemented in three phases and included certain benefits conferred to participating employees, as follows:

- *Phase I: Incentivized Voluntary Resignation and Voluntary Permanent Workday Reduction Programs:* The Incentivized Voluntary Resignation Program offered public employees a compensation incentive based on the time of service in the government. The Voluntary Permanent Workday Reduction Program was available to public employees with 20 or more years of service. The Workday Reduction Program consisted of a voluntary reduction of one regular workday every fifteen calendar days, which is equivalent to approximately a 10% reduction in annual workdays. Phase I commenced in March 2009 and public employees had until April 27, 2009 to submit the required information to participate in the voluntary programs available under Phase I and be eligible for the Public Employees Alternatives Program. Under Phase I, 2,553 employees resigned under the Incentivized Voluntary Resignation Program and 27 employees took advantage of the Voluntary Permanent Workday Reduction Program. Based on the number of employees who agreed to participate in these programs, the administration estimates that expenses for fiscal year 2010 were reduced by $90.9 million.

- *Phase II: Involuntary Layoff Plan:* As provided in Act 7, Phase II went into effect because the objective of reducing $2 billion in expenses was not achieved after implementation of Phase I and Phase III (see below). Under Phase II, subject to certain exceptions, employees with transitory or non-permanent positions were terminated. As a result, 1,986 positions were eliminated, representing an estimated savings of $44.6 million annually. In addition, Phase II provided for one or more rounds of involuntary layoffs and applied to most central government public employees unless excluded pursuant to Act 7, strictly according to seniority in public service, starting with employees with the least seniority. The plan excluded certain employees providing "essential" services, certain employees paid by federal funds, those on military leave, and political appointees and their trust employees (political appointees and their trust employees, who do not hold a permanent or career position in the government, are referred to herein as "non-career employees"). Employees in Phase II received a severance package that included health coverage payment for up to a maximum of six months or until the former public employee became eligible for health insurance coverage at another job. As of September 30, 2010, total government employees dismissed under Phase II (excluding the 1,986 transitory or non-permanent positions eliminated) was approximately 12,505, representing an estimated savings of $322.8 million annually. This amount excludes approximately 1,784 employees rehired by the Department of Education as a result of an agreement with the union providing for certain salary and workday reductions and the inclusion of additional service requirements, among other things. The negotiation of this agreement by the administration resulted in annual savings of $51 million, an increase of $25 million over the estimated savings achievable through the termination of such employees.

- *Phase III: Temporary Suspension of Certain Provisions of Laws, Collective Bargaining Agreements, and Other Agreements:* Phase III went into effect on March 9, 2009 and imposed a temporary freeze on salary increases and other economic benefits included in laws, collective bargaining agreements, and any other agreements. Phase III remained in effect for a period of two years. The administration estimates that savings from the implementation of these measures was approximately $186.9 million for fiscal year 2010.

- <u>Public Employees Alternatives Program</u>: The employees that elected to participate in the Incentivized Voluntary Resignation Program under Phase I or that were subject to involuntary layoffs under Phase II, were eligible to participate in the Public Employees Alternatives Program. This program assists public employees in their transition to other productive alternatives, and offers vouchers for college education, technical education, and professional training, as well as for establishing a business and for relocation.

Act 7 extended the term of collective bargaining agreements with public employees that had expired at the time of its enactment or that expire while it is in effect for a period of two years (until March 9, 2011) and provided that during this period such collective bargaining agreements may not be renegotiated or renewed. Act No. 73 of May 17, 2011 ("Act 73") extended the term of the non-economic clauses of such collective bargaining agreements for an additional period of two years (until March 9, 2013) and provided that the economic clauses may be negotiated considering primarily the fiscal condition of the applicable agency and the Government and the safeguarding of services to the people. Act 73 further provides that for the negotiation of any economic clauses, OMB must evaluate the current and projected fiscal condition of the applicable agency and the Government and issue a certification as to the available resources, if any, for such negotiations.

The following table summarizes the amount of employees affected by the workforce and labor related expense reduction measures included in Act 7 and the expected annual savings in operational expenses from the implementation of Phases I through III of the Fiscal Plan. The implementation of the workforce and labor related expense reduction measures included in Act 7 concluded on June 30, 2010.

Phase	**Affected Employees**	**Savings (in millions)**
Phase I: Voluntary Resignation	2,553	$90.9
Phase II: Involuntary Layoffs		
Termination of transitory and non-permanent employees	1,986	44.6
Layoffs (as of April 30, 2010)	12,505	322.8
Phase III: Suspension of Certain Benefits	-	186.9
Total	17,044	$645.2

The second element of the expense-reduction measures, which pertains to other operating expenses, was conducted through an austerity program in combination with other expense reduction measures. The austerity program mandated a 10% reduction in other operational expenses, including cellular phone use, credit cards, and official vehicles.

In July 2010, the Governor renewed an executive order issued in September 2009 requiring all agencies and public corporations to reduce, modify or cancel service contracts to achieve a cost reduction of at least 15%. The executive order covers advertising, consulting, information technology, accounting, legal and other services (except for direct services to the public), and grants the Fiscal Restructuring and Stabilization Board created under Act 7 (the "Fiscal Board") the power to monitor agencies and public corporations in order to ensure the required 15% minimum cost reduction. Each agency or public corporation had 30 days to report the following to the Fiscal Board: (i) all service contracts currently in effect, (ii) all canceled and/or modified contracts and the corresponding savings, (iii) justification for any remaining contracts in light of the mission of the agency or public corporation, and (iv) the reasonableness of the fees or compensation terms for each remaining contract.

In July 2010, the Governor also renewed another executive order issued in September 2009 requiring all agencies and public corporations to report the following to the Fiscal Board within 30 days: (i) all lease contracts currently in effect, (ii) the uses of leased premises, (iii) the needs for such premises, (iv) the terms and conditions of each lease, and (v) budgeted amounts for rent and other related expenses. During fiscal year 2010, the administration achieved savings by, among other things, consolidating operations of one or more agencies or public corporations and renegotiating leases to obtain more favorable terms. The administration estimates annual savings as a result of the revision of all leases of at least 15% of rent and related expenses, or approximately $22 million annually.

Tax Revenue Enforcement Measures. The Fiscal Plan also sought to increase tax revenues by implementing a more rigorous and ongoing tax enforcement and compliance strategy. Specific tax enforcement initiatives included: (i) enhancements to the administration of federal grants and fund receipts, (ii) stronger collections and auditing efforts on Puerto Rico's sales and use tax, and (iii) a voluntary tax compliance program.

Revenue Raising Measures. The goal of achieving fiscal and budgetary balance required a combination of measures that included the introduction of permanent and temporary tax increases. The Fiscal Plan included six temporary and four permanent revenue increasing measures. The temporary revenue increasing measures consisted of: (i) a 5% surtax on income of certain individuals, (ii) a 5% surtax on income of certain corporations, (iii) a 5% income tax on credit unions (commonly known as "cooperativas" in Puerto Rico), (iv) a 5% income tax on Puerto Rico international banking entities, (v) a special property tax on residential and commercial real estate, and (vi) a moratorium on certain tax credits. The temporary measures were initially set to be in effect for up to three fiscal years beginning in fiscal year 2010. Act 1 of 2011, however, limited the duration of the 5% surtax on income derived by certain individuals and corporations and the special property tax to two years. The permanent measures include (i) modifications to the alternative minimum tax for individuals and corporations, (ii) an increase in the excise tax on cigarettes, (iii) a new excise tax on motorcycles, and (iv) an increase in the excise tax on alcoholic beverages. The total revenues from these temporary and permanent measures for fiscal year 2010 were $428 million. The total preliminary revenues from these temporary and permanent measures for fiscal year 2011 were $450 million.

Financial Measures. The administration has also carried out several financial measures designed to achieve fiscal stability throughout the Fiscal Plan implementation period. These measures included, among others, (i) a financing or bond issuance program, the proceeds of which were used to bridge the budgetary imbalance during the Fiscal Plan implementation period and fund some of the Economic Plan initiatives, (ii) the restructuring of the securities held in the

Corpus Account of the Infrastructure Development Fund and (iii) the restructuring of a portion of the Commonwealth's debt service.

These financial measures were anchored on the bond-issuance program of COFINA. Act 7, in conjunction with Act No. 91 of May 13, 2006, as amended ("Act 91 of 2006"), and Act No. 1 of January 14, 2009 ("Act 1 of 2009"), allocated to COFINA, commencing on July 1, 2009, 2.75% (one-half of the tax rate of 5.5%) of the sales and use tax imposed by the central government, thus increasing COFINA's financing capacity and allowing the Commonwealth to achieve fiscal stability throughout the implementation period of the Fiscal Plan.

During fiscal years 2009 and 2010, COFINA issued approximately $5.6 billion and $3.6 billion, respectively, of revenue bonds payable from sales and use tax collections transferred to COFINA. The proceeds from these bond issues were used for, among other uses, paying approximately $1.9 billion of Commonwealth obligations that did not have a designated source of repayment, paying or financing approximately $4.8 billion of operational expenses constituting a portion of the Commonwealth's deficit, and funding the Local Stimulus Fund (described below) and the Stabilization Fund for fiscal year 2011 with approximately $500 million and $1.0 billion, respectively. During fiscal year 2012, COFINA expects to issue approximately $2 billion of revenue bonds payable from sales and use tax collections transferred to COFINA, the proceeds of which will be mainly used to finance a portion of the government's operating expenses for fiscal year 2012 and refund outstanding bonds payable from Commonwealth appropriations.

Act No. 3, approved by the Legislative Assembly of the Commonwealth on January 14, 2009 ("Act 3"), authorized the sale of the securities held in the Corpus Account. PRIFA sold the securities in January 2009 and used the proceeds to, among other things, make a deposit to the General Fund of approximately $319 million, which was applied to cover a portion of the Commonwealth's budget deficit and make a transfer to GDB of approximately $159 million as a capital contribution. The gross proceeds resulting from the sale were approximately $884 million.

Another financial measure taken has been the restructuring of a portion of the Commonwealth's debt service on the Commonwealth's general obligation bonds and bonds of PBA that are guaranteed by the Commonwealth and are payable from Commonwealth budget appropriations. During fiscal year 2010, the Commonwealth refinanced $512.9 million of interest accrued during such fiscal year on the Commonwealth's general obligation bonds and $164.5 million of interest accrued during such fiscal year on PBA bonds. During fiscal year 2011, the Commonwealth refinanced $490.9 million of interest accrued during such fiscal year and principal due on July 1, 2011 on the Commonwealth's general obligation bonds. During fiscal year 2011, PBA also used a line of credit from GDB to make payments of approximately $147.8 million of interest accrued during such fiscal year on its Commonwealth guaranteed bonds, which line of credit was refinanced with the proceeds of a series of Commonwealth guaranteed bonds issued by PBA.

During fiscal year 2012, the Government expects to refinance approximately $537.4 million of principal due in and interest to accrue during such fiscal year on the Commonwealth's general obligation bonds and approximately $153.8 million of interest to accrue during such fiscal year on Commonwealth guaranteed PBA bonds.

The Fiscal Plan has provided more fiscal stability, thereby safeguarding and strengthening Puerto Rico's credit. The fiscal structure resulting from the full implementation of the plan will be sustainable and conducive to economic growth and development.

Economic Reconstruction Plan

To balance the impact of the Fiscal Plan, the administration developed and is implementing an economic reconstruction program designed to stimulate growth in the short term and lay the foundation for long-term economic development. The Economic Plan consists of two main components: (i) two economic stimulus programs, and (ii) a supplemental stimulus plan.

Economic Stimulus Programs. The cornerstone of Puerto Rico's short-term economic reconstruction plan was the implementation of two economic stimulus programs aimed at reigniting growth and counterbalancing any adverse effects associated with the Fiscal Plan. The economic stimulus programs consisted of Puerto Rico's participation in ARRA (also referred to herein as the "Federal Stimulus") and a local plan (the "Local Stimulus") designed to complement the Federal Stimulus.

- ***Federal Stimulus Program:*** Puerto Rico was awarded $6.8 billion in stimulus funds from ARRA. The funds are distributed in four main categories: relief to individuals, budgetary and fiscal relief, taxpayers' relief, and capital improvements. In terms of government programs, the Federal Stimulus allocates funds to education, agriculture and food assistance, health, housing and urban development, labor, and transportation, among others. As of October 14, 2011, PRIFA, which is responsible for the administration of ARRA in Puerto Rico, reported that approximately $5.5 billion in ARRA funds had been disbursed, representing 78.8%, of awarded funds.

- ***Local Stimulus Program:*** The administration formulated the Local Stimulus to supplement the Federal Stimulus and address specific local challenges associated with the local mortgage market, the availability of credit, and the infrastructure and construction sectors. Despite the fact that the Local Stimulus amounted to a $500 million investment by the government, it is estimated that its effect would be greater due to certain lending programs, which are being coordinated in collaboration with commercial banks in Puerto Rico. The administration has been disbursing funds under the $500 million local stimulus program. Most municipalities have received disbursements earmarked to pay outstanding debts and fund local projects. The administration has also disbursed funds allocated towards job training programs, a strategic water distribution project in a southern municipality and the revamping of the Puerto Rico permits system. It is estimated that approximately $400 million of Local Stimulus funds will be used for infrastructure projects. As of September 30, 2011, approximately $360 million of Local Stimulus funds had been disbursed.

Supplemental Stimulus Plan. The Supplemental Stimulus Plan was designed to provide investment in strategic areas with the objective of laying the foundations for long-term growth in Puerto Rico. The coordinated implementation of the Supplemental Stimulus Plan is expected to reinforce continuity in reigniting economic growth while making key investments for long-term development.

The Supplemental Stimulus Plan is being conducted through a combination of direct investments and guaranteed lending. Specifically, the Supplemental Stimulus Plan targets critical areas such as key infrastructure projects, public capital improvement programs, private-sector lending to specific industries, and the export and research-and-development knowledge industries. The Supplemental Stimulus Plan takes into account the strategic needs that Puerto Rico must fulfill in order to become a more competitive player in its region and in the global economy.

On September 1, 2010 the Governor signed Act No. 132, also known as the Real Estate Market Stimulus Act of 2010 ("Act 132"), which provides certain incentives to help reduce the existing housing inventory. The incentives provided by Act 132 were effective from September 1, 2010 through June 30, 2011, and were subsequently extended until October 31, 2011 by Act No. 115 of July 5, 2011. On November 1, 2011, the Government approved Act 216, which provides incentives similar to the ones available under Act 132 and establishes an orderly transition to gradually reduce those incentives without disrupting the functioning of the housing market in Puerto Rico. The incentives provided by Act 216 are limited to residential real property and are effective from November 1, 2011 to December 31, 2012, with certain reductions after December 31, 2011 and June 30, 2012 See "Economic Performance by Sector—Construction" below.

Economic Development Program

The Department of Economic Development and Commerce ("DEDC"), in coordination with other government agencies, is in the process of implementing the *Strategic Model for a New Economy*, which consists of a comprehensive, long-term, economic development program aimed at improving Puerto Rico's overall global relevance, competitiveness, and business environment, and increasing private-sector capital formation and participation in the economy. These initiatives are centered on the dual mission of fostering multi-sector growth while reducing costs and barriers to business and investment, and are a medium-to-long-term counterpart to the Economic Plan and the Supplemental Stimulus Plan described above.

The administration is emphasizing the following initiatives to enhance Puerto Rico's competitive position: (i) overhauling the permitting process, (ii) reducing energy costs, (iii) reforming the tax system, (iv) promoting the development of various projects through public-private partnerships, (v) implementing strategic initiatives targeted at specific economic sectors, and (vi) promoting the development of certain strategic/regional projects.

Permitting Process. The first initiative, the reengineering of Puerto Rico's permitting and licensing process, has already been achieved. On December 1, 2009, the Governor signed into law Act No. 161, known as the Law for the Restructuring & Unification of the Permit Evaluation & Authorization Process, which overhauls the existing permitting and licensing process in Puerto Rico in order to provide for a leaner and more efficient process that fosters economic development. In the short term, this restructuring is focused on eliminating the significant backlog of unprocessed permits that are currently in the pipeline of various government agencies. In the long term, this law seeks to significantly reduce the number of inter-agency processes and transactions currently required by creating a centralized, client-focused system that simplifies and shortens the permitting process for applicants. The Integrated Permits System (SIP by its Spanish acronym), as the new Puerto Rico permits process is called, became operational on December 1, 2010. Through September, 2011 38,500 permits requests have been filed and 88% of these have already been resolved.

The Permit Management Office (OGPe, by its Spanish acronym), the government body responsible for evaluating permit applications and issuing final determinations concerning construction and land use, currently offers 80% of its services online, representing 90% of the total volume of transactions.

Energy Policy. On July 19, 2010, the Governor signed Acts No. 82 and 83, providing for, among other things, the adoption of a new energy policy, which is critical for Puerto Rico's competitiveness. Presently, fluctuations in oil prices have a significant effect on Puerto Rico's overall economic performance. Act No. 82 of 2010, known as the "Public Policy on Energy Diversification through Renewable and Alternative Sources," focuses on reducing Puerto Rico's dependence on fossil fuels, particularly oil, through the promotion of diverse, renewable-energy technologies. This new energy policy seeks to lower energy costs, reduce energy-price volatility, and establish environmentally sustainable energy production through a reduction in ecologically harmful emissions. Act 82 of 2010 creates a Renewable Portfolio Standard, recognizing many sources of renewable energy utilizing various technologies, setting a hard target of 12% renewable energy production by 2015 and 15% by 2020, and a requirement for retail energy providers to establish a plan to reach 20% renewable energy production by 2035.

Moreover, Act No. 83 of 2010, also known as the "Green Energy Incentives Act, assembles under one law the incentives for the construction and use of renewable energy sources. Act 83 offers new benefits to stimulate the development of green energy projects, creates Renewable Energy Certificates (RECs) and creates the Green Energy Fund (the "GEF"). Through the GEF the Government will co-invest $290 million in renewable energy projects over the next 10-years. Initial funding of $20 million began on July 1, 2011 and steps up to $40 million per year by fiscal year 2016. Through the GEF, the Puerto Rico Energy Affairs Administration will offer cash rebates of up to 60% on the cost of installing Tier 1 projects (0 – 100 kW) for residences and small businesses and up to 50% on the cost of Tier 2 projects (100 kW – 1 MW) for commercial or industrial use. In its first round of funding, the GEF backed 25 solar energy projects with $6.6 million, including grants to 13 businesses and a government agency. These initiatives are expected to address energy prices in Puerto Rico and provide a means of attracting investment in the energy sector.

Tax Reform. Legislation to implement the first and second phases of the tax reform was enacted as Act No. 171 of 2010 and Act 1 of 2011, respectively. See "Major Sources of General Fund Revenues—Tax Reform" under PUERTO RICO TAXES, OTHER REVENUES AND EXPENDITURES for a summary of the principal provisions of the tax reform.

Public-Private Partnerships. The Government believes that PPPs represent an important tool for economic development, particularly in times of fiscal difficulties. PPPs are long-term contracts between government and non-governmental entities—such as private companies, credit unions, and municipal corporations—to develop, operate, manage or maximize infrastructure projects and/or government services. PPP contracts are centered on the concept of risk transfer. The non-governmental partner takes on certain responsibilities and risks related to the development and/or operation of the project in exchange for certain benefits. PPPs can play a pivotal role in restoring investment in infrastructure and bringing about economic growth.

PPPs provide the opportunity for the government to lower project development costs, accelerate project development, reduce financial risk, create additional revenue sources, establish service quality metrics, re-direct government resources to focus on the implementation of public policy, create jobs and attract new investment. Puerto Rico has opportunities for the establishment of PPPs in the areas of toll roads, airports and maritime ports, public schools, water provision, correctional facilities, and energy, among others.

On June 8, 2009, the Legislative Assembly approved Act No. 29 ("Act 29"), which established a clear public policy and legal framework for the establishment of PPPs in Puerto Rico to further the development and maintenance of infrastructure facilities, improve the services rendered by the Government and foster the creation of jobs. Act 29 created the Public-Private Partnerships Authority (the "PPP Authority"), the entity tasked with implementing the Commonwealth's public policy regarding PPPs. On December 19, 2009, the PPP Authority approved regulations establishing the administrative framework for the procurement, evaluation, selection, negotiation and award process for PPPs in Puerto Rico.

During fiscal year 2010, the PPP Authority engaged various financial advisors to assist it in the evaluation and procurement of various projects in the energy, transportation, water and public school infrastructure sectors. During the fourth quarter of fiscal year 2010, the PPP Authority published desirability studies for four public-private partnership priority projects and commenced procurement for such projects.

As part of the Government's PPPs initiative, the PPP Authority and the Highways and Transportation Authority (collectively, the "Sponsors") recently completed the procurement for a concession of toll roads PR-22 and PR-5 (the "Toll Roads"). On June 10, 2011, the Sponsors selected Autopistas Metropolitanas de Puerto Rico, LLC ("Metropistas"), a consortium comprised of Goldman Sachs Infrastructure Partners and Abertis Infraestructuras, as the winning proponent based on a bid of $1.080 billion. On June 27, 2011, Metropistas and the Highways and Transportation Authority executed the concession agreement for the Toll Roads (the "Concession Agreement") and, on September 22, 2011, the parties successfully completed the financial closing. As a result of this transaction, the Highways and Transportation Authority received a lump-sup payment of $1.136 billion and a commitment to invest $56 million in immediate improvements and comply with world-class operating standards.

To modernize public school facilities throughout the island and improve academic performance, the PPP Authority launched the "Schools for the 21st Century" program, which will modernize and build a selected number of public schools throughout Puerto Rico. At least one school in each municipality will benefit from the "Schools for the 21st Century" program.

The Government expects this project will impact nearly 50,000 students, 2,000 teachers and various communities and create 14,000 jobs throughout Puerto Rico's 78 municipalities. The Government will fund this project with the proceeds of Qualified School Construction Bonds (QSCB) issued by PBA in the aggregate principal amount of $756 million. As of June 2011, the PPP Authority had awarded approximately $464 million in contracts and construction had begun in approximately 57 schools.

On August 8, 2011, the PPP Authority and the Puerto Rico Ports Authority ("PRPA") received statements of qualifications from twelve (12) world-class consortia in response to the Request for Qualifications (RFQ) to acquire a concession to finance, operate, maintain and improve the Luis Muñoz Marín International Airport ("Airport"), the busiest airport in the Caribbean. The PPP Authority and the PRPA are seeking to achieve their primary objectives of: (i) maximizing the upfront value for the Airport, (ii) improving the Airport's safety standards, service levels and quality, (iii) maintaining and improving the quality of service to travelers as well as achieving a higher level of customer satisfaction, and (iv) creating a world-class gateway to Puerto Rico while increasing the Island's profile as a destination in the Caribbean, in order to positively impact the development of the tourism industry and overall economic prospects in Puerto Rico. The PPP Authority published the Request for Proposals for the Airport in October 2011 and expects to select a winning bidder in the first quarter of calendar 2012.

Sector Initiatives. The administration will complement the previously mentioned initiatives with specific strategic initiatives with the objective of creating jobs and increasing economic activity across various sectors of the Puerto Rico economy. The Commonwealth has natural or structural competitive advantages in several areas, such as pharmaceutical and biotechnology manufacturing. These advantages provide opportunities for the development of regional clusters in high-tech manufacturing, research and development, tourism, renewable energy, international trade and professional services. The specific initiatives will be designed to promote sustainable economic growth while accelerating to a knowledge-based and innovation driven economy, focused mainly in the development of human capital and intellectual property, thus diversifying Puerto Rico's economic base.

Strategic/Regional Projects. The administration has also targeted strategic/regional projects that will generate investments in various regions of the Island in order to foster balanced economic development.

One of the strategic projects for the northern region is called the Urban Bay (formerly known as the Golden Triangle), an urban redevelopment project that incorporates the areas of Old San Juan, Puerta de Tierra, Isla Grande, including the Puerto Rico Convention Center District (the "District"), and Condado, as well as other communities in the vicinity of historic San Juan Bay. The aim of the Urban Bay project is to develop San Juan Bay into a major tourism, recreation, commercial and residential sector which serves the local community and becomes a major attraction for leisure and business travelers, both local and external. Construction of the immediate improvements on the project footprint is already underway.

Also in the northern region, Science City also represents a critical effort to move Puerto Rico to the forefront of science, technology and research and development. It seeks to leverage the significant competitive advantages in the knowledge-based sectors that put Puerto Rico in an ideal position to undertake this type of development. Through the recently enacted Law No. 208 of October 20, 2011, the benefits of investing in and performing science and technology research and development activities in the newly denominated "Science District" were expanded through the inclusion of such activities as eligible for tax exemption under the Economic Incentives Act. See "Tax Incentives – Industrial Incentives Program" under THE ECONOMY. The benefits of the Science District under Law 208 may also be expanded to satellite districts throughout the island. The Science City approved site consultation will be amended to modify its land use. Demolition related activities and earth movement is expected to commence before the end of fiscal year 2012.

In the eastern region, the Caribbean Riviera entails the redevelopment of the old Roosevelt Roads navy facility in Ceiba and is a key element in the administration's strategy to create jobs and reignite the economy of Puerto Rico's eastern region, including Ceiba, Naguabo, Vieques, and Culebra. This tourist complex will include hotels, casinos, eco-tourist attractions, international airport, retail, yacht marina, and cruise ship ports. Negotiations with the Navy regarding the transfer of the property to the Local Redevelopment Authority are in advanced stages and should be completed by the end of 2011.

In the western region, the administration is focused on the redevelopment of the Aguadilla airport to serve as the second international airport of Puerto Rico and as a regional logistics hub. The Government is in the process of submitting a formal application to obtain a Foreign Trade Zone designation for the Aguadilla airport.

Employment and Unemployment

According to the Household Survey, the number of persons employed in Puerto Rico during fiscal year 2011 averaged 1,077,000, a decrease of 2.3% compared to previous fiscal year; and the unemployment rate averaged 15.9%. During the first four months of fiscal year 2012, total employment averaged 1,067,500, a decline of 1.2% with respect to the same period of the prior year; and the unemployment rate decreased to 16.1%.

The following table presents annual statistics of employment and unemployment for fiscal year 2007 through fiscal year 2011, and the average figures for the first two months of fiscal year 2012. These employment figures are based on the Household Survey, which includes self-employed individuals and agriculture employment, instead of the non-farm, payroll employment survey (the "Payroll Survey"), which does not. The number of self-employed individuals represents around 15% of civilian employment in Puerto Rico, more than double the level in the United States. On the other hand, agriculture employment in Puerto Rico represented 1.6% of total employment in fiscal year 2011.

Commonwealth of Puerto Rico
Employment and Unemployment[1]
(persons age 16 and over, in thousands)

Fiscal Years Ended June 30,	Labor Force	Employed	Unemployed	Unemployment Rate[2]
		(Annual Average)		
2007	1,410	1,263	147	10.4
2008	1,368	1,218	151	11.0
2009	1,349	1,168	181	13.4
2010	1,313	1,103	210	16.0
2011	1,287	1,077	204	15.9
2012[3]	1,272	1,068	205	16.1

(1) Totals may not add due to rounding.
(2) Unemployed as percentage of labor force.
(3) Average figures for the first four months of fiscal year 2012 (July 2011 through October 2011).

Source: Department of Labor and Human Resources – Household Survey

Economic Performance by Sector

From fiscal year 2007 to fiscal year 2010, the manufacturing and service sectors generated the largest portion of gross domestic product. The manufacturing, service, and government sectors were the three sectors of the economy that provided the most employment in Puerto Rico.

The following table presents annual statistics of gross domestic product by sector and gross national product for fiscal years 2007 to 2010.

Commonwealth of Puerto Rico
Gross Domestic Product by Sector and Gross National Product[1]
(in millions at current prices)

	Fiscal Years Ended June 30,			
	2007	**2008**	**2009**	**2010[1]**
Manufacturing	$37,637	$40,234	$44,019	$44,641
Service[2]	40,190	41,372	40,333	41,472
Government[3]	8,585	8,762	9,047	8,276
Agriculture	430	519	506	553
Construction[4]	2,027	2,032	1,818	1,658
Statistical discrepancy	(464)	(312)	(512)	(340)
Total gross domestic product[5]	$88,405	$92,606	$95,211	$96,261
Less: net payment abroad	(28,884)	(30,941)	(32,534)	(32,969)
Total gross national product[5]	$59,521	$61,665	$62,678	$63,292

(1) Preliminary.
(2) Includes wholesale and retail trade, utilities, transportation and warehousing, information, finance and insurance, real estate and rental, and certain services such as professional, scientific, technical, management, administrative, support, educational, health care, social, recreational, accommodation, food and other services.
(3) Includes the Commonwealth, its municipalities and certain public corporations, and the federal government. Excludes certain public corporations, such as the Electric Power Authority and the Aqueduct and Sewer Authority, whose activities are included under "Service" in the table.
(4) Includes mining.
(5) Totals may not add due to rounding.

Source: Planning Board

Traditionally, the Government has presented the industrial distribution of production in Puerto Rico using gross domestic product because the Planning Board had not published such a distribution using real gross national product as a base measurement. Recently, the Planning Board presented an industrial distribution of production based on real gross national product, which shows significant differences in the importance of the manufacturing sector to the Puerto Rico economy:

Commonwealth of Puerto Rico
Gross National Product by Sector
(at current prices, in millions)

	Fiscal Years Ended June 30,			
	2007	**2008**	**2009**	**2010[1]**
Service[2]	$35,443	$36,127	$35,429	$36,252
Manufacturing	12,570	13,556	15,282	15,769
Government[3]	9,529	9,757	10,167	9,411
Construction[4]	2,013	2,018	1,805	1,646
Agriculture	430	520	507	553
Statistical discrepancy	(464)	(312)	(12)	(340)
Total gross national product[5]	$59,520	$61,665	$62,678	$63,292

(1) Preliminary.
(2) Includes wholesale and retail trade, utilities, transportation and warehousing, information, finance and insurance, real estate and rental, and certain services such as professional, scientific, technical, management, administrative, support, educational, health care, social, recreational, accommodation, food and other services.
(3) Includes the Commonwealth, its municipalities and certain public corporations, and the federal government. Excludes certain public corporations, such as the Electric Power Authority and the Aqueduct and Sewer Authority, whose activities are included under "Service" in the table.
(4) Includes mining.
(5) Totals may not add due to rounding.

Source: Planning Board

The service sector's (which includes wholesale and retail trade, utilities, transportation and warehousing, information, finance and insurance, real estate and rental, and certain services such as professional, scientific, technical, management, administrative, support, educational, health care, social, recreational, accommodation, food and other services) share appears significantly higher than manufacturing when compared to the industrial distribution of production in Puerto Rico based on gross domestic product. This variance occurs because manufacturing activity is principally carried out by non-resident entities whose income is not accounted for in Puerto Rico's real gross national product.

The data for employment by sector or industries presented here, like in the United States, are based on the Payroll Survey, which is designed to measure number of payrolls by sector. The Payroll Survey excludes agricultural employment and self-employed persons.

The following table presents annual statistics of average employment based on NAICS for fiscal years 2007 to 2011.

Commonwealth of Puerto Rico
Non-Farm, Payroll Employment by Economic Sector[(1)]
(persons age 16 and over)

	Fiscal Years Ended June 30,				
	2007	**2008**	**2009**	**2010[(2)]**	**2011[(2)]**
Natural resources and construction	64,700	59,675	49,067	35,917	28,683
Manufacturing					
Durable goods	45,417	43,100	39,242	34,792	33,650
Non-durable goods	62,442	60,950	57,483	53,483	50,967
Sub-total	107,858	104,050	96,725	88,275	84,617
Trade, transportation, warehouse, and Utilities					
Wholesale trade	33,267	33,717	33,267	32,533	31,508
Retail trade	133,750	130,883	127,492	126,242	125,217
Transportation, warehouse, and utilities	16,992	16,742	15,692	14,550	14,208
Sub-total	184,008	181,342	176,450	173,325	170,933
Information	22,642	21,442	20,217	18,767	19,067
Finance	49,108	48,483	48,492	45,883	44,717
Professional and business	108,800	108,150	103,333	102,492	107,567
Educational and health	105,225	108,550	109,992	111,108	113,192
Leisure and hospitality	73,567	73,408	70,933	70,850	70,300
Other services	18,242	17,367	16,667	15,750	15,583
Government[(3)]	298,125	297,742	300,708	277,333	263,717
Total non-farm	1,032,275	1,020,208	992,583	939,700	918,375

(1) The figures presented in this table are based on the Payroll Survey prepared by the Bureau of Labor Statistics of the Puerto Rico Department of Labor and Human Resources. There are numerous conceptual and methodological differences between the Household Survey and the Payroll Survey. The Payroll Survey reflects information collected from payroll records of a sample of business establishments, while the Household Survey is based on responses to a series of questions by persons in a sample of households. The Payroll Survey excludes the self-employed and agricultural employment. Totals may not add due to rounding.
(2) Preliminary.
(3) Includes state, local, and federal government employees.

Source: Department of Labor and Human Resources, Current Employment Statistics Survey (Establishment Survey – NAICS Codes)

Manufacturing

Manufacturing is the largest sector of the Puerto Rico economy in terms of gross domestic product and the second largest in terms of real gross national product. The Planning Board figures show that in fiscal year 2010 manufacturing generated $44.6 billion, or 46.4%, of gross domestic product. Manufacturing, however, only generated $15.8 billion, or 24.9%, of real gross national product in fiscal year 2010. During fiscal year 2011, payroll employment for the manufacturing sector was 84,617, a decrease of 4.1% compared with fiscal year 2010. Most of Puerto Rico's manufacturing output is shipped to the U.S. mainland, which is also the principal source of semi-finished manufactured articles on which further manufacturing operations are performed in Puerto Rico. Federal minimum wage laws are applicable in Puerto Rico. For fiscal year 2011, the average hourly manufacturing wage rate in Puerto Rico was approximately 66.6% of the average mainland U.S. rate.

Although the manufacturing sector is less prone to business cycles than the agricultural sector, that does not guarantee the avoidance of the effects of a general downturn of manufacturing on the rest of the economy. In the last three decades, industrial development has tended to be more capital intensive and more dependent on skilled labor. This gradual shift in emphasis is best exemplified by large investments over the last two decades in the pharmaceutical and medical-equipment industries in Puerto Rico. Historically, one of the factors that encouraged the development of the manufacturing sector was the tax incentives offered by the federal and Puerto Rico governments. Federal legislation enacted in 1996, however, which amended Section 936 of the U.S. Internal Revenue Code of 1986, as amended (the "U.S. Code"), phased out these federal tax incentives during a ten-year period that ended in 2006. Moreover, Act 154 expanded the income tax rules as they relate to certain nonresident alien individuals, foreign corporations and foreign partnerships and imposed a new temporary excise tax on persons that purchase products manufactured in Puerto Rico by other persons that are members of the same controlled group. The elimination of the benefits provided by Section 936 of the U.S. Code has had, and Act 154 may have, a long-term impact on local manufacturing activity. See "Tax Incentives—Incentives under the U.S. Code" under THE ECONOMY and "Major Sources of General Fund Revenues—Tax Reform" and "Major Sources of General Fund Revenues—Income Taxes," respectively, under PUERTO RICO TAXES, OTHER REVENUES AND EXPENDITURES.

The following table sets forth gross domestic product by manufacturing sector for fiscal years 2007 to 2010.

Commonwealth of Puerto Rico
Gross Domestic Product by Manufacturing Sector
(at current prices, in thousands)

	Fiscal Years Ended June 30,			
	2007	**2008**	**2009**	**2010[1]**
Food	$1,083,300	$822,008	$ 1,018,486	$ 1,040,339
Beverage and Tobacco Products	924,900	1,243,200	1,197,325	1,203,142
Textile Mills	2,200	1,295	975	791
Textile Product Mills	13,200	13,438	12,072	12,418
Apparel	200,700	252,062	270,251	296,192
Leather and Allied Products	17,000	19,982	22,052	21,997
Wood Products	23,600	22,011	18,809	20,228
Paper	70,600	66,066	66,233	69,664
Printing and Related Support Activities	124,400	118,525	111,416	109,457
Petroleum and Coal Products	370,900	94,986	355,598	353,757
Chemical	27,016,500	29,338,802	31,013,076	31,384,322
Plastics and Rubber Products	121,700	117,556	111,835	119,614
Nonmetallic Mineral Products	284,900	218,469	198,717	197,925
Primary Metals	101,900	150,693	138,708	139,063
Fabricated Metal Products	239,200	247,860	227,572	209,446
Machinery	217,500	234,410	196,456	213,689
Computer and Electronic Products	4,217,200	4,462,560	6,308,916	6,384,137
Magnetic and Optical	-	-	-	-
Electrical Equipment, Appliances and Components	510,900	657,298	639,313	593,777
Transportation Equipment	78,000	77,560	66,111	61,243
Furniture and Related Products	65,500	56,439	47,045	47,761
Miscellaneous	1,955,500	2,018,693	1,998,060	2,162,405
Total gross domestic product of manufacturing sector[2]	$37,636,600	$40,233,913	$44,019,025	$44,641,368

[1] Preliminary.
[2] Totals may not add due to rounding.

Source: Planning Board

The following table presents annual statistics of average manufacturing employment by industry based on NAICS for fiscal years 2007 to 2011.

Commonwealth of Puerto Rico
Non-Farm Payroll Manufacturing Employment by Industry Group*
(persons age 16 years and over)

	Fiscal Years Ended June 30,				
Industry group	**2007**	**2008**	**2009**	**2010[(1)]**	**2011[(1)]**
Durable goods					
Nonmetallic mineral products manufacturing	3,825	3,758	3,058	2,500	2,133
Fabricated metal products	5,675	5,375	4,908	4,042	3,583
Computer and electronic	10,092	8,600	7,042	5,708	5,867
Electrical equipment	6,617	6,658	5,867	5,058	5,033
Miscellaneous manufacturing	12,292	11,967	11,975	11,675	11,400
Other durable goods manufacturing	6,917	6,742	6,392	5,808	5,633
Total – durable goods	45,417	43,100	39,242	34,792	33,650
Non-durable goods					
Food manufacturing	12,183	11,725	11,383	11,592	11,600
Beverage and tobacco products manufacturing	3,258	3,267	3,133	3,275	2,983
Apparel manufacturing	7,708	9,633	9,825	8,808	8,108
Chemical manufacturing	30,467	27,900	25,042	22,392	21,425
Plastics and rubber products	2,200	1,983	1,967	1,867	1,567
Other non-durable goods manufacturing	6,625	6,442	6,133	5,550	5,283
Total – non-durable goods	62,442	60,950	57,483	53,483	50,967
Total manufacturing employment	107,858	104,050	96,725	88,275	84,617

* Totals may not add due to rounding.
(1) Preliminary.

Source: Department of Labor and Human Resources, Current Employment Statistic Survey (Establishment Survey – NAICS Codes)

Total employment in the manufacturing sector decreased by 32,700 from fiscal year 2005 to fiscal year 2011. Manufacturing employment had been declining during the past decade, but the decline accelerated during fiscal years 2002 and 2003, falling 10.6% and 4.8%, respectively. Thereafter, manufacturing employment stabilized around 118,000 jobs, but the acceleration in job losses reappeared in fiscal year 2006 with the sector experiencing another drop of 4.0%. For fiscal years 2007, 2008, 2009, 2010 and 2011, manufacturing employment decreased by 4.2%, 3.5%, 7.0%, 8.7% and 4.1%, respectively. For the first four months of fiscal year 2012, the sector lost an average of 4,800 jobs, or 5.5%, compared to the same period of the previous year. Given that this sector pays, on average, the highest wages in Puerto Rico, its general downturn has represented a major difficulty for restoring growth for the whole economy. There are several reasons that explain this sector's job shrinkage: the end of the phase-out of the tax benefits afforded by Section 936 of the U.S. Code, the net loss of patents on certain pharmaceutical products, the escalation of manufacturing production costs (particularly electricity), the increased use of job outsourcing, and, currently, the effects of the global economic decline. Puerto Rico's manufacturing sector continues to face increased international competition. As patents on pharmaceutical products manufactured in Puerto Rico expire and the production of such patented products is not replaced by new products, there may be additional job losses in this sector and a loss of tax revenues for the Commonwealth.

Service Sector

Puerto Rico has experienced mixed results in the service sector, which, for purposes of the data set forth below, includes wholesale and retail trade, utilities, transportation and warehousing, information, finance and insurance, real estate and rental, and certain services such as professional, scientific, technical, management, administrative, support, educational, health care, social, recreational, accommodation, food and other services. This sector has expanded in terms of income over the past decade, following the general trend of other industrialized economies, but with differences on the magnitudes of those changes. During the period between fiscal years 2007 and 2010, the gross domestic product in this sector, in nominal terms, increased at an average annual rate of 1.1%, while payroll employment in this sector decreased at an average annual rate of 0.9% between fiscal years 2007 and 2011. In the Puerto Rico labor market, self-employment, which is not accounted for in the Payroll Survey, represents approximately 15% of total employment according to the Household Survey. Most of the self-employment is concentrated in the service and construction sectors. The development of the service sector has been positively affected by demand generated by other sectors of the economy, such as manufacturing and construction.

The high degree of knowledge, skills, and expertise in professional and technical services available in Puerto Rico places the island in a favorable competitive position with respect to Latin America and other trading countries throughout the world.

The service sector ranks second to manufacturing in its contribution to gross domestic product, but first in its contribution to real gross national product. The service sector is also the sector with the greatest amount of employment. In fiscal year 2010, the service sector generated $41.5 billion, or 43.1%, of gross domestic product, while it generated $36.3 billion, or 57.3%, of real gross national product. Trade, information services, education and health services, finance, insurance and real estate and rentals experienced growth in fiscal year 2010, as measured by gross domestic product and by gross national product at current prices. Transportation, professional and technical, and management services experienced a contraction in fiscal year 2010, as measured by gross domestic product and gross national product at current prices. Service-sector employment decreased from 561,592 in fiscal year 2007 to 541,358 in fiscal year 2011 (representing 58.9% of total, non-farm, payroll employment). The average service-sector employment for fiscal year 2011 represents a decrease of 0.6% compared to the prior fiscal year. For the first four months of fiscal year 2012, average service-sector employment was 533,900, a decrease of 0.1% with respect to the same period for the prior fiscal year.

Puerto Rico has a developed banking and financial system. As of June 30, 2011, there were eleven commercial banks operating in Puerto Rico. Commercial banks in Puerto Rico are generally regulated by the Federal Deposit Insurance Corporation (the "FDIC") or the Board of Governors of the Federal Reserve System and by the Office of the Commissioner of Financial Institutions of Puerto Rico (the "OCFI"). The OCFI reports that total assets of commercial banks (including assets of units operating as international banking entities) as of June 30, 2011 were $73.7 billion, as compared to $75.5 billion as of December 31, 2010. On April 30, 2010, the OCFI closed three commercial banks and the FDIC was named receiver. On the same date, the FDIC entered into loss share purchase and assumption agreements with three of the other commercial banks with operations in Puerto Rico, providing for the acquisition of most of the assets and liabilities of the closed banks including the assumption of all of the deposits. To date, the amount of jobs lost as a result of these consolidations has not been significant. The administration expects that this consolidation will strengthen the Puerto Rico banking sector.

Broker-dealers in Puerto Rico are regulated by the Financial Industry Regulatory Authority ("FINRA") and the OCFI, and are mainly dedicated to serve investors that are residents of Puerto Rico. According to the OCFI, assets under management by broker-dealers in Puerto Rico totaled $5.5 billion as of June 30, 2011, as compared to $6.0 billion on December 31, 2010. Another relevant component of the financial sector in Puerto Rico is the mutual-fund industry. Local mutual funds are organized as investment companies and recorded assets under management of $14.3 billion as of June 30, 2011, as compared to $14.2 billion as of December 31, 2010 according to the OCFI.

Other components of the financial sector in Puerto Rico include international banking entities ("IBEs") and credit unions (locally known as cooperativas). IBEs are licensed financial businesses that conduct offshore banking transactions. As of June 30, 2011, there were 31 international banking entities (including units of commercial banks) operating in Puerto Rico licensed to conduct offshore banking transactions, with total assets of $43.6 billion, an increase from $40.6 billion in total assets as of December 31, 2010. Meanwhile, credit unions, which tend to provide basic consumer financial services, reached $7.6 billion in assets as of June 30, 2011, a slight increase from $7.5 billion as of December 31, 2010.

In addition, there are specialized players in the local financial industry that include mortgage-origination companies and auto and personal finance companies.

The following table sets forth gross domestic product for the service sector for fiscal years 2007 to 2010.

Commonwealth of Puerto Rico
Gross Domestic Product by Service Sector
(in millions at current prices)

	Fiscal Years ended June 30			
	2007	**2008**	**2009**	**2010[(1)]**
Wholesale trade	$ 2,751.6	$ 2,950.9	$ 2,934.8	$ 2,984.0
Retail trade	4,471.4	4,569.4	4,614.5	4,723.7
Transportation and warehousing	968.3	978.5	908.6	891.0
Utilities	2,214.4	2,118.0	1,971.9	1,943.8
Information	2,466.5	2,363.1	2,306.4	2,359.2
Finance and insurance	6,694.3	7,120.4	5,174.7	5,543.2
Real Estate and rental	11,685.7	12,064.2	13,030.8	13,318.3
Professional and business	3,112.5	3,183.6	3,132.0	3,246.5
Education and health	3,592.5	3,786.2	4,125.7	4,278.5
Leisure and hospitality	1,861.5	1,874.7	1,783.3	1,828.1
Other services	371.6	119.3	112.3	115.9
Total	$40,190.3	$41,371.9	$40,333.2	$41,471.8

Source: Puerto Rico Planning Board

The following table sets forth employment for the service sector for fiscal years 2007 to 2011.

Commonwealth of Puerto Rico
Non-Farm Payroll Employment by Service Sector*
(thousands of persons age 16 and over)

	Fiscal Years Ended June 30,				
	2007	**2008**	**2009**	**2010[(1)]**	**2011[(1)]**
Wholesale trade	33,267	33,717	33,267	32,533	31,508
Retail trade	133,750	130,883	127,492	126,242	125,217
Transportation, warehouse and utilities	16,992	16,742	15,692	14,550	14,208
Information	22,642	21,442	20,217	18,767	19,067
Finance	49,108	48,483	48,492	45,883	44,717
Professional and business	108,800	108,150	103,333	102,492	107,567
Educational and health	105,225	108,550	109,992	111,108	113,192
Leisure and hospitality	73,567	73,408	70,933	70,850	70,300
Other services	18,242	17,367	16,667	15,750	15,583
Total	561,592	558,742	546,083	538,175	541,358

* Totals may not add due to rounding.
(1) Preliminary.

Source: Department of Labor and Human Resources, Benchmark on Employment, Hours and Earnings

Hotels and Related Services—Tourism

For fiscal year 2011, the number of persons registered in tourist hotels, including residents of Puerto Rico and tourists, was 1,906,900, an increase of 5.7% over the number of persons registered during the same period of fiscal year 2010. The average occupancy rate in tourist hotels during fiscal year 2011 was 68.9%, a decrease of 0.3% from the prior fiscal year. Also, during fiscal year 2011, the average number of rooms available in tourist hotels increased by 5.8% to 11,509 rooms compared to the same period of fiscal year 2010.

During the first month of fiscal year 2012, the number of persons registered in tourist hotels, including residents of Puerto Rico and tourists, was 234,200, an increase of 18.4% over the number of persons registered during the same period of fiscal year 2011. The average occupancy rate in tourist hotels during the first month of fiscal year 2012 was 80.2%, a decrease of 0.7% from the prior fiscal year. Also, during the first month of fiscal year 2012, the average number of rooms available in tourist hotels increased by 4.1% to 12,056 rooms compared to the same period of fiscal year 2011.

In terms of employment figures, this sector has shown a behavior consistent with the local business cycle, accentuated by the contraction of U.S. economic activity. For fiscal year 2011, employment in hotels and other lodging facilities increased by 2.3% to 12,700 jobs. Nevertheless, for the first four months of fiscal year 2012, the average decrease in employment in hotels and other lodging facilities was 3.3% as compared to the same period for the prior fiscal year. According to the Payroll Survey, employment in the leisure and hospitality sector was 70,300 for fiscal year 2011, a decrease of 0.8% over employment for fiscal year 2010. For the first four months of fiscal year 2012, employment decreased by 3.2% to 68,800 compared to the same period of the prior fiscal year.

San Juan is the largest homeport for cruise ships in the Caribbean and one of the largest homeports for cruise ships in the world.

Commonwealth of Puerto Rico
Tourism Data[1]

Number of Visitors

Fiscal Years Ended June 30,	Tourist Hotels[2]	Excursionists[3]	Other[4]	Total
2006	1,424,166	1,300,115	2,297,839	5,022,120
2007	1,353,376	1,375,433	2,333,597	5,062,406
2008	1,342,810	1,496,853	2,373,436	5,213,099
2009	1,277,749	1,232,010	2,272,778	4,782,537
2010[5]	1,347,487	1,193,549	2,331,393	4,872,429

Total Visitors' Expenditures
(in millions)

Fiscal Years Ended June 30,	Tourist Hotels[2]	Excursionists[3]	Other[4]	Total
2006	1,537.7	160.9	1,670.7	3,369.3
2007	1,501.6	172.2	1,740.1	3,413.9
2008	1,526.3	194.3	1,814.3	3,535.0
2009	1,464.4	173.7	1,834.8	3,472.8
2010[5]	1,546.1	168.6	1,883.5	3,598.2

(1) Only includes information about non-resident tourists registering in tourist hotels. They are counted once even if registered in more than one hotel.
(2) Includes visitors in guesthouses.
(3) Includes cruise ship visitors and transient military personnel.
(4) Includes visitors in homes of relatives, friends, and in hotel apartments.
(5) Preliminary.

Sources: Puerto Rico Tourism Company and the Planning Board

The Commonwealth, through the Puerto Rico Convention Center District Authority ("PRCDA"), has developed the Dr. Pedro Rosselló González Convention Center, the largest convention center in the Caribbean, and the centerpiece of a 100-acre, private development, that includes hotels, restaurants, office space, and housing. The convention center district is being developed at a total cost of $1.3 billion in a public/private partnership effort to improve Puerto Rico's competitive position in the convention and group-travel segments. The convention center opened on November 17, 2005 and, since its inauguration, the facility has hosted more than 1,000 events accounting for more than 1,000,000 attendees. A 500 room hotel located next to the convention center commenced operations at the end of November 2009.

The PRCDA also owns an 18,500-person capacity multipurpose arena, known as the José Miguel Agrelot Coliseum, located in San Juan, Puerto Rico. The coliseum was inaugurated in 2004 and has hosted more than 2.5 million people attending over 400 world-caliber events. The venue has received numerous awards including "Best International Large Venue of the Year" from Pollstar magazine in 2005.

Government

The government sector of Puerto Rico plays an important role in the economy. It promoted the transformation of Puerto Rico from an agricultural economy to an industrial one during the second half of the previous century, providing the basic infrastructure and services necessary for the modernization of the Island.

In fiscal year 2010, the government (state and local) accounted for \$8.3 billion, or 8.6%, of Puerto Rico's gross domestic product. The government is also a significant employer, employing 248,800 workers (state, including public corporations, and local), or 27.1% of total, non-farm, payroll employment in fiscal year 2011. From fiscal year 2007 to fiscal year 2011, state and municipal government employment averaged approximately 272,300. During fiscal year 2010, state and municipal government employment decreased by 24,800 jobs, or 8.7%. According to the payroll survey, the distribution of the job reductions during fiscal year 2010 was 20,600 jobs in the state government and approximately 4,200 jobs in municipal government. During fiscal year 2011, state and municipal government employment decreased by 11,900 jobs, or 4.6%, compared to fiscal year 2010. According to the payroll survey, the decrease was attributable to a reduction of 12,000 jobs in the state government and an increase of approximately 100 jobs in municipal government. Nevertheless, during the first four months of fiscal year 2012, government employment increased by 2.2% from the previous fiscal year, or by an average of 5,800 jobs. This increase in government employment for the first four months of fiscal year 2012 consists of an average increase of 7,500 jobs, or 4.1%, in state government offset by an average reduction of 1,400 jobs, or 9.0%, and 300 jobs, or 0.5%, in federal and local government, respectively.

As discussed previously, Act 7 established, among other things, a temporary freeze of salary increases and other economic benefits included in laws, collective bargaining agreements, and any other agreements. In addition, Act 7 provided that, for a period of two years after its enactment (until March 9, 2011), collective bargaining agreements that had already expired or that would expire while the law is in effect and that relate to public employees could not be renegotiated or renewed. Act 73 extended the term of the non-economic clauses of such collective bargaining agreements for an additional period of two years (until March 9, 2013) and provided that the economic clauses may be negotiated considering primarily the fiscal condition of the applicable agency and the Government and the safeguarding of services to the people.

Transportation

Thirty-four shipping lines offer regular ocean freight service to eighty United States and foreign ports. San Juan is the island's leading seaport, but there are also seaport facilities at other locations in Puerto Rico including Arecibo, Culebra, Fajardo, Guayama, Guayanilla, Mayagüez, Ponce, Vieques, and Yabucoa.

Puerto Rico's airport facilities are located in Carolina, San Juan, Ponce, Mayaguez, Aguadilla, Arecibo, Ceiba, Vieques, Culebra, and Humacao.

Luis Muñoz Marín International Airport in the San Juan metropolitan area is currently served by 24 domestic and international airlines. The airport receives over 10 million passengers per year, making it the busiest airport in the Caribbean. At present, there is daily direct service between San Juan and Atlanta, Baltimore, Boston, Chicago, Dallas, Miami, New York, Orlando, Philadelphia, and numerous other destinations within the U.S. mainland. San Juan has also become a hub for intra-Caribbean service for a major airline. While the main hubs in the U.S. mainland serve as the gateway from San Juan to most international destinations, Latin American destinations are also served through Panama City, Panama, with connections to Central and South America, while European cities are also served through Madrid, Spain. On December 22, 2009, the Federal Aviation Administration ("FAA") approved the Ports Authority's preliminary application to participate in the FAA's airport public-private partnership pilot program. During fiscal year 2010, the PPP Authority engaged a team of advisors and in June 2010 published the related desirability and convenience study, which is required for the establishment of a public-private partnership. On July 5, 2011 the PPP Authority published its "Request for Qualifications to Acquire a Concession to Finance, Operate, Maintain and Improve the Luis Muñoz Marin International Airport". On August 8, 2011, the PPP Authority and the Puerto Rico Ports Authority received statements of qualifications from twelve (12) world-class consortia and, on September 23, 2011, they published a short-list of six consortia. The PPP Authority issued its Request for Proposals for the Airport in October 2011 and expects to select a winning bidder in the first quarter of calendar 2012.

Regarding other airports, Rafael Hernandez Airport in Aguadilla has regularly scheduled service to and from Fort Lauderdale, New York, Newark and Orlando; and Ponce's Mercedita Airport has regularly scheduled service to and from New York and Orlando. Both of these airports also have scheduled service to other Caribbean islands. Smaller regional airports serve intra-island traffic. Cargo operations are served by both Federal Express and United Parcel Service (UPS) at the airports in San Juan and Aguadilla.

The island's major cities are connected by a modern highway system, which, as of December 31, 2009, totaled approximately 4,636 miles and 12,045 miles of local streets and adjacent roads. The highway system comprises 389 miles of primary system highways, which are the more important interregional traffic routes and include PR-52, PR-22, PR-53, PR-66 and PR-20 toll highways, 230 miles of primary urban system highways, 959 miles of secondary system highways serving the needs of intra-regional traffic, and 3,058 miles of tertiary highways and roads serving local, intra-regional traffic. On September 22, 2011, the PPP Authority and the Highways and Transportation Authority completed the procurement for a concession of toll roads PR-22 and PR-5.

The Port of the Americas is a deep draft container terminal under development on the south coast of Puerto Rico in the City of Ponce, the Commonwealth's fourth largest municipality by population. Managed by the Port of the Americas Authority, the terminal can handle containerized import/export and transshipment cargo. The first phase of the port development was completed in 2004 while the second phase, which resulted in container yard with capacity of up to 250,000 Twenty-Foot Equivalent Units per year, was completed during the first quarter of calendar year 2009. A third development phase, which entails a public investment of $84.4 million, is ongoing through September 2011. The completion of phase three will result in an annual terminal processing capacity of up to 500,000 Twenty-Foot Equivalent Units as well as the installation of basic infrastructure required to develop an industrial value-added zone on land adjacent to the Port.

Construction

Although the construction industry represents a relatively small segment of the economy compared to other sectors, it has made significant contributions to the growth of economic activity due to its multiplier effect on the whole economy. Since its peak in fiscal year 2000, real construction investment has declined at an average annual growth rate of 8.7%. Such rates of interest started to decrease significantly in fiscal year 2005, as a consequence of the current contraction of the local economic activity. During the last four fiscal years (from fiscal year 2007 to 2010) real construction investment decreased at an average annual rate of 17.0%. During the same time period, the total value of construction permits, in current dollars, decreased at an average annual rate of 16.8%. The Planning Board expects a decrease in construction investment of 7.8% in real terms for fiscal year 2011.

Public investment has been an important component of construction investment. During fiscal year 2010, approximately 49.3% of the total investment in construction was related to public projects, which represents an increase in its share of total construction investment compared to 37.9% in fiscal year 2000. Public investment in construction has been negatively affected by the Commonwealth's fiscal difficulties, while private investment in construction is still suffering from the credit conditions that prevailed during the last decade. Public investment was primarily in housing, schools (and school reconstruction programs), water projects, and other public infrastructure projects.

During fiscal year 2010, the number of construction permits decreased 15.2%, while the total value of construction permits dropped by 29.2% compared to fiscal year 2009. During the first six months of fiscal year 2011, the total value of construction permits decreased by 22.6%. These figures are consistent with cement sales, which declined by 26.3% in fiscal year 2010 and by 5.0% in 2011, respectively, reaching levels not seen in almost three decades. During the first three months of fiscal year 2012, cement sales decreased by 3.7% from the previous fiscal year.

Average payroll employment in the construction sector during fiscal year 2011 was 28,700, a reduction of 20.1% from fiscal year 2010. During the first four months of fiscal year 2012, payroll employment in the construction sector averaged 29,100, a further reduction of 5.4% for the same period in fiscal year 2011.

On September 2, 2010, the Governor signed Act 132. Act 132 was designed primarily to stimulate the Puerto Rico real estate market, which in recent years has been suffering from lower sales, rising inventories, falling median prices and increased foreclosure rates. Pursuant to the provisions of Act 132, the Government has provided tax and transaction fee incentives to both purchasers and sellers of new and existing residential properties, as well as commercial properties with sale prices that do not exceed $3 million. The incentives provided by Act 132 were effective from September 1, 2010 through June 30, 2011, and were subsequently extended until October 31, 2011 by Act No. 115 of July 5, 2011. Certain permanent incentives are also available for rental housing. On November 1, 2011, the Government approved Act 216, which provides incentives similar to the ones available under Act 132 and establishes an orderly transition to gradually reduce those incentives without disrupting the functioning of the housing market in Puerto Rico. The incentives provided by Act 216 are limited to residential real property and are effective from November 1, 2011 to December 31, 2012, with certain reductions after December 31, 2011 and June 30, 2012. New incentives are also available for property that constitutes the seller's principal residence, as defined in Act 216.

Agriculture

The Department of Agriculture and related agencies have directed their efforts at increasing and improving local agricultural production, increasing efficiency and the quality of produce, and stimulating the consumption of locally produced agricultural products. It should be noted, however, that agriculture production represents less than 1% of Puerto Rico's gross domestic product. During fiscal year 2010, gross income from agriculture was $822 million, an increase of 3.8% compared with fiscal year 2009.

The administration supports agricultural activities through incentives, subsidies, and technical and support services, in addition to income tax exemptions for qualified income derived by bona fide farmers. Act No. 225 of 1995 provides a 90% income tax exemption for income derived from agricultural operations, grants for investments in qualified agricultural projects, and a 100% exemption from excise taxes, real and personal property taxes, municipal license taxes and tariff payments. It also provides full income tax exemption for interest income from bonds, notes and other debt instruments issued by financial institutions to provide financing to agricultural businesses.

Policy changes have been implemented to promote employment and income generated by the agricultural sector. The policy initiatives include a restructuring of the Department of Agriculture, an increase in government purchases of local agricultural products, new programs geared towards increasing the production and sales of agricultural products, and a new system of agricultural credits and subsidies for new projects.

Higher Education

During the six decades from 1950 to 2010, Puerto Rico made significant advances in the field of education, particularly at the college and graduate-school level. The transformation of Puerto Rico during the 1950s and 1960s from an agricultural economy to an industrial economy brought about an increased demand for educational services at all levels. During the 1970s and 1980s, certain higher-wage, higher-technology industries became more prominent in Puerto Rico. More recently, employment in the service sector has increased significantly. This has resulted in an increased demand for workers having a higher level of education and greater expertise in various technical fields. During the same time period, enrollments in institutions of higher learning rose very rapidly due to growth in the college-age population, and the increasing percentage of college attendance by such population. During the 1990s and into the current decade, college attendance and college attendance as a percentage of the college-age population continued to increase, although the college-age population has declined since 2000.

The following table presents comparative trend data for Puerto Rico and the United States mainland with respect to college-age population and the percentage of such population attending institutions of higher learning.

Commonwealth of Puerto Rico
Trend in College Enrollment

	Commonwealth of Puerto Rico			United States Mainland		
Academic Year	Population 18-24 Years of Age	Higher Education Enrollment	Percent[1]	Population 18-24 Years of Age	Higher Education Enrollment	Percent[1]
1970	341,448[2]	57,340	16.8%	23,714,000[2]	8,580,887	36.2%
1980	397,839[2]	130,105	32.7%	30,022,000[2]	12,096,895	40.3%
1990	417,636[2]	156,147	37.4%	26,961,000[2]	13,818,637	51.3%
2000	428,894[2]	176,015	41.0%	27,141,150[2]	14,791,224	54.5%
2001	430,880[3]	184,126	42.7%	27,992,652[3]	15,312,289	54.7%
2002	428,065[3]	190,776	44.6%	28,480,708[3]	15,927,987	55.9%
2003	423,338[3]	199,842	47.2%	28,916,746[3]	16,611,711	57.4%
2004	417,141[3]	206,791	49.6%	29,302,179[3]	16,911,481	57.7%
2005	408,044[3]	208,032	51.0%	29,441,546[3]	17,272,044	58.7%
2006	398,586[3]	209,547	52.6%	29,602,839[3]	17,487,475	59.1%
2007	389,640[3]	225,402	57.8%	29,808,025[3]	17,758,870	59.6%
2008	384,751[3]	227,546	59.1%	30,194,274[3]	18,248,128	60.4%
2009	379,500[3]	235,618	62.1%	30,530,346[3]	19,102,814	62.6%
2010	375,145[2]	249,372	66.5%	30,672,088[2]	20,427,711	66.6%

(1) Number of persons of all ages enrolled in institutions of higher education as percent of population 18-24 years of age.
(2) Based on census population as of April 1 of the stated year.
(3) Estimated population (reference date July 1 of the stated year).

Sources: U.S. Census Bureau (U.S. Mainland Population), U.S. National Center for Education Statistics (NCES), Planning Board (Puerto Rico Population) and Council on Higher Education of Puerto Rico

The University of Puerto Rico, the only public university in Puerto Rico, has eleven campuses located throughout the island. The University's total enrollment for academic year 2010-2011 was approximately 61,630 students. The Commonwealth appropriates annually for the University of Puerto Rico an amount equal to 9.60% of the average annual revenue from internal sources (subject to certain exceptions) for each of the two fiscal years immediately preceding the current fiscal year.

In addition to the University of Puerto Rico, there are 40 public and private institutions of higher education located in Puerto Rico. Such institutions had an enrollment during academic year 2009-2010 of approximately 183,673 students and provide programs of study in liberal arts, education, business, natural sciences, technology, secretarial and computer sciences, nursing, medicine, and law. Degrees are offered by these institutions at the associate, bachelor, master, and doctoral levels.

Institutions providing education in Puerto Rico must satisfy state licensing requirements to operate. Also, the vast majority of educational institutions are accredited by U.S. Department of Education-recognized accrediting entities.

Tax Incentives

One factor that has promoted and continues to promote the development of the manufacturing and service sector in Puerto Rico is the various local and federal tax incentives available, particularly those under Puerto Rico's Industrial Incentives Program and, until 2006, Sections 30A and 936 of the U.S. Code. Tax and other incentives have also been established to promote the development of the tourism industry. These incentives are summarized below.

Industrial Incentives Program

Since 1948, Puerto Rico has had various incentives laws designed to promote investment and job creation. Under these laws, companies engaged in manufacturing and certain other designated activities were eligible to receive full or partial exemption from income, property, and other local taxes. The most recent of these incentives laws is the Economic Incentives Act, enacted in May 2008.

The benefits provided by the Economic Incentives Act are available to new companies as well as companies currently conducting tax-exempt operations in Puerto Rico that choose to renegotiate their existing tax exemption grants, expand current operations or commence operating a new eligible business. The activities eligible for tax exemption under the Economic Incentives Act include manufacturing, certain designated services performed for markets outside Puerto Rico (including the United States), the production of energy from local renewable sources for consumption in Puerto Rico and laboratories for research and development. The Economic Incentives Act expands the definition of eligible business from that included in Act No. 135 of December 2, 1997, as amended (the "1998 Tax Incentives Act"), to include clusters and supply chains.

Companies qualifying under the Economic Incentives Act can benefit from a simplified income tax system: in most cases, an income tax rate of 4% and a withholding tax rate of 12% on royalty payments. Alternatively, the income tax rate can be 8% and a withholding rate of 2% on royalty payments. Special rates apply to projects located in low and mid-development zones (an income tax reduction of 0.5%), certain local projects (an income tax rate as low as 3%), certain small- and medium-sized businesses (an income tax rate as low as 1%) and pioneering activities (an income tax rate of 1%, but for those using intangible property created or developed in Puerto Rico the income tax rate may be 0%). In addition, as with the 1998 Tax Incentives Act, the Economic Incentives Act grants 90% exemption from property taxes, 100% exemption from municipal license taxes during the first three semesters of operations and at least 60% thereafter, and 100% exemption from excise taxes, and sales and use taxes with respect to the acquisition of raw materials and certain machinery and equipment used in the exempt activities.

The Economic Incentives Act is designed to stimulate employment and productivity, research and development, capital investment, reduction in the cost of energy and increased purchase of local products.

Under the Economic Incentives Act, as with the 1998 Tax Incentives Act, companies can repatriate or distribute their profits free of Puerto Rico dividend taxes. In addition, passive income derived by exempted businesses from the investment of eligible funds in Puerto Rico financial institutions, obligations of the Commonwealth, and other designated investments is fully exempt from income and municipal license taxes. Gain from the sale or exchange of shares or substantially all the assets of an exempted business during the exemption period that is otherwise subject to Puerto Rico income tax would be subject to a special Puerto Rico income tax rate of 4%.

The Economic Incentives Act, like the 1998 Tax Incentives Act, also provides investors that acquire an exempted business that is in the process of closing its operations in Puerto Rico a 50% credit in connection with the cash purchase of such corporation's stocks or operational assets.

Green Energy Incentives Program

On July 19, 2010 the Legislative Assembly enacted Act No. 83 of July 19, 2010, also known as the "Green Energy Incentives Act", to encourage the production of renewable energy on a commercial scale. The activities eligible for tax exemption under the Green Energy Incentives Act include businesses engaged in the production and sale of green energy on a commercial scale for consumption in Puerto Rico, a producer of green energy, the installation of machinery and equipment for the production of green energy, and property used for the production of green energy.

Companies qualifying under the Green Energy Incentives Act can benefit from a simplified income tax system: an income tax rate of 4% and a withholding tax rate of 12% on royalty payments, license fees and rental payments to non-Puerto Rico resident companies. In addition, Green Energy Incentives Act grants 90% exemption from property taxes, 100% exemption from municipal license taxes during the first three semesters of operations and at least 60% thereafter, and 100% exemption from excise taxes, and sale and use taxes with respect to the acquisition of raw materials and certain machinery and equipment used in the exempt activities.

Under the Green Energy Incentives Act, companies can repatriate or distribute their profits free of Puerto Rico dividend taxes. Gain from the sale or exchange of shares or substantially all the assets of an exempted business during the exemption period that is otherwise subject to Puerto Rico income tax would be subject to a special Puerto Rico income tax rate of 4%. Moreover, the Green Energy Incentives Act creates a rebate program of up to 6% of the acquisition, installation, and related costs of the physical plant and the machinery and equipment of small and medium green energy projects located in Puerto Rico. In the case of large scale green energy projects developed in Puerto Rico, the Green Energy Incentives Act creates a renewal green energy certificates program.

Tourism Incentives Program

For many years, Puerto Rico has enacted incentives laws designed to stimulate investment in hotel operations on the island. The Puerto Rico Tourism Development Act of 2010 (the "Tourism Development Act") provides partial exemptions from income, property, and municipal license taxes for a period of ten years. The Tourism Development Act also provides certain tax credits for qualifying investments in tourism activities, including hotel and condo-hotel development projects. The Tourism Development Act provides further tourism incentives by granting tax exemption on interest income, fees and other charges received with respect to bonds, notes, or other obligations issued by tourism businesses for the development, construction, rehabilitation, or improvements of tourism projects.

As part of the incentives to promote the tourism industry, in 1993 the Commonwealth established the Tourism Development Fund as a subsidiary of GDB with the authority to (i) make investments in or provide financing to entities that contribute to the development of the tourism industry and (ii) provide financial guarantees and direct loans for financing tourism development projects. To date, the Fund has provided direct loans and financial guarantees in the aggregate of approximately $1.368 billion for loans made or bonds issued to finance the development of twenty-one tourism projects representing 4,744 new hotel rooms and a total investment of approximately $2.135 billion.

Treatment of Puerto Rico Corporations under the U.S. Code - Controlled Foreign Corporations

As a result of the modification and phase-out of the federal tax incentives under Section 936 of the U.S. Code, many corporations previously operating thereunder reorganized their operations in Puerto Rico to become controlled foreign corporations ("CFCs"). A CFC is a corporation that is organized outside the United States (including, for these purposes, in Puerto Rico) and is controlled by United States shareholders. In general, a CFC may defer the payment of federal income taxes on its trade or business income until such income is repatriated to the United States in the form of dividends or through investments in certain United States properties. The Puerto Rico Office of Industrial Tax Exemption has received notification from numerous corporations that have converted part or all of their operations to CFCs. These include most of the major pharmaceutical, instrument and electronics manufacturing companies in Puerto Rico.

CFCs operate under transfer pricing rules for intangible income that are different from those applicable to United States corporations operating under Section 936 of the U.S. Code ("Section 936 Corporations"). In many cases, they are allowed to attribute a larger share of this income to their Puerto Rico operation but must make a royalty payment "commensurate with income" to their U.S. affiliates. Section 936 Corporations were exempted from Puerto Rico withholding taxes on any cost-sharing payments they might have opted to make, but CFCs are subject to a 15% Puerto Rico withholding tax on royalty payments, unless they have a renegotiated Puerto Rico tax grant issued under the Economic Act in which case this withholding tax could be lowered to 2% or 12%.

In May 2009, the U.S. Department of the Treasury announced proposed changes to the U.S. Code that include, among others, changes to remove incentives for shifting jobs overseas. Several of these initiatives could affect CFCs operating in Puerto Rico. As of this date, no legislation has been approved by either House of Congress of the United States. It is not possible at this time to determine the legislative changes that may be made to the U.S. Code, or their effect on the long-term outlook on the economy of Puerto Rico. The administration will develop policy responses to the U.S. government to seek to safeguard Puerto Rico's economic reconstruction and development plans.

On September 22, 2011, HR No. 3020 was presented in the U.S. Congress House of Representatives, which allows corporations organized under the laws of Puerto Rico which derive fifty percent (50%) or more of their gross income from Puerto Rico sources to elect to be treated as domestic U.S. corporations for almost all provisions of the U.S. Code, including Section 243 of the U.S. Code pertaining to the dividends received deduction. By way of exception, the electing Puerto Rico corporations would not consider as part of their gross income for federal income tax purposes income derived from sources within Puerto Rico.

DEBT

Public Sector Debt

Public sector debt comprises bonds and notes of the Commonwealth, its municipalities, and public corporations ("notes" as used in this section refers to certain types of non-bonded debt regardless of maturity), subject to the exclusions described below.

Section 2 of Article VI of the Constitution of the Commonwealth provides that direct obligations of the Commonwealth evidenced by full faith and credit bonds or notes shall not be issued if the amount of the principal of and interest on such bonds and notes and on all such bonds and notes theretofore issued that is payable in any fiscal year, together with any amount paid by the Commonwealth in the fiscal year preceding the fiscal year of such proposed issuance on account of bonds or notes guaranteed by the Commonwealth, exceed 15% of the average annual revenues raised under the provisions of Commonwealth legislation and deposited into the treasury (hereinafter "internal revenues") in the two fiscal years preceding the fiscal year of such proposed issuance. Section 2 of Article VI does not limit the amount of debt that the Commonwealth may guarantee so long as the 15% limitation is not exceeded through payments by the Commonwealth on such guaranteed debt. Internal revenues consist principally of income taxes, property taxes, sales taxes and excise taxes. Certain revenues, such as federal excise taxes on offshore shipments of alcoholic beverages and tobacco products and customs duties, which are collected by the United States Government and returned to the Treasury Department, and motor vehicle fuel taxes, crude oil and derivative products excise taxes and license fees, which are allocated to the Highway and Transportation Authority, are not included as internal revenues for the purpose of calculating the debt limit, although they may be available for the payment of debt service. In addition, the portion of the Sales Tax (as defined under "Major Sources of General Fund Revenues—Sales and Use Taxes" under "Puerto Rico Taxes, Other Revenues, and Expenditures" below) allocated to COFINA is not included as internal revenues since the legislation that created COFINA transferred ownership of such portion of the Sales Tax to COFINA and provided that such portion was not "available resources" under the Constitutional provisions relating to full faith and credit bonds.

As of September 30, 2011, future maximum annual debt service for the Commonwealth's outstanding general obligation debt is $981,295,893 in the fiscal year ending June 30, 2015 (based on the assumption that the (i) Public Improvement Refunding Bonds, Series 2004A, which are variable rate bonds, bear interest at their actual rate per annum through July 1, 2012 and thereafter at 12% per annum, (ii) Public Improvement Refunding Bonds, Series 2004B, which are variable rate bonds, bear interest at 12% per annum, and (iii) the outstanding Public Improvement Refunding Bonds, Series 2003 C, Public Improvement Bonds of 2006, Series A, Public Improvement Refunding Bonds, Series 2007A and Public Improvement Refunding Bonds, Series 2011B that are variable rate bonds, bear interest at 12% per annum). This amount ($981,295,893) *plus* the amount paid by the Commonwealth in fiscal year 2011 on account of bonds or notes guaranteed by the Commonwealth ($16,520,000), for a total of $997,815,893, is equal to 13.13% of $7,600,369,000, which is the average of the adjusted internal revenues for the fiscal years ended June 30, 2010 and the preliminary internal revenues for the fiscal year ended June 30, 2011. If the interest on the outstanding bonds described in items (ii) through (iii) above was calculated using the effective fixed interest rate payable by the Commonwealth under the interest rate exchange agreements entered into in respect thereof, the future maximum annual debt service for the Commonwealth outstanding general obligations debt would be $883,909,051 in fiscal year 2020 and the percentage referred to in the preceding sentence would be 11.85%. The potential termination payment (which is a full faith and credit obligation of the Commonwealth) payable by the Commonwealth (based on the then applicable mark-to-market value) upon termination of the above mentioned swap agreements is not included in the calculation of the 15% constitutional debt limitation. For a discussion of the Commonwealth's obligations under its interest rate exchange agreements, see "Interest Rate Exchange Agreements" under DEBT.

Except as set forth below, annual debt service payments on bonds guaranteed by the Commonwealth are not included in the calculation of the 15% debt limitation. In the event any of the public corporations issuers of guaranteed bonds are unable to make any portion of the future debt service payments on its guaranteed bonds, the Commonwealth would be required to make such payments under its guarantee from the General Fund, and such debt service would be included in the calculation of the 15% constitutional debt limitation.

As of June 30, 2011, Port of the Americas Authority ("PAA") had outstanding bonds guaranteed by the Commonwealth (the "PAA Guaranteed Bonds"), representing a $250 million GDB financing with an outstanding principal amount of $214.5 million. The Commonwealth has begun to make payments of debt service on the PAA Guaranteed Bonds and expects to make all payment on the PAA Guaranteed Bonds under the full faith and credit guarantee of the Commonwealth. During fiscal year 2011, the Commonwealth made payments under its guaranty of the PAA Guaranteed Bonds of $16.5 million. In addition, the Commonwealth had made special budgetary appropriations to Puerto Rico Aqueduct and Sewer Authority ("PRASA") to provide a subsidy for its operational expenses. See "Commonwealth Guaranteed Debt" below.

The Commonwealth's policy has been and continues to be to prudently manage such debt within the constitutional limitation. Debt of municipalities, other than bond anticipation notes, is supported by real and personal property taxes and municipal license taxes. Debt of public corporations, other than bond anticipation notes, is generally supported by the revenues of such corporations from rates charged for services or products. See "Public Corporations." However, certain debt of public corporations is supported, in whole or in part, directly or indirectly, by Commonwealth appropriations or taxes.

Direct debt of the Commonwealth is issued pursuant to specific legislation approved in each particular case. Debt of the municipalities is issued pursuant to ordinances adopted by the respective municipal legislatures. Debt of public corporations is issued in accordance with their enabling statutes. GDB, as fiscal agent of the Commonwealth and its municipalities and public corporations, must approve the specific terms of each issuance.

The following table presents a summary of public sector debt as of June 30, 2011. This table includes debt not primarily payable from either Commonwealth or municipal taxes, Commonwealth appropriations or rates charged by public corporations for services or products, some of which debt is set forth in footnote 6 below. Excluded from the table is debt the inclusion of which would reflect double counting including, but not limited to, \$1.1 billion of outstanding bonds (as of June 30, 2011) issued by Municipal Finance Agency to finance its purchase of bonds of Puerto Rico municipalities, and \$1.6 billion of obligations of Public Finance Corporation issued to purchase certain Commonwealth public sector debt.

Commonwealth of Puerto Rico
Public Sector Debt*
(in millions)

	June 30, 2011	**September 30, 2011**
GENERAL FUND RELATED DEBT		
Direct full faith and credit obligations	\$ 9,682	\$ 9,772
Puerto Rico guaranteed debt(1)	4,296	5,312
Debt supported by Puerto Rico appropriations or taxes(2)	3,840	3,880
Tax and Revenue Anticipation Notes(3)	-	650
Pension Obligation Bonds(4)	2,948	2,948
TOTAL GENERAL FUND RELATED DEBT	\$20,766	\$22,562
Sales Tax debt	\$13,765	\$13,765
Public corporations and agencies(5)	24,064	23,151
Municipal debt	3,537	3,400
Limited obligations/non-recourse debt(6)	2,389	2,384
TOTAL PUBLIC SECTOR DEBT	\$64,521	\$65,262

* Totals may not add due to rounding.

(1) Consists of \$598 million of bonds issued by Aqueduct and Sewer Authority (September 30 - \$666 million), \$413 million of State Revolving Fund Loans incurred under various federal water laws (September 30 - \$423 million), \$214.5 million of bonds issued by Port of the Americas Authority (September 30 - \$212 million) and \$3.070 billion of PBA bonds (September 30 – \$4.012 billion). Excludes \$267 million of GDB bonds payable from available moneys of GDB.

(2) Represents bonds and notes payable from the Commonwealth General Fund and Public Improvement Fund. Includes Public Finance Corporation.

(3) Includes related short-term financings.

(4) Represents Senior Pension Funding Bonds, Series A, B, and C issued by the Employees Retirement System, which are payable solely from employer contributions made to the Employees Retirement System by the Commonwealth and its instrumentalities after the issuance of the bonds.

(5) Excludes \$5.4 billion of notes issued by GDB, the proceeds of which have been principally used to fund loans to the Commonwealth, public corporations, agencies and municipalities. Loans made by GDB to the Commonwealth, public corporations, agencies and municipalities are included the table.

(6) Includes the following: \$1.3 billion of Children's Trust bonds, which are payable solely from the payments to be received pursuant to the tobacco litigation settlement; \$180 million of Housing Finance Authority bonds, which are payable from Puerto Rico Housing Administration's annual allocation of Public Housing Capital Funds from the United States Department of Housing and Urban Development; \$343.8 million of Capital Fund Modernization Program Subordinate Bonds, Series 2008, and \$100 million of Housing Revenue Bonds, Series 2008, issued the Puerto Rico Housing Finance Authority; \$151.0 million of Special Facilities Revenue Bonds issued by Highways and Transportation Authority, which are payable from net toll revenues collected from the Teodoro Moscoso Bridge (September 30 - \$149.1 million); \$155 million of Special Facilities Bonds issued by Ports Authority, which are solely payable from the pledge of certain payments made by a private corporation under a special facilities agreement; \$76.3 million of Educational Facilities Revenue Bonds, 2000 Series A (University Plaza Project) issued by Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority ("AFICA"), which are payable from rent payments made by the University of Puerto Rico (September 30- \$74.6 million); and approximately \$74.7 million of bonds issued by AFICA to finance the construction of various government infrastructure projects, which are payable from rent payments made by various government entities (September 30 - \$73.5 million).

Source: Government Development Bank for Puerto Rico

No deductions have been made in the table above for deposits on hand in debt service funds and debt service reserve funds. The table above and the amounts shown throughout this section as representing outstanding debt include outstanding capital appreciation bonds at their respective original principal amounts and do not include any accretion thereon.

Debt Service Requirements for Commonwealth General Obligation Bonds

The following table presents the debt service requirements for Commonwealth general obligation bonds outstanding on September 30, 2011. This table, however, does not include payments made by the Commonwealth on the PAA Guaranteed Bonds, which are paid from General Fund budgetary appropriations determined in consultation with GDB, as holder of the PAA Guaranteed Bonds. The amounts paid by the Commonwealth under the PAA Guaranteed Bonds for the prior fiscal year, however, are taken into account in the determination of the constitutional debt limit.

In addition, in respect of certain variable rate general obligation bonds, as to which the Commonwealth has entered into interest rate exchange agreements, the interest in the table is calculated by using the respective fixed rates of interest that the Commonwealth is paying under said agreements.

Debt service requirements for each fiscal year, as shown in the following table, include principal and interest due on July 1 immediately following the close of such fiscal year.

Puerto Rico General Obligation Debt Service Requirements*
(In thousands)

Fiscal Year Ending June 30	Outstanding Bonds Principal	Interest	Total
2012	$ 362,335	$ 485,097	$ 847,432
2013	387,005	463,523	850,528
2014	374,613	463,433	838,045
2015	406,765	445,356	852,120
2016	426,790	425,183	851,974
2017	373,392	404,247	777,638
2018	376,110	385,632	761,742
2019	479,356	351,250	830,606
2020	546,400	319,314	865,714
2021	421,540	292,069	713,609
2022	351,420	272,147	623,567
2023	321,255	255,411	576,666
2024	336,215	240,754	576,969
2025	340,610	224,910	565,520
2026	349,280	207,339	556,619
2027	367,005	189,618	556,623
2028	386,340	170,197	556,537
2029	339,095	150,748	489,843
2030	352,240	134,726	486,966
2031	371,395	117,908	489,303
2032	224,545	99,992	324,537
2033	163,245	87,491	250,736
2034	172,615	79,028	251,643
2035	233,700	70,813	304,513
2036	247,115	57,394	304,509
2037	256,790	42,777	299,567
2038	160,675	27,854	188,529
2039	170,105	18,421	188,526
2040	130,450	8,215	138,665
	$9,428,400	$6,490,846	$15,919,246

* Totals may not add due to rounding. Includes the effective fixed rate on certain variable rate general obligation bonds as to which the Commonwealth has entered into interest rate exchange agreements.

Sources: Government Development Bank for Puerto Rico and Treasury Department

Interest Rate Exchange Agreements

General. The Commonwealth and various public corporations are party to various interest rate exchange agreements or swaps. Except for the basis swaps discussed below, the purpose of all of the interest rate exchange agreements currently in place is to hedge the Commonwealth's variable rate debt exposure and the interest rate risks associated therewith. When the Commonwealth or a public corporation has issued variable rate bonds, it has entered into an interest rate exchange agreement with a counterparty pursuant to which the Commonwealth or the public corporation agrees to pay the counterparty a fixed rate and the counterparty agrees to pay the Commonwealth or public corporation a variable rate intended to match the variable rate payable on the bonds (a "synthetic fixed rate swap"). In theory, the variable rate payments received by the Commonwealth under the swap off-set the variable rate payments on the bonds and, thus, the Commonwealth or the public corporation is left with a net fixed rate payment to a counterparty. The intention of these swaps was to lower the all-in cost of borrowing below what could have been achieved by issuing fixed rate bonds.

Basis Swap. The Commonwealth and the Puerto Rico Electric Power Authority ("PREPA") are also party to agreements ("basis swaps"), entered into in June 2006 and March 2008, respectively, pursuant to which they are making payments on a specified notional amount based on a short-term interest rate index published by the Securities Industry and Financial Markets Association ("SIFMA") and are receiving from their counterparties payments on the same notional amount based on the published three-month London Interbank Offered Rate ("LIBOR") plus a specified fixed rate payment (the "basis annuity"). The basis swaps are the only interest rate exchange agreements that do not hedge specific variable rate debt. For fiscal year 2011 and the first three months of fiscal year 2012, the Commonwealth received $7.3 million and $2.0 million, respectively, from its counterparties under the basis swap, net of the Commonwealth's payments to the counterparties, and PREPA received $9.6 million and $2.7 million, respectively, from its counterparty under the basis swap, net of PREPA's payments to the counterparty.

Risks. By using derivative financial instruments, the Commonwealth exposes itself, among other risks, to credit risk (based on the counterparty's ability to perform under the terms of the agreement), market risk (based on the changes in the value of the instrument resulting from changes in interest rates and other market factors) and, in the case of basis swaps, basis risk (based on changes to the correlation between different indexes used in connection with a derivative and the variable rate debt they hedge). GDB, as fiscal agent, regularly monitors the exposure of the Commonwealth and the public corporations under the interest rate exchange agreements and attempts to minimize the risks. To minimize some of the credit risk, the Commonwealth and the public corporations enter into agreements with highly-rated counterparties. The outstanding interest rate exchange agreements are with eleven different counterparties, all of which are rated in one of the three highest rating categories by either Moody's or S&P. In addition, most of the agreements contain requirements of posting collateral by the counterparties based on certain valuation thresholds and credit ratings.

During fiscal years 2009, 2010 and 2011, in order to reduce the risks associated with the swaps portfolio, the Commonwealth and the public corporations terminated approximately $2.5 billion of swaps. The aggregate notional amount of the swaps for the Commonwealth and the public corporations has decreased from $9.2 billion as of June 30, 2008, to $6.7 billion as of September 30, 2011, an aggregate decrease of 27.2%.

Notional Amounts. The table below shows the aggregate notional amount as of September 30, 2011 of synthetic fixed rate swaps and basis swaps of the Commonwealth and the public corporations.

Swap Portfolio Breakdown
Notional Amount
(as of September 30, 2011)

	Synthetic Fixed	Basis Swaps	Total
Commonwealth (General Obligation)	$1,093,825,000	$1,698,370,000	$2,792,195,000
Electric Power Authority	411,825,000	1,375,000,000	1,786,825,000
Highways and Transportation Authority	647,025,000	—	647,025,000
Ports Authority	411,705,000	—	411,705,000
Sales Tax Financing Corporation	1,043,000,000	—	1,043,000,000
Total	$3,607,380,000	$3,073,370,000	$6,680,750,000

Market Value. Generally, the interest rate exchange agreements may be terminated by the Commonwealth or the public corporations at any time at their then current market values. The agreements may also be terminated upon the occurrence of certain credit events. If a termination occurs due to a credit event, the Commonwealth or the public corporations may be obligated to pay to the applicable swap counterparty an amount based on the terminating swap's market value, which may be substantial, or vice versa, with other termination costs being paid by the defaulting party. The mark-to-market value of the swaps fluctuates with interest rates and other market conditions. The Commonwealth's obligations under the interest rate exchange agreements are secured by the full faith, credit and taxing power of the Commonwealth.

The following table shows, as of September 30, 2011, the net mark-to-market value of all outstanding interest rate exchange agreements. The mark-to-market value of all swaps of the Commonwealth and the public corporations was negative as of September 30, 2011. Thus, the Commonwealth or the public corporations, as applicable, would owe money to the counterparties if any of the agreements had been terminated as of that date.

Swap Portfolio Mark-to-Market Valuation
(as of September 30, 2011)

	Synthetic Fixed	Basis Swaps	Total
Commonwealth (General Obligation)	$(241,139,564)	$(61,486,467)	$(302,626,031)
Electric Power Authority	(98,911,332)	(13,668,641)	(112,579,973)
Highways and Transportation Authority	(208,821,840)	—	(208,821,840)
Ports Authority	(62,729,312)	—	(62,729,312)
Sales Tax Financing Corporation	(467,132,322)	—	(467,132,322)
Total	$(1,078,734,370)	$(75,155,108)	$(1,153,889,478)

Collateral Requirements. Under the majority of the interest rate exchange agreements, the Commonwealth and the public corporations are required to deliver collateral to the counterparties to guarantee their performance under the agreements based on the credit ratings of the Commonwealth and the public corporations and certain contractual mark-to-market value thresholds. During the fourth quarter of 2008, as a result of the U.S. financial market crisis, the Commonwealth and the public corporations were required to post collateral of approximately $251.8 million and $82.5 million, respectively, to their counterparties on certain interest rate exchange agreements. Based on an improvement in the mark-to-market value of the swap portfolio since then, the Commonwealth and the public corporations had posted collateral of $4.0

million and $66.6 million, respectively, as of September 30, 2011. However, if the mark-to-market value of the swaps portfolio deteriorates or the credit ratings of the Commonwealth or the public corporations are lowered, the collateral posting obligations contained in the agreements may require further deliveries of collateral.

Variable Rate Bonds and Mandatory Tender Bonds

Variable Rate Bonds. The Commonwealth and various public corporations have outstanding variable rate bonds, consisting of (1) variable rate demand bonds which are subject to mandatory tender for purchase prior to their maturity on certain interest rate reset dates and upon expiration of an associated credit or liquidity facility ("VRDO Bonds"), (2) variable rate bonds and notes that have been purchased directly from the Commonwealth by certain financial institutions where the interest rate changes periodically based on the LIBOR or SIFMA index and that are subject to mandatory tender on certain dates prior to their maturities ("Mandatory Tender FRNs"), and (3) other bonds and notes where the interest rate changes periodically based on the LIBOR rate or a particular index but that are not subject to tender prior to their maturity. The Commonwealth and the public corporations have hedged their variable rate debt exposure by entering into interest rate exchange agreements with certain swap providers with respect to all variable rate bonds. Pursuant to these agreements, the Commonwealth and the public corporations receive a variable rate payment expected to approximate the interest cost of the variable rate bonds, and pay a fixed rate. See "Interest Rate Exchange Agreements."

The following table shows the breakdown of variable rate debt of the Commonwealth and the public corporations as of September 30, 2011.

Variable Rate Debt Breakdown
(as of September 30, 2011)

	VRDO Bonds	Mandatory Tender FRNs	Other Variable Rate Debt	Total
Commonwealth (General Obligation)	$288,160,000	$609,775,000	$ 126,725,000	$1,024,660,000
Electric Power Authority	—	—	411,825,000	411,825,000
Highways and Transportation Authority	200,000,000	—	447,025,000	647,025,000
Ports Authority	—	—	411,705,000	411,705,000
Sales Tax Financing Corporation	—	—	136,000,000	136,000,000
Total	$488,160,000	$609,775,000	$1,533,280,000	$2,631,215,000

The VRDO Bonds bear a floating interest rate adjusted at specified intervals, such as daily or weekly (each, a "remarketing date") and provide investors the option to tender or put the bonds at par on each remarketing date. The tendered bonds are then resold by a remarketing agent in the secondary market to other investors. Most of the VRDO Bonds are secured by letters of credit or other liquidity or credit facilities ("credit/liquidity facilities") that provide for the payment of the purchase price payable upon the tender of the bonds. The credit/liquidity facilities expire prior to the final maturity of the bonds. If, upon the expiration or termination of any credit/liquidity facility with respect to a series of VRDO Bonds, the Commonwealth or the applicable public corporation is unable to renew or replace such facility with an alternate credit/liquidity facility, the VRDO Bonds of such series are subject to mandatory tender for purchase by the credit/liquidity facility provider and generally become subject to higher interest rates and accelerated amortization schedules pursuant to the terms of each expiring credit/liquidity facility.

The recent U.S. financial market crisis has resulted in a significant reduction in the availability of credit/liquidity facilities to support VRDO Bonds, and a related increase in the price of these facilities when they can be obtained. Thus, if the Commonwealth and the public corporations are not able to renew or rollover the expiring credit/liquidity facilities with respect to VRDO Bonds, or are not able to do so at an acceptable price, the Commonwealth and the public corporations would have to refinance the VRDO Bonds or otherwise obtain financing for such bonds in order to avoid the higher interest rates and accelerated amortization schedules set forth in the expiring credit/liquidity facility.

In addition, since there are interest rate exchange agreements with respect to all VRDO Bonds, if the Commonwealth or the applicable public corporation cannot renew or replace a credit/liquidity facility upon its expiration or remarket the related series of bonds successfully upon their mandatory tender as variable rate bonds, the Commonwealth or the applicable public corporation may have to terminate the interest rate exchange agreements associated with such series of VRDO Bonds. Termination of the applicable interest rate exchange agreement may result, depending on then current interest rate levels and market conditions, in the payment of a termination amount, which may be substantial, by the Commonwealth to compensate the counterparty for its economic losses. As of September 30, 2011, the mark-to-market value of all the interest rate exchange agreements with respect to VRDO Bonds was negative $64.3 million for the Commonwealth and negative $52.0 million for the public corporations. See "Interest Rate Exchange Agreements – Market Value."

The following table shows, by fiscal year, the amount of VRDO Bonds subject to mandatory tender upon expiration of the applicable credit/liquidity facilities.

VRDO Bonds Rollover
(by Fiscal Year)

	2012	2013	Total
Commonwealth (General Obligation)	—	$288,160,000	$288,160,000
Highways and Transportation Authority	—	200,000,000	200,000,000
Total	—	$488,160,000	$488,160,000

The Mandatory Tender FRNs are discussed in the "Mandatory Tender Bonds" section below.

Mandatory Tender Bonds. As of September 30, 2011, the Commonwealth and the public corporations also had outstanding $609.8 million of Mandatory Tender FRNs and $1.7 billion of fixed rate bonds also subject to mandatory tender for purchase prior to maturity (collectively, the "Mandatory Tender Bonds"). The Commonwealth and the public corporations have not provided any liquidity facility for the payment of the purchase price payable upon the mandatory tender, which purchase price is expected to be obtained from the remarketing of the bonds. If the Commonwealth or the applicable public corporation cannot remarket the Mandatory Tender

Bonds, they would have to obtain other funds in order to provide for the purchase price of these bonds or, in some cases, the bonds would become subject to higher interest rates and an accelerated amortization schedule.

The following table shows, as of September 30, 2011, the breakdown of the Mandatory Tender Bonds of the Commonwealth and the public corporations and the respective dates when such bonds are subject to mandatory tender for purchase.

Mandatory Tender Bonds Breakdown
(as of September 30, 2011)

	Mandatory Tender Bonds	Type	Mandatory Tender Date
Commonwealth (General Obligation)	$279,240,000	Fixed	July 1, 2012
	67,650,000	Variable	March 1, 2013
	141,450,000	Variable	April 1, 2013
	203,290,000	Variable	May 1, 2013
	197,385,000	Variable	June 1, 2014
Public Finance Corporation	963,050,000	Fixed	February 1, 2012
Public Buildings Authority	335,580,000	Fixed	July 1, 2012
	129,300,000	Fixed	July 1, 2017
Total	$2,316,945,000		

As discussed previously, the Commonwealth has entered into interest rate exchange agreements with respect to all Mandatory Tender FRNs. In the event the Commonwealth cannot remarket these bonds on their mandatory tender dates as variable rate bonds, the Commonwealth may have to terminate the associated interest rate exchange agreements. As of September 30, 2011, the mark-to-market value of all interest rate exchange agreements with respect to the Mandatory Tender FRNs was negative $143.5 million.

The Commonwealth has entered into forward starting interest rate exchange agreements with respect to approximately $69.2 million of its fixed rate Mandatory Tender Bonds. COFINA has also entered into forward starting interest rate exchange agreement with respect to approximately $907 million of fixed rate Mandatory Tender Bonds of Public Finance Corporation. The Commonwealth forward starting interest rate exchange agreement assumes that the related Commonwealth fixed rate Mandatory Tender Bonds will be remarketed as variable rate bonds after their mandatory tender date. If the Commonwealth cannot remarket or issue these bonds as variable rate bonds at that time, the Commonwealth may have to terminate the respective forward starting interest rate exchange agreement, which may result in the payment of a termination amount. The Commonwealth expects to refund the Public Finance Corporation fixed rate Mandatory Tender Bonds prior their mandatory tender date through the issuance of COFINA and Public Finance Corporation fixed rate bonds, and in connection therewith terminate the Public Finance Corporation forward starting interest rate exchange agreement. The termination payment regarding this interest rate exchange agreement is also expected to be financed through the issuance of COFINA bonds. As of September 30, 2011, the mark-to-market value of these forward starting interest rate exchange agreements to the Commonwealth and COFINA was negative $20.7 million and negative $386.3 million, respectively, which are approximately the amounts the Commonwealth and COFINA would have been required to pay to terminate the interest rate exchange agreements on that date.

Ratings of Commonwealth General Obligation Bonds

The Commonwealth's general obligation and appropriation debt is currently rated "Baa1" with a negative outlook by Moody's, "BBB+" with a stable outlook by Fitch, and "BBB" with a stable outlook by S&P.

Commonwealth Guaranteed Debt

As of June 30, 2011, $3.070 billion of Commonwealth guaranteed bonds of the PBA were outstanding. Following the issuance by PBA on August 24, 2011 of $756,449,000 Government Facilities Revenue Bonds, Series R (Qualified School Construction Bonds – Issuer Subsidy) and $303,945,000 Government Facilities Revenue Bonds, Series S, $4.012 billion of Commonwealth guaranteed bonds of PBA are outstanding. Maximum annual debt service on these bonds is $992.2 million in fiscal year 2028, assuming the receipt of the issuer subsidy from the federal government on the Series R Bonds, and $1.025 billion without taking into consideration said subsidy, with their final maturity being July 1, 2039. No payments under the Commonwealth guaranty have been required to date for these bonds.

As of June 30, 2011, $267 million of Commonwealth guaranteed bonds of GDB were outstanding. No payments under the Commonwealth guaranty have been required for these bonds.

As of June 30, 2011, GDB held approximately $214.5 million of the Port of the Americas Authority's outstanding bonds, which are guaranteed by the Commonwealth. The Authority is authorized to issue and GDB is authorized to purchase its bonds guaranteed by the Commonwealth in a maximum aggregate principal amount of $250 million. The proceeds from these bonds will be used to continue the development of the Port of the Americas. Payments of $43.4 million under the Commonwealth guaranty have been required to pay interest and principal on these bonds. See "Other Public Corporations—Port of the Americas Authority" under "Public Corporations" below.

As of June 30, 2011, the aggregate outstanding principal amount of obligations of PRASA guaranteed by the Commonwealth was $1.012 billion. This amount consisted of $284.8 million in revenue bonds sold to the public, $313.6 million in bonds issued to the United States Department of Agriculture, Rural Development, and $413.4 million of loans by the State Revolving (Clean Water and Safe Drinking Water Act) Funds for the benefit of PRASA. From January 1997 through fiscal year 2005, the Commonwealth made debt service payments under its guaranty. Beginning with the debt service payment due January 1, 2006, the Commonwealth stopped making guarantee payments on these obligations and PRASA resumed making payment on this debt. The Commonwealth, however, has been making certain subsidy payments to PRASA for its operational expenses. In the event PRASA is unable to make any portion of the future debt service payments on its guaranteed obligations, the Commonwealth would be required once more to make such payments from the General Fund under its guarantee. See "Other Public Corporations—Puerto Rico Aqueduct and Sewer Authority" under "Public Corporations" below.

Trends of Public Sector Debt

The following table shows the growth rate of short-term and long-term public sector debt and the growth rate of gross national product (in current dollars) for the five fiscal years ended June 30, 2011. As of June 30, 2011, outstanding short-term debt, relative to total debt, was 7.4%. Total public sector debt for fiscal year 2010 shown in the table below represented 89.8% of gross national product for fiscal year 2010.

Commonwealth of Puerto Rico
Public Sector Debt and Gross National Product
(dollars in millions)*

	Public Sector					Gross National Product[(1)]	
June 30,	Long Term[(2)]	Short Term[(3)]	Total	Short Term as % of Total	Rate of Increase	Amount	Rate of Increase
2007	39,492	3,326[(4)]	42,818	7.8	7.2	59,521	4.9
2008	43,663	3,269[(4)]	46,932	7.0	10.0	61,665	3.6
2009	48,332	4,648[(4)]	52,980	8.8	13.0	62,678	1.6
2010	53,351	3,472	56,823	6.1	7.3	63,291	0.98
2011	54,804	4,380	59,184	7.4	3.7	-	-

* Totals may not add due to rounding.

(1) In current dollars.

(2) Does not include debt totaling $5.3 billion consisting of (i) Senior Pension Funding Bonds, Series A, B, and C issued by the Employees Retirement System, which are payable solely from employer contributions made to the Employees Retirement System by the Commonwealth, its municipalities and participating public corporations after the issuance of the bonds, identified in footnote 4, and (ii) bonds identified in footnote 6, of the table above entitled “Commonwealth of Puerto Rico—Public Sector Debt,” which would have been issued and outstanding at the time, all of which would be considered long-term debt.

(3) Obligations (other than bonds) issued with an original maturity of three years or less and lines of credit with a remaining maturity of three years or less are considered short-term debt.

(4) Does not include the tax and revenue anticipation notes that were outstanding at the close of the indicated fiscal years because prior to the end of said fiscal years sufficient funds had been set aside for the payment of such notes in full.

Source: Government Development Bank

The following table shows the trend of public sector debt by major category for the five fiscal years ended June 30, 2011.

Commonwealth of Puerto Rico
Public Sector Debt by Major Category
(dollars in millions)*

	Commonwealth[(1)]			Municipalities			Public Corporation[(2)]			Total		
June 30,	Long Term	Short Term[(3)]	Total	Long Term	Short Term[(3)]	Total	Long Term	Short Term[(3)]	Total	Long Term	Short Term[(3)]	Total
2007	10,335	224[(4)]	10,559	2,164	299	2,463	26,993	2,803	29,796	39,492	3,326	42,818
2008	9,273	519[(4)]	9,792	2,507	313	2,820	31,633	2,437	34,070	43,413	3,269	46,682
2009	9,382	557[(4)]	9,939	2,691	306	2,997	36,259	3,785	40,044	48,332	4,648	52,980
2010	10,033	270	10,303	2,905	326	3,231	40,413	2,876	43,289	53,351	3,472	56,823
2011	10,199	164	10,363	3,204	333	3,537	41,401	3,883	45,284	54,804	4,380	59,184

* Totals may not add due to rounding.

(1) Does not include the Senior Pension Funding Bonds, Series A, B, and C issued by the Employees Retirement System, which are payable solely from employer contributions made to the Employees Retirement System by the Commonwealth, its municipalities and participating public corporations after the issuance of the bonds, identified in footnote 4 of the table above entitled "Commonwealth of Puerto Rico—Public Sector Debt."

(2) Includes Commonwealth guaranteed debt; does not include the bonds identified in footnote 6 of the table above entitled "Commonwealth of Puerto Rico—Public Sector Debt."

(3) Obligations (other than bonds) issued with an original maturity of three years or less and lines of credit with a remaining maturity of three years or less are considered short-term debt.

(4) Does not include the tax and revenue anticipation notes that were outstanding at the close of the indicated fiscal years because prior to the end of said fiscal years sufficient funds had been set aside for the payment of such notes in full.

Source: Government Development Bank

PUBLIC CORPORATIONS

In Puerto Rico, many governmental and quasi-governmental functions are performed by public corporations created by the Legislative Assembly with varying degrees of independence from the central government to perform generally a single function or a limited number of related functions. Most public corporations obtain revenues from rates charged for services or products, but many are subsidized to some extent by the central government. Most public corporations are governed by boards whose members are appointed by the Governor with the advice and consent of the Senate, but some public corporations are attached to departments of the central government. Capital improvements of most of the larger public corporations are financed by revenue bonds issued under trust agreements or bond resolutions, or by notes issued under loan agreements. The following table presents the outstanding bonds and notes of certain of the public corporations as of June 30, 2011 ("notes" as used in this section refers primarily to certain types of non-bonded debt regardless of maturity). Debt of certain other public corporations is excluded from this table because such debt is payable primarily from funds or grants provided by the federal government, is payable from sources other than Commonwealth appropriations or taxes or revenues of public corporations, or is payable from revenues derived from private sector services or products, such as industrial development bonds. Also excluded from this table is debt of certain public corporations the inclusion of which would reflect double counting. No deductions have been made in the table for debt service funds and debt service reserve funds. More detailed information about the major public corporations is presented in the following sections.

Commonwealth of Puerto Rico
Outstanding Debt of Public Corporations
June 30, 2011
(in thousands)

	Bonds			Notes			Total Bonds and Notes		
	With Guaranty	Without Guaranty	Total	With Guaranty	Without Guaranty	Total	With Guaranty	Without Guaranty	Total
Aqueduct and Sewer Authority	$ 598,389	$ 1,338,650	$ 1,937,039	$413,449	$1,271,785	$1,685,234	$ 1,011,838	$ 2,610,435	$ 3,622,273
Convention Center District Authority	-	447,160	447,160	-	147,600	147,600	-	594,760	594,760
Electric Power Authority	-	7,780,890	7,780,890	-	191,362	191,362	-	7,972,252	7,972,252
Highway and Transportation Authority	-	6,119,949[1]	6,119,949	-	1,294,307	1,294,307	-	7,414,255	7,414,255
Housing Finance Authority	-	297,894[2]	297,894	-	67,498	67,498	-	365,392	365,392
Industrial Development Company	-	235,065	235,065	-	88,532	88,532	-	323,597	323,597
Infrastructure Financing Authority[3]	-	1,840,308	1,840,308	-	10,321	10,321	-	1,850,629	1,850,629
Port of the Americas Authority	214,525	-	214,525	-	-	-	214,525	-	214,525
Ports Authority	-	46,326[4]	46,326	-	691,519	691,519	-	737,845	737,845
Public Buildings Authority	3,069,539	-	3,069,539	-	400,314	400,314	3,069,539	400,314	3,469,853
Public Finance Corporation	-	1,618,284[5]	1,618,284	-	-	-	-	1,618,284	1,618,284
P.R. Sales Taxes Financing Corp. (COFINA)	-	13,764,557	13,764,557	-	-	-	-	13,764,557	13,764,557
University of Puerto Rico	-	532,846[6]	532,846	-	93,706	93,706	-	626,552	626,552
Others[7]	-	-	-	-	2,467,441	2,467,441	-	2,467,441	2,467,441
Total[8]	$3,882,453	$34,021,929	$37,904,382	$413,449	$6,724,384	$7,137,833	$4,295,902	$40,746,313	$45,042,215

(1) Excludes $151 million of Special Facilities Revenue Bonds issued by the Highway and Transportation Authority, which are payable from net toll revenues collected from the Teodoro Moscoso Bridge.

(2) Excludes the $180 million of Housing Finance Authority bonds, which are payable solely from Puerto Rico Public Housing Administration's annual allocation of Public Housing Capital Funds from the U.S. Department of Housing and Urban Development; $343.8 million of Housing Finance Authority Capital Fund Modernization Program Subordinate Bonds, Series 2008; and $100 million of Housing Finance Authority Housing Revenue Bonds, Series 2008.

(3) Includes $42.2 million of Mental Health Infrastructure Revenue Bonds, 2007 Series A (MEPSI Campus Project), which bonds are limited obligations of the Infrastructure Financing Authority payable solely from the pledge of certain payments made by a governmental entity under a lease agreement.

(4) Excludes $155 million of Special Facilities Revenues Bonds issued by the Ports Authority, which bonds are payable solely from the pledge of certain payments made by a private corporation under a special facilities agreement.

(5) Payable primarily from Commonwealth appropriations.

(6) Excludes $76.3 million of Educational Facilities Revenue Bonds, 2000 Series A (University Plaza Project) issued by AFICA, which bonds are payable from rent payments made by the University of Puerto Rico.

(7) Includes lines of credit with GDB.

(8) Excludes accretion of interest from the respective issuance dates on capital appreciation bonds. Also excludes $1.3 billion original principal amount of Children's Trust Tobacco Settlement Asset-Backed Bonds, Series 2002, 2005 and 2008 which bonds will be repaid from payments made by certain tobacco companies under a master settlement agreement. See "Children's Trust" under "Other Public Corporations" below.

Source: Government Development Bank

Government Development Bank for Puerto Rico

The principal functions of GDB are to act as financial advisor to and fiscal agent for the Commonwealth, its municipalities and public corporations in connection with the issuance of bonds and notes, to make loans and advances to public corporations and municipalities, and to promote the economic development of Puerto Rico. As part of its role as fiscal agent, during fiscal years 2009, 2010 and 2011, GDB entered into fiscal oversight agreements with the Aqueduct and Sewer Authority, Electric Power Authority, Highway and Transportation Authority, Ports Authority, Health Insurance Administration and Medical Services

Administration. As part of these agreements, GDB imposed certain conditions on the extension of credit to these entities and continually monitors their finances, among other things.

As of June 30, 2011, GDB had total assets of $15.5 billion and total liabilities of $12.9 billion (preliminary, unaudited). GDB's debt is currently rated A3 and BBB by Moody's and S&P, respectively, with a stable outlook.

As of June 30, 2011, $5.4 billion of bonds and notes of GDB (excluding its subsidiaries) were outstanding, consisting of $267 million in Commonwealth guaranteed bonds and $5.2 billion of medium term senior notes. Act No. 12 of May 9, 1975, as amended, provides that the payment of principal of and interest on specified notes and other obligations of GDB, not exceeding $550 million, may be guaranteed by the Commonwealth, of which $267 million were outstanding as of June 30, 2011. As of said date, GDB also had approximately $8.3 billion in loans outstanding to the central government of the Commonwealth and its public corporations and municipalities.

Act No. 82 of June 16, 2002 ("Act 82") amended GDB's Charter to authorize GDB to transfer annually to the General Fund, beginning with fiscal year 2001, up to 10% of its audited net income or $10,000,000, whichever is greater. GDB is not required by Act 82 to transfer any funds. GDB made payments to the General Fund of $11.6 million for fiscal year 2003 and $18.4 million for fiscal year 2004. GDB has not made any payment to the General Fund under Act 82 since fiscal year 2004.

Under Act No. 271 of November 21, 2002, GDB made a required special capital contribution to the Special Communities Perpetual Trust (the "Perpetual Trust") of $500 million and provided the Perpetual Trust with a $500 million, non-revolving, line of credit. The amounts transferred to the Perpetual Trust were deposited in two investment accounts held by GDB for the benefit of the Perpetual Trust. As of June 30, 2011, the Perpetual Trust had repaid $131.8 million of its line of credit and had an outstanding balance of $368 million and no interest due. The line of credit is payable from legislative appropriations.

As part of its role as lender and promoter of the economic development of Puerto Rico, GDB provides financing to the Commonwealth, its public corporations and municipalities. This financing includes interim loans to finance the capital expenditures of the Commonwealth in anticipation of the issuance of bonds and notes, and loans to cover operational deficits of those government entities. GDB generally does not provide financing to any governmental entity of the Commonwealth unless GDB reasonably believes that the borrower governmental entity will have sufficient resources, including the ability to issue bonds or notes or otherwise borrow funds, to repay such loan. GDB, however, has provided financing in the past and may continue to provide financing to governmental entities that do not have sufficient independent resources to cover operating expense, to the extent permitted by law. A material increase in the amount of loans to the public sector, coupled with continued deterioration of the public sector's fiscal situation and financial condition may have an adverse effect on GDB's financial condition and liquidity. As of June 30, 2011, GDB had outstanding loans to the Commonwealth in the aggregate principal amount of $2.1 billion, outstanding loans to, and bonds of, the public corporations in the aggregate principal amount of $4.3 billion, and outstanding loans to the municipalities in the aggregate principal amount of $1.8 billion.

GDB has several subsidiaries that perform various functions. The principal subsidiaries and their functions are listed below:

Puerto Rico Housing Finance Authority. Puerto Rico Housing Finance Authority ("Housing Finance Authority") (formerly known as Housing Finance Corporation) was created to provide needed rental housing units and stimulate the construction industry under federally subsidized programs. Effective February 8, 2002, Housing Finance Corporation became the Housing Finance Authority and the Housing Bank and Finance Agency was dissolved and its powers transferred to the Housing Finance Authority. Housing Finance Authority provides financing for rental housing units, stimulates the construction industry under federally subsidized programs and provides interim financing for low-income housing projects and single-family homeownership programs. It is also engaged in insuring and servicing mortgages originated by the former Housing Bank and Finance Agency. As of June 30, 2011, Housing Finance Authority's total outstanding principal balance of loans to the private sector for development of housing projects targeted to low and moderate income families were $136.2 million. The Housing Finance Authority's mortgage loans to low and moderate income homeowners represented an additional outstanding principal balance of $110.6 million as of the same date.

Housing Finance Authority has outstanding tax-exempt revenue bonds the proceeds of which were loaned to the Puerto Rico Public Housing Administration to finance improvements to various housing projects in the Commonwealth. Such bonds are limited obligations of Housing Finance Authority payable solely from revenues collected from such housing units, with certain exceptions. As of June 30, 2011, $623.8 million of these bonds were outstanding.

As of June 30, 2011, the Housing Finance Authority had total notes and bonds outstanding of $952.2 million (including $106.8 million of debt outstanding under GDB lines of credit and $823.3 million in bonds issued to fund certain payments under its mortgage subsidy programs for low and moderate income families). As of June 30, 2011, Housing Finance Authority had total unrestricted net assets of $245.2 million.

Puerto Rico Tourism Development Fund. Puerto Rico Tourism Development Fund ("TDF") was created in September 1993 for the purpose of promoting the development of Puerto Rico's hotel industry by working with private-sector financial institutions in structuring financings for new hotel projects. TDF can provide guarantees to interim and permanent financings. In certain transactions, TDF can act as direct lender, guarantee mezzanine financings, and provide preferred equity capital. As of June 30, 2011, TDF had $372.5 million in guarantees and $408.2 million in loans.

In addition, TDF has a $50 million preferred equity investment in a tourism-related project.

Since 1993, TDF has made payments under its guarantees and letters of credit in the aggregate amount of approximately $221.3 million with respect to several projects. Of the total amount disbursed, TDF has been able to recover approximately $172.3 million from the borrowers.

Un-audited fiscal year-end 2011 financial statements reflected net assets of $179.7 million and its allowances for losses on loans and guarantees and letters of credit were approximately $86.0 million.

Government Development Bank for Puerto Rico Capital Fund. Government Development Bank for Puerto Rico Capital Fund (the "Capital Fund") was created in November 1992 for the purpose of investing and trading in debt obligations and publicly traded shares of domestic and foreign corporations separate from GDB's general investment operations. On June 30, 2010, the Capital Fund transferred to the Tourism Development Fund, on behalf of GDB, $72.1 million representing all the investments in the Capital Fund portfolio. As of June 30, 2011, the Capital Fund had assets of $243,000, consisting principally of money market investments.

Puerto Rico Development Fund. Puerto Rico Development Fund (the "Development Fund") was established in April 1977 to provide an alternate source of financing to private enterprises. The Development Fund is also authorized to guarantee obligations of those enterprises and invest in their equity securities. On December 31, 2010, the Development Fund acquired for $8.5 million a commercial loan from a private commercial bank, secured by a first mortgage over a 2.34 acre parcel of land in the Convention Center District. As of June 30, 2011, the Development Fund had assets of $24 million, including investments of $8.5 million in loans to private entities, $11.1 million in an interest bearing account, and $3.6 million in preferred shares of various private entities.

Puerto Rico Public Finance Corporation. Puerto Rico Public Finance Corporation ("PFC") was established in November 1984 to provide agencies and instrumentalities of the Commonwealth with alternate means of meeting their financing requirements. The trustees of certain limited obligation bonds issued by the PFC currently hold notes payable by the Commonwealth, the Maritime Shipping Authority, the Office for the Improvement of Public Schools, the Department of Health and the Aqueduct and Sewer Authority, among others. All such PFC bonds are limited, non-recourse obligations of PFC payable solely from Commonwealth appropriations made to pay debt service on the notes held by the bond trustees. As of June 30, 2011, PFC had $1.6 billion aggregate principal amount of limited obligation bonds outstanding.

A description of certain other affiliates of GDB is provided in "Other Public Corporations" below.

Other Public Corporations

Aqueduct and Sewer Authority. PRASA owns and operates Puerto Rico's public water supply and wastewater systems. Such systems provide water and wastewater services to 97% and 58% of the Commonwealth's population, respectively.

PRASA reported a preliminary operating loss of $39.6 million for fiscal year 2011, compared to operating losses of $58.3 million and $63.7 million for fiscal years 2010 and 2009, respectively. In order to improve its financial condition, PRASA adopted a comprehensive plan to increase its revenues and reduce its expenses.

As of June 30, 2011, PRASA's total debt was $3.6 billion, including approximately $1.0 billion of outstanding indebtedness with GDB. PRASA's senior debt is rated Baa1, BBB- and BBB by Moody's, S&P and Fitch Ratings ("Fitch"), respectively. On November 9, 2010, Moody's affirmed PRASA's rating but revised its outlook to negative from stable. The negative outlook reflects PRASA's continued reliance on GDB and the Commonwealth for financial support, as well as the operational challenges it faces to reduce the significant amount of water lost through its Systems.

The Commonwealth guarantees the principal and interest payments on the outstanding revenue refunding bonds, 2008 Series A and 2008 Series B, any bonds issued on or before June 30, 2015 to the Rural Utilities Service of the United States Department of Agriculture, and the loans granted on or before June 30, 2015 by the Puerto Rico Water Pollution Control Revolving Fund and the Puerto Rico Safe Drinking Water Revolving Fund to PRASA. In the event that PRASA is unable to make all or any portion of the future debt service payments on these guaranteed debts, the Commonwealth will be responsible for covering such payments.

During fiscal year 2011, PRASA received a $105 million assignment from the OMB in Commonwealth appropriations and other Commonwealth available funds. According to the provisions of PRASA's trust agreement, these moneys are taken into account for purposes of determining its revenues and its compliance with certain covenants therein.

On April 28, 2006, the Authority entered into a consent decree with the U.S. Environmental Protection Agency ("EPA") that requires the Authority to implement system wide remedial measures at all of the wastewater treatment plants operated by the Authority. The EPA consent decree establishes deadlines for the compliance with the conditions set forth therein and stipulates penalties for violation of any of those deadlines.

On December 15, 2006, a settlement agreement was signed between the Authority and the Department of Health of the Commonwealth ("DOH") relating to violations of the Safe Drinking Water Act. The settlement agreement was preliminarily approved by the supervising court on March 15, 2007, and was amended and finally approved by that court on June 20, 2008. The Authority agreed to implement a work plan to remediate the violations, establish preventive and mitigation measures, and execute a preventive maintenance program for the purpose of meeting the requirements of the Safe Drinking Water Act.

PRASA needs to make a substantial investment in infrastructure and a major overhaul of its operations to maintain the viability of the Systems, to finance its expansion for new users and to implement remedial measures required by a consent decree between PRASA and the EPA and a settlement agreement with the DOH. Funds for this investment will be provided through a combination of revenues from PRASA, financing transactions, federal grants and other sources. PRASA has established a 15-year capital improvement program with a total investment of $2.2 billion in order to comply with the consent decree and the settlement agreement. PRASA has committed an investment of $1.2 billion to comply with the EPA consent decree and $1.0 billion to comply with the DOH settlement agreement.

Children's Trust. Children's Trust is a not-for-profit corporate entity created in 1999 as a public instrumentality of the Commonwealth. The Commonwealth has transferred to Children's

Trust all of its rights, title and interest under the tobacco litigation Master Settlement Agreement, including the Commonwealth's right to receive initial, annual and strategic contribution payments to be made by the participating cigarette manufacturers under the Master Settlement Agreement.

Children's Trust issued $397 billion Tobacco Settlement Asset-Backed Bonds in November 2002. The proceeds were used to pay certain capital expenditures, to fund the Liquidity Reserve account and certain costs of issuance. On June 30, 2005, Children's Trust issued $108.2 million subordinate Tobacco Settlement Asset-Backed Bonds to pay working capital expenses of the Commonwealth. On May 1, 2008, Children's Trust issued an additional $195.9 million of subordinate Tobacco Settlement Asset-Backed Bonds to make grants to third parties, pay certain expenses of the Commonwealth and cost of issuance. As of June 30, 2011, Children's Trust had outstanding bonds in the principal amount of $1.3 billion. These bonds and any, other additional senior bonds issued by Children's Trust are payable solely from, and secured by a statutory pledge of, the payments made and to be made by the participating cigarette manufacturers under the Master Settlement Agreement. To date, all principal and interest payments required to be made by Children's Trust on its outstanding bonds have been made on a timely basis from contribution payments made by the participating cigarette manufacturers under the Master Settlement Agreement.

Convention Center District Authority. Convention Center District Authority was created to own, develop, finance, plan, design, build, operate, maintain, administrate and promote the Dr. Pedro Rosselló González Convention Center, a new convention center, and designated private parcels located within the Convention Center District in San Juan. The convention center opened in November 17, 2005. Convention Center District Authority also owns a multipurpose coliseum in San Juan, known as the José Miguel Agrelot Coliseum. As of June 30, 2011, Convention Center District Authority's debt was $447.2 million in outstanding bonds issued in March 2006 to finance the Convention Center and payable from a portion of a hotel room tax. As of June 30, 2011, Convention Center District Authority also had outstanding indebtedness to GDB of approximately $147.8 million related to the financing of the Coliseum.

Electric Power Authority. Puerto Rico Electric Power Authority ("PREPA") owns and operates Puerto Rico's electric power system.

PREPA reported preliminary net operating income of $328.9 million and $359.5 million during fiscal years 2011 and 2010, respectively. The total debt of PREPA was $8.0 billion as of June 30, 2011. This debt includes outstanding bonds of $7.8 billion and interim financing for operations of $191.4 million. PREPA's debt is rated A3, BBB+ and A- by Moody's, S&P and Fitch, respectively.

As a means of reducing its dependency on oil, PREPA has entered into long-term power purchase agreements with private operators of two co-generation plants that use fuels other than oil. Currently, these two co-generation plants provide approximately 31% of PREPA's energy needs. PREPA has also commenced developing plans for the conversion of its main oil-fired units into natural gas and clean-coal fired units, as well as other strategies to further reduce its dependency on oil.

Health Insurance Administration. The Health Insurance Administration was created in 1993 to negotiate and contract for the provision of comprehensive health insurance coverage for qualifying (generally low income) Puerto Rico residents. Under this system, the government selected, through a bidding system, one private health insurance company in each of eight designated regions of the island and paid such insurance company the insurance premium for each eligible beneficiary within such region. The health insurance system covered the entire island. Approximately 1.5 million persons were covered by the system during fiscal year 2011.

The total cost of the health insurance program was $2.013 billion for fiscal year 2011, $1.962 billion for fiscal year 2010 and $1.861 billion for fiscal year 2009. During fiscal year 2011, the General Fund covered $1.225 billion of the total cost of the health insurance program and $75 million was covered from proceeds of COFINA bonds. The remaining $713 million was paid from federal, municipal, internal and other sources. On March 14, 2011, the Health Insurance Administration borrowed approximately $186 million from GDB in order to pay amounts owed to its suppliers, including premiums owed to certain insurance companies for services rendered under the Health Reform program. As of June 30, 2011, the Health Insurance Administration had outstanding indebtedness to GDB of approximately $173.1 million related to this borrowing.

On October 1, 2010, the administration implemented "Mi Salud," which is the health program that replaced the government's Health Reform program. The principal differences between "Mi Salud" and the Health Reform are the use of a preferred-provider network organization rather than independent practice associations, an increase of benefits and services and an expansion of eligible participants. During the implementation of the program's second phase, eligibility requirements will be expanded to include small to medium businesses. The estimated cost for "Mi Salud" during fiscal year 2012 is $1.994 billion. The General Fund is expected to cover $867 million, while the remaining $1.127 billion will be paid from federal, municipal and other sources. This projection, however, does not take into account increases in the enrollment of new beneficiaries, which could affect this estimate.

The Commonwealth has entered into various contracts with several Medicare Advantage organizations for the provision of health coverage to approximately 180,000 eligible beneficiaries. Pursuant to these agreements, the Commonwealth pays each Medicare Advantage organization a premium difference to cover services not included in their contracts with the Center for Medicaid and Medicare Services.

On July 7, 2011, the Secretary of Health of the Commonwealth announced the cancellation of the contract through which MCS HMO administered five regions, with approximately 850,000 insureds, of the "Mi Salud" program. MCS HMO continued to render services to covered insureds during a 90 day transition period. On October 17, 2011, the Health Insurance Administration and Triple-S Salud, Inc. ("Triple-S") entered into an agreement pursuant to which Triple-S will provide healthcare services to insureds in the five regions previously administered by MCS HMO. Pursuant to the agreement, Triple-S will act as a third party administrator, will be compensated based on a per member per month administration fee, and will not be financially responsible or otherwise at risk for the provision of services to insureds. In contrast to the agreement with MCS HMO, the Government will now be financially responsible and bear the risk for the provision of services to insureds in the five regions administered by Triple-S. The Government is currently evaluating the extent of the impact of the agreement with Triple-S on the budget of the health insurance program for fiscal year 2012 and no assurance can be given that the amounts budgeted will be sufficient to cover the additional financial responsibility and risk assumed.

Highways and Transportation Authority. Puerto Rico Highways and Transportation Authority ("PRHTA") is responsible for highway construction in Puerto Rico. Such construction is financed by debt (interim notes and revenue bonds), revenues of PRHTA, and federal and Commonwealth grants.

PRHTA reported a preliminary net operating loss of $523.6 million for fiscal year 2011, compared to a net operating loss of $445.3 million for fiscal year 2010 and $493.9 million for fiscal year 2009. As of June 30, 2011, PRHTA's total debt was $7.4 billion, consisting of $6.1 billion of bonds and $1.3 billion of GDB financings. As of September 30, 2011, PRHTA's total debt decreased to $6.7 billion, consisting of $5.1 billion of bonds and $1.6 billion of GDB financings.

Debt service on PRHTA's revenue bonds constitutes a first lien on its gross revenues, which consist currently of all the proceeds of the tax on gasoline, one-half of the proceeds of the tax on gas oil and diesel oil, all the proceeds of the excise taxes on crude oil, unfinished oil and derivative products, up to $120 million per fiscal year, highway toll revenues and the gross receipts of $15.00 per vehicle per year from certain motor vehicle license fees. Such revenues (except for toll revenues) may be applied first to the payment of debt service on general obligation bonds and notes of the Commonwealth and to payments required to be made by the Commonwealth under its guarantees of bonds and notes, to the extent that no other revenues are available for such purpose. The Commonwealth has never applied such revenues for such payment.

PRHTA's Highway Revenue Bonds are rated A3 and BBB+ by Moody's and S&P, respectively, and the Senior Transportation Revenues Bonds are rated Baa1 and BBB by Moody's and S&P, respectively.

PRHTA has a mass transit system, known as Tren Urbano, serving a portion of metropolitan San Juan. It was constructed under several design/build contracts and is being privately operated under a five-year contract with an additional five-year option at PRHTA's election. The cost of the project was $2.4 billion, which cost was financed by federal Transit Administration grants, other federal funding sources and PRHTA's own resources, including revenue bonds. Tren Urbano commenced operations in June 2005. The operation of the Tren Urbano generated a loss of $51.7 million, $64.5 million, and $62.5 million in fiscal years 2010, 2009 and 2008, respectively.

PRHTA is a party to a concession agreement under which a private company designed, constructed and currently is operating a toll bridge spanning the San José Lagoon. The toll bridge was financed with special facility revenue bonds of PRHTA, payable by the private operator of the bridge principally from toll revenues. The concession is for a term of 35 years, subject to earlier termination or extension. The bridge opened for traffic in February 1994. In certain circumstances described in the concession agreement, including where toll revenues are insufficient to generate certain rates of return to the private operator, the private operator may require PRHTA, among other things, to assume the operator's obligations with respect to the special facility revenue bonds. Some of those circumstances, including lower than projected toll revenues, exist at this time, but PRHTA does not currently anticipate that the operator will exercise its remedy against PRHTA.

On September 22, 2011, PRHTA and PPP Authority completed the procurement process whereby a concession agreement was awarded to Metropistas, for the operation of toll roads PR-22 and PR-5. In connection with the establishment of the concession, PRHTA defeased, redeemed and/or purchased approximately $873.1 million aggregate principal amount of its bonds. See "Public-Private Partnerships – Fiscal Stabilization and Economic Reconstruction" under THE ECONOMY.

Industrial Development Company. Puerto Rico Industrial Development Company ("PRIDCO") participates in the Commonwealth-sponsored economic development program by providing physical facilities, general assistance, and special incentive grants to manufacturers. PRIDCO reported consolidated change in net assets of $8.4 million for fiscal year 2011, compared to consolidated change in net assets of $10.3 million for fiscal year 2010, and consolidated change in net assets of $6.0 million for fiscal year 2009. Rentals derived from the leasing of specified facilities of PRIDCO are pledged to the payment of PRIDCO's revenue bonds. As of June 30, 2011, PRIDCO's total debt was $423.1 million, including approximately $88.5 million from GDB financings and the outstanding debt of Puerto Rico Industrial Investment Corporation, a subsidiary of PRIDCO. PRIDCO's debt is rated Baal and BBB- by Moody's and S&P, respectively.

Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority. The Puerto Rico Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority ("AFICA") was created to finance (through the issuance of its revenue bonds) industrial, tourist, educational, medical, and environmental control facilities in Puerto Rico for the use of private companies, non-profit entities, or government agencies. The bonds are payable solely from payments to be made to AFICA by such private companies, non-profit entities, or government agencies, and do not constitute a debt of the Commonwealth or any of its other public corporations or municipalities. As of June 30, 2011, approximately $1.45 billion of AFICA's bonds were outstanding. In addition, as of June 30, 2011, AFICA has a $67 million line of credit with GDB with a principal outstanding balance of $59.3 million used for the acquisition of assets from PREPA.

Infrastructure Financing Authority. Puerto Rico Infrastructure Financing Authority ("PRIFA") was created to provide financial, administrative, consulting, technical, advisory, and other types of assistance to other public corporations, governmental instrumentalities, political subdivisions and municipalities (collectively, "Benefited Entities") authorized to develop infrastructure facilities and to establish alternate means for financing those facilities. PRIFA is authorized to issue bonds and provide loans, grants and other financial assistance for the construction, acquisition, repair, maintenance and reconstruction of infrastructure projects by Benefited Entities.

As of June 30, 2011, PRIFA's total debt was $1.85 billion. This debt includes bonds outstanding of $1.84 billion and interim financing for capital improvements of $10.3 million. PRIFA's debt is rated Baa3 and BBB+ by Moody's and S&P, respectively.

PRIFA oversees the Puerto Rico Infrastructure Fund, which is being funded annually thru fiscal year 2052 with the first $117 million of proceeds of federal excise taxes imposed on rum and other articles produced in Puerto Rico and sold in the United States that are transferred to Puerto Rico pursuant to the United States Internal Revenue Code of 1986, as amended. See "Major Sources of General Fund Revenues – Revenues from Non-Commonwealth Sources" under PUERTO RICO TAXES, OTHER REVENUES AND EXPENDITURES. Rum is the only article currently produced in Puerto Rico subject to federal excise taxes, the proceeds of which are required to be returned to the Treasury Department. The Authority is using these funds to pay debt service of bonds issued to finance various infrastructure projects.

PRIFA also has custody and control of the Infrastructure Development Fund and its Corpus Account, a perpetual account established under Act No. 92 of June 24, 1998 that was funded with $1.2 billion of the proceeds of the sale of Puerto Rico Telephone Company. The interest earned on the securities held in the Corpus Account were being used by PRIFA to pay debt service on its $1.1 billion Series 2000 A and B Bonds. Act No. 3, approved by the Legislative Assembly of the Commonwealth on January 14, 2009 ("Act 3"), authorized the sale of the securities held in the Corpus Account. PRIFA sold the securities in January 2009 and used the proceeds to: (i) make a deposit into an escrow account in an amount sufficient to retire the Series 2000 A and B Bonds on October 1, 2010, (ii) make a deposit to the General Fund which was applied to cover a portion of the Commonwealth's budget deficit, (iii) make a transfer to GDB as a capital contribution, and (iv) make a deposit to the Corpus Account to be invested in a long-term investment agreement with GDB.

As part of the Government's actions to address in part the financial condition of the Employees Retirement System, the Government enacted Act 96. On June 23, 2011, in accordance with Act 96, $162.5 million of funds on deposit in the Corpus Account were contributed to the Employees Retirement System and invested in capital appreciation bonds issued by COFINA maturing annually on August 1, 2043 through 2048 and accreting interest at a rate of 7%. PRIFA also invested $165.0 million of funds on deposit in the Corpus Account in capital appreciation bonds of COFINA maturing annually on August 1, 2045 through 2050 and accreting interest at 7%.

Pursuant to Act No. 8 of March 9, 2009, PRIFA is responsible for implementing in the Commonwealth the applicable provisions of ARRA. One of its main responsibilities regarding ARRA is to maximize the flow of funds from the Federal Government for the appropriate investment in qualified projects and activities. PRIFA also has responsibility for the receipt, administration and disbursement of such funds and monitoring those governmental agencies and entities that receive ARRA funds.

Municipal Finance Agency. Puerto Rico Municipal Finance Agency ("MFA") is authorized to issue bonds to purchase general obligation bonds and notes of Puerto Rico municipalities and to fund a debt service reserve. Debt service on MFA's bonds is payable from debt service payments on municipal bonds and notes held by MFA and from the debt service reserve, including investment income thereon. The Commonwealth has agreed to pay such amounts to the debt service reserve as may be necessary to maintain it at its required level, subject to appropriation by the Legislative Assembly, which appropriation is authorized but not legally required to be made. To date no such payments have been required. As of June 30, 2011, MFA had $1.1 billion of bonds outstanding.

Port of the Americas Authority. PAA is responsible for the development and operation of the Port of the Americas (the "Port"), a deep draft port on the south coast of Puerto Rico.

PAA is authorized to issue bonds guaranteed by the Commonwealth in a maximum aggregate principal amount of $250 million. The proceeds from these bonds must be used to continue the development of the Port. Currently, GDB is authorized by law to purchase bonds of PAA in an aggregate principal amount not to exceed $250 million. As of June 30, 2011, GDB held approximately $214.5 million of PAA's outstanding bonds, which are guaranteed by the Commonwealth.

The first phase of the Port was completed in fiscal year 2004. This initial phase included the improvement of piers 4, 5 and 6 of the Port and the acquisition of heavy equipment at a cost of $40 million. The second phase of the Port was completed during the first quarter of calendar year 2009. This phase, which was designed to provide capacity to handle up to 250,000 Twenty-Foot Equivalent Units ("TEU") per year, included (i) dredging the entrance channel and adjacent areas of the Port to a depth of 50 feet, (ii) reconstructing the container terminals, (iii) commencing certain required environmental risk mitigation procedures, and (iv) preparing final construction schematics.

A third phase, which provides for the expansion of the Port's capacity, was initiated in August 2008. This phase includes, among other improvements, (i) infrastructure improvements related to access roads, (ii) relocation of the storm sewer channel. (iii) relocation of the server, water and power distribution systems, (iv) additional dredging at certain pier locations, (v) the expansion of the container terminal, and (vi) additional mitigation measures. The first expansion under this phase will provide sufficient capacity to process 500,000 TEU annually. This phase is expected to be finished in 2012.

Ports Authority. Puerto Rico Ports Authority ("Ports Authority") owns and operates the major airport and seaport facilities in Puerto Rico. Ports Authority derives revenues from a variety of sources, including charges on airplane fuel sales, air terminal space rentals, landing fees, wharfage, dockage and harbor fees, and rentals for the lease of property and seaport equipment. Ports Authority reported operating losses of $38.7 million and $46.7 million during fiscal years 2010 and 2009, respectively. As of June 30, 2011, the Ports Authority had $737.8 million in debt, including approximately $155.3 million from GDB financings.

As of June 30, 2011, the outstanding balance of the credit facilities for capital improvements with private financial institutions was $533.7 million, which is guaranteed by GDB.

Public Buildings Authority. PBA is authorized to construct, purchase or lease office, school, health, correctional and other facilities for lease to departments, public corporations, and instrumentalities of the Commonwealth. Bonds that have been issued by PBA to finance such facilities (through retirement of interim notes or otherwise) are payable from lease payments, which are largely derived from legislative appropriations and are secured by the Commonwealth's guaranty. PBA is authorized by law to have outstanding at any one time up to $4.3 billion of bonds guaranteed by the Commonwealth.

On August 24, 2011 PBA issued $756,449,000 Government Facilities Revenue Bonds, Series R (Qualified School Construction Bonds – Issuer Subsidy) and $303,945,000 Government Facilities Revenue Bonds, Series S. The proceeds of this bond issue will be used to pay part of the cost of constructing, renovating, remodeling and/or improving approximately 100 public schools.

As of October 1, 2011, PBA had $4.049 billion principal amount of bonds outstanding (not including accretion of interest from the respective issuance dates on capital appreciation bonds). As of October 1, 2011, PBA's line of credit with GDB had an outstanding balance of $119.8 million.

PBA debt is rated Baa1, BBB and BBB+ by Moody's, S&P and Fitch, respectively.

Sales Tax Financing Corporation. COFINA is an independent governmental instrumentality of the Commonwealth created by Act 91 of 2006. COFINA was originally created for the purpose of financing the payment, retirement, or defeasance of certain appropriation-backed debt outstanding as of June 30, 2006, payable to GDB and PFC.

In 2009, the Legislative Assembly of Puerto Rico expanded the purposes for which COFINA was created and, correspondingly, increased its revenues by increasing from 1% to 2.75% (one-half of the tax rate of 5.5%) the portion that is transferred to COFINA of the sales and use tax imposed by the central government. As a result, COFINA was authorized to issue bonds for the following additional purposes: (i) to pay, in whole or in part, the debt of the Secretary of the Treasury with GDB in the amount of $1 billion, the proceeds of which were used to cover the budgetary deficit for fiscal year 2009, (ii) to pay, in whole or in part, certain financing granted to the Secretary of the Treasury by GDB payable from future Commonwealth general obligation bonds, and any debt of the Commonwealth outstanding as of December 31, 2008 that did not have a source of repayment or was payable from budgetary appropriations, (iii) to pay, in whole or in part, the accounts payable to suppliers of the Commonwealth, (iv) to pay or finance operational expenses of the Commonwealth for fiscal years 2009, 2010, and 2011, (v) to pay or finance operational expenses of the Commonwealth for fiscal year 2012, which would have to be included in the annual budget of the Government of Puerto Rico, (vi) to fund the Puerto Rico Economic Stimulus Fund, (vii) to fund the Commonwealth Emergency Fund in order to cover expenses resulting from catastrophic events such as hurricanes or floods, and (viii) to generate moneys to fund the Economic Cooperation and Public Employees Alternatives Fund. As of June 30, 2011, COFINA had approximately $13.8 billion outstanding of its Sales Tax Revenue Bonds (excluding all accretion on capital appreciation bonds). COFINA's Sales Tax Revenue Bonds are rated Aa2, AA- and AA- by Moody's, S&P and Fitch, respectively, and the Sales Tax Revenue Bonds, First Subordinate Series are rated A1, A+ and A+ by Moody's, S&P and Fitch, respectively.

Special Communities Perpetual Trust. The Perpetual Trust is a public corporation created by law to be an irrevocable and permanent trust. Perpetual Trust's principal purpose is to fund development projects that address the infrastructure and housing needs of underprivileged communities. GDB made a special capital contribution to Perpetual Trust of $500 million and provided the Perpetual Trust with a $500 million, non-revolving, line of credit. As of June 30, 2011, Perpetual Trust had disbursed most of its funds and its line of credit with GDB had an outstanding balance of $367.9 million. The line of credit is payable from legislative appropriations.

University of Puerto Rico. The University of Puerto Rico (the "University"), with approximately 62,342 students at the beginning of academic year 2010-2011, is by far the largest institution of higher education on the Island. Government appropriations are the principal source of University revenues, but additional revenues are derived from tuition, student fees, auxiliary enterprises, interest income, federal grants, and other sources. University capital improvements have been financed mainly by revenue bonds. As of June 30, 2011, the University's total debt was $626.6 million (excluding $18.9 million owed by the University's Medical Services). The University's debt is rated Baa3 and BBB- by Moody's and S&P, respectively. Moody's rating of the University is currently on "watchlist" for possible revision.

In 2000, AFICA issued its $86,735,000 Educational Facilities Revenue Bonds, 2000 Series A (University Plaza Project) for the purpose of financing the construction of additional student housing and parking and office space for the University. The project was built, is being operated by Desarrollos Universitarios, Inc., a Puerto Rico not-for-profit corporation, and is leased to the University for a term equal to the term of the bonds, with University lease payments being sufficient to pay debt service on said bonds as they become due. These bonds are not included in the University's total debt or outstanding revenue bonds set forth in the prior paragraph.

In June 2007, the Board of Trustees of the University approved Certification No. 60 establishing a new policy and methodology for tuition fees structure. This new structure covers the tuition fees to be charged to new students until academic year 2012-2013. This policy was adopted to pursue continued development and financial stability of the University.

In June 2010, the Board of Trustees of the University approved Certification No. 146 establishing a $400 stabilization fee to be charged each semester to all students in addition to tuition charges and other fees already in place at the University. This stabilization fee was imposed to address the University's fiscal difficulties and is expected to increase annual revenues by approximately $40 million.

As a result of a student-led strike that lasted approximately two months, on June 26, 2010, the Middle States Commission on Higher Education (the "Commission"), the regional accreditation entity of the eleven units that comprise the University system, placed on probation ten of the University's units for lack of evidence of compliance with two of fourteen accreditation standards. This action was prompted by a student stoppage that interrupted the operations of these units for up to 62 days, but less in most cases. The ten affected units will remain fully accredited while on probation. After a Monitoring Report submitted by the ten affected units in September 2010 and a subsequent evaluation visit, the Commission lifted probation over one of the questioned standards and added an additional standard, thereby continuing the review over two of the fourteen accreditation standards.

A second Monitoring Report was submitted to the Commission by the ten affected units on March 1, 2011 to further substantiate compliance with these two standards. Evaluation visits to the eleven units of the University were conducted between March and April 2011 as a follow up to the probationary process as well as the regular decennial re-accreditation review for some of the units. Following these visits, the evaluation teams reported that they intend to inform the Commission that 95% of all accreditation standards evaluated throughout the system were found in compliance, and significant progress was evidenced in the remaining 5%. In June 2011, the Commission lifted probation and reaffirmed accreditation of seven of the ten affected units.

Evaluation visits to the three units of the University on probation were conducted in September 2011. Following these visits, the evaluation teams reported that they intend to inform the Commission that these units are in full compliance with the standards under review. The Commission is expected to act upon the evaluation teams recommendations at their meeting in November 2011. The University anticipates that probation will be lifted for the three remaining units on probation after said meeting.

Other public corporations. Public corporations not described above have outstanding debt in the aggregate amount of $1.702 billion as of June 30, 2011. Debt service on $915 million of such outstanding debt is being paid from legislative appropriations. The Commonwealth is not, however, obligated to make any such appropriations. Additional legislative appropriations are made to enable certain of such corporations to pay their operating expenses.

INSURANCE MATTERS

Government-owned property is insured through policies obtained by the Secretary of the Treasury and through self-insurance, except for property owned by Electric Power Authority and Puerto Rico Aqueduct and Sewer Authority, whose properties are insured through arrangements and policies obtained by the respective Authorities. Personal injury awards against the Commonwealth are limited by law to $150,000 per occurrence.

RETIREMENT SYSTEMS

General. Substantially all of the public employees of the Commonwealth and its instrumentalities are covered by five retirement systems: the Employees Retirement System of the Government of the Commonwealth (the "Employees Retirement System"), the Puerto Rico System of Annuities and Pensions for Teachers (the "Teachers Retirement System"), the Commonwealth Judiciary Retirement System (the "Judiciary Retirement System"), the Retirement System of the University of Puerto Rico (the "University Retirement System") and the Employees Retirement System of Puerto Rico Electric Power Authority (the "Electric Power Authority Retirement System"). The Employees Retirement System and the Teachers Retirement System are the largest plans, both in number of active members and retirees and in the amount of their actuarial accrued liabilities.

The University Retirement System and the Electric Power Authority Retirement System covers employees of the University of Puerto Rico and Electric Power Authority, respectively, and are funded by those public corporations from their revenues. Although the Commonwealth is not required to contribute directly to those two systems, a large portion of the University's revenues is derived from legally mandated legislative appropriations. The discussion that follows only covers the Employees Retirement System, the Teachers Retirement System and the Judiciary Retirement System (each a "Retirement System" and, collectively, the "Retirement Systems").

The Employees Retirement System is a trust created by Act No. 447 of May 15, 1951 ("Act 447") and is a hybrid defined benefit plan consisting of different benefit structures. Members who entered the Employees Retirement System on or before December 31, 1999 generally participate in a defined benefit program. Members participating in the defined benefit program prior to April 1, 1990 ("Act 447 Participants") are entitled to the highest benefits structure, while those who became members on or after April 1, 1990 ("Act 1 Participants") are subject to a longer vesting period and a reduced level of benefits, as provided by Act No. 1 of February 16, 1990 ("Act 1 of 1990").

In 1999, Act 447 was amended to close the defined benefit program and, prospectively, establish a new benefit structure similar to a cash balance plan (this new benefit structure is referred to as "System 2000"). Members who entered the Employees Retirement System on or after January 1, 2000 ("System 2000 Participants") participate solely in System 2000. Under the System 2000 benefits structure, a participant is entitled to receive a lump-sum payment, which may be received in full or used to purchase an annuity from a third party, based solely on the amounts contributed by such participant. System 2000 Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. System 2000 Participants do not benefit from any employer contributions. Instead, employer contributions with respect to System 2000 Participants are used to reduce the accumulated unfunded pension benefit obligation of the Employees Retirement System.

System 2000 is not a separate plan as there are no separate accounts for System 2000 Participants. Contributions received from System 2000 Participants are pooled and invested by the Employees Retirement System together with the assets corresponding to the defined benefit structure. Thus, future benefit payments under the original defined benefit structure and System 2000 will be paid from the same pool of assets of the Employees Retirement System.

The Teachers Retirement System is a trust created by Act No. 91 of March 29, 2004 ("Act 91 of 2004"), which superseded Act No. 218 of May 6, 1951, and is a defined benefit pension plan. The Judiciary Retirement System is a trust created by Act No. 12 of October 19, 1954 and is also a defined benefit pension plan.

The Retirement Systems are funded principally by contributions made by employers (the Commonwealth, public corporations and municipalities) and employees, as well as investment income.

Covered Employees. The Employees Retirement System covers substantially all employees of the departments and agencies of the Commonwealth, all members and regular employees of the Legislative Branch, and all employees of the public corporations (other than the University of Puerto Rico or the Electric Power Authority) and municipalities, except for those employees that are covered by the other two Retirement Systems. The Judiciary Retirement System only covers judges.

The Teachers Retirement System covers public school teachers and certain private school teachers, as well as teachers working in administrative positions. Act 91 of 2004 establishes that: (i) the Teachers Retirement System's active employees as of March 29, 2004 (not public school teachers or other Department of Education employees) have the option to participate in the Teachers Retirement System or in the Employees Retirement System; (ii) persons hired by the Teachers Retirement System after the approval of the new law may only become members of the Teachers Retirement System, (iii) active teacher employees of the Department of Education are members of the Teachers Retirement System, and (iv) licensed teachers working in private schools or other educational organizations may elect to become members of the Teachers Retirement System as long as the required employer and employee contributions are satisfied. Currently, there are no teachers from private schools or other educational institutions participating in the Teachers Retirement System.

The following table shows the number of active members, retired members, disabled members and beneficiaries and terminated vested members for each of the Retirement Systems as of June 30, 2011.

Participant Data
(as of June 30, 2011)

	Active Members	Retired Members	Disabled Members	Beneficiaries	Terminated Vested Members[1]	Total
Employees Retirement System						
Act 447 Participants	30,057	79,177	16,208	13,073	-	138,515
Act 1 Participants	50,346	4,239	462	32	-	55,079
System 2000 Participants	55,569	-	-	-	-	55,569
Total	135,972	83,416	16,670	13,105	-	249,163
Teachers Retirement System	43,402	30,431	2,095	2,835	768	79,531
Judiciary Retirement System	362	335	0	56	48	801

(1) Represents generally members who ceased employment without the right to a retirement annuity and are due a refund of member contributions and, if applicable, employer contributions, plus interest thereon. There are terminated vested members of the Employees Retirement System, but the Employees Retirement System does not possess reliable data on the amount of such members.

The Commonwealth central government (consisting of department and agencies) is not the only employer participating in the Employees Retirement System. The municipalities and most public corporations participate as employers as well with respect to their employees. However, the assets contributed by the Commonwealth central government and all other employers are invested together and not otherwise segregated. As of June 30, 2011, the central government was responsible for making contributions with respect to 82,554 active members of the Employees Retirement System, or 60.7% of total active members (consisting of 19,230 Act 447 Participants, 33,347 Act 1 Participants and 29,977 System 2000 Participants). Municipalities were responsible for 32,264, or 23.7%, active members, and public corporations were responsible for 21,154, or 15.6%, active members.

Funding Requirements. The Commonwealth central government is responsible for approximately 59% of total employer contributions to the Employees Retirement System, and the other 41% is the responsibility of public corporations and municipalities. The Commonwealth central government is also responsible for 100% and 99% of total employer contributions to the Judiciary and Teachers Retirement Systems, respectively. Retirement and related benefits provided by the Retirement Systems and required contributions to the Retirement Systems by employers and employees are determined by law rather than by actuarial requirements. The Commonwealth is ultimately responsible for any funding deficiency with respect to central government employees in the three Retirement Systems.

As of July 1, 2011, after the adoption of Act 116, the statutory employer contribution for the Employees Retirement System increased from a minimum of 9.275% to a minimum of 10.275% of covered payroll. Covered payroll is the compensation regularly paid to active employees on which contributions to the retirement systems are computed and is generally equivalent to their annual salary. The employer contribution rate of 9.275% had been in effect since February 1990. Act 447 requires that employer contributions cover the difference between (i) the benefits provided by the System, plus administrative costs, and (ii) the contributions that employees are required to make to the System. This requirement, however, has not been adhered to and the level of employer contributions has been limited to the minimum statutory rate.

Required employee contributions for the Employees Retirement System vary according to how the individual employee's retirement benefits are coordinated with social security benefits.

As of July 1, 2011, after the adoption of Act 114, the statutory employer contribution for the Teachers Retirement System increased from 8.5% to 9.5% of covered payroll. The statutory employee contribution for the Teachers Retirement System is 9.0% of covered payroll. For the Judiciary Retirement System, the employer contribution is 30.34% of covered payroll and 8% for the employees. The employer contribution rate for the Judiciary Retirement System increased from 20.0% to 30.34% of payroll as of July 1, 2008.

Benefits and Special Benefits. Each Retirement System provides basic benefits principally consisting of a retirement annuity and death and disability benefits (collectively referred to herein as "Basic System Pension Benefits"). Each also administers benefits granted under various special laws that have provided additional benefits for the retirees and beneficiaries (collectively referred to herein as "System Administered Pension Benefits"). The System Administered Pension Benefits include, among others, additional minimum pension, death and disability benefits, ad-hoc cost-of-living adjustments and summer and Christmas bonuses. See Note 20 to the Commonwealth's audited financial statements for fiscal year 2010 included in the Comprehensive Annual Financial Report of the Commonwealth ("CAFR") for a summary of the benefits provided by each of the Retirement Systems.

The System Administered Pension Benefits are funded on a pay-as-you-go basis by the Commonwealth from the General Fund or by the participating public corporation and municipalities. These benefits are not an obligation of the respective Retirement Systems. Except for the System Administered Pension Benefits corresponding to former employees of municipalities and public corporations, which are obligations of the municipalities and public corporations, most of the funds used to cover these benefits are required to be paid by the Commonwealth through annual appropriations from the General Fund. Historically, however, the Retirement Systems have made current payments of System Administered Pension Benefits to participants but the costs of these pension benefits have not been recuperated by the Retirement Systems in full and on a timely basis from the Commonwealth and the participating public corporations and municipalities.

Through June 30, 2004, the Teachers Retirement System had paid $119.6 million from its resources to cover System Administered Pension Benefits that should have been received from the Commonwealth through annual appropriations. On May 31, 2004, the Teachers Retirement System made a claim to OMB to collect this amount. OMB disputed the Teachers Retirement System's interpretation of certain System Administered Pension Benefit laws to the effect that the Commonwealth is required to reimburse the Teachers Retirement System for such benefits paid. During 2009, the Department of Education paid $12.2 million that was part of the amounts claimed to OMB. On April 23, 2010, OMB and the Teachers Retirement System settled the remaining claim for $53.8 million, to be paid in five equal installments of $10.8 million during the next five fiscal years, starting in fiscal year 2011. In July 2011, the Teachers Retirement System received the second installment.

The Employees Retirement System is also seeking reimbursement from the Commonwealth, the municipalities and public corporations in the amount of approximately $78 million, $24 million and $40 million, respectively, for cumulative System Administered Pension Benefits paid to its beneficiaries through June 30, 2011.

Composition and Market Value of Investment Portfolios. As of June 30, 2011, the market value of the Employees Retirement System's investment portfolio was $4.224 billion (unaudited), compared to $4.138 billion as of June 30, 2010. As of June 30, 2011, the investment portfolio was comprised of approximately 31.4% of U.S. domestic and international equity investments, 24.5% of fixed income securities, 30.5% of internally managed mortgage and personal loans portfolio, 12.0% of short-term cash equivalents, and 1.6% of other investments. As of September 30, 2011, the market value of the Employees Retirement System's investment portfolio was $4.046 billion. The decrease in value of the investment portfolio since June 30, 2011 principally reflects market fluctuations and the continued use of investment portfolio assets to pay current benefits, as discussed below.

As of June 30, 2011, the market value of the Teachers Retirement System's investment portfolio was $2.338 billion (unaudited), compared to $2.157 billion as of June 30, 2010. As of June 30, 2011, the investment portfolio was comprised of approximately 51.9% of U.S. domestic and international equity investments, 26.3% of fixed income securities, 17.5% of internally managed mortgage and personal loans portfolio, 3.1% of short-term cash equivalents, and 1.1% of other investments. As of September 30, 2011, the market value of the Teachers Retirement System's investment portfolio was $2.123 billion. The decrease in value of the investment portfolio since June 30, 2011 principally reflects market fluctuations and the continued use of investment portfolio assets to pay current benefits, as discussed below.

As of June 30, 2011, the market value of the Judiciary Retirement System's investment portfolio was $60.6 million (unaudited), compared to $80.5 million as of June 30, 2010. As of June 30, 2011, the investment portfolio was comprised of approximately 31.9% of U.S. domestic and international equity investments, 59.3% of fixed income securities, 1.2% of internally managed mortgage and personal loans portfolio, and 7.6% of short-term cash equivalents. As of September 30, 2011, the market value of the Judiciary Retirement System's investment portfolio was $65.9 million.

Actuarial Valuations of the Retirement Systems. Historically, each of the Retirement Systems has conducted an actuarial valuation as of the end of every two fiscal years. However, due to the deterioration of the funding status of the Retirement Systems, as discussed below, each of the Retirement Systems began conducting annual actuarial valuations effective June 30, 2009. The latest actuarial valuations were conducted by Milliman Inc., a firm of independent consulting actuaries, as of June 30, 2010.

Informational copies of the actuarial valuation reports of the Employees Retirement System and the Judiciary Retirement System as well as other financial information are available on the website of the Administration of the Retirement Systems at www.retiro.pr.gov. Informational copies of the actuarial valuation report of the Teachers Retirement System as well as other financial information are available at the website of the Teachers Retirement System at www.srm.pr.gov. No information contained on these websites is deemed incorporated herein by reference.

The purpose of an actuarial valuation is to calculate the actuarial accrued liability of each of the Retirement Systems, which estimates on the basis of demographic and economic assumptions the present value of the benefits that each of the Retirement Systems will pay to its retired members and active members upon retirement. The actuarial valuations are performed in accordance with generally recognized and accepted actuarial principles and practices. The actuarial valuation compares the actuarial accrued liability with the actuarial value of assets and any excess of that liability over the assets represents an unfunded actuarial accrued liability ("UAAL") of the applicable Retirement System. In the case of the actuarial valuations of the Retirement Systems, the actuarial value of assets is equal to the market value of assets (net of liabilities). An actuarial valuation will also express the percentage that a Retirement System is funded through a "Funded Ratio" which represents the quotient obtained by dividing the actuarial value of assets of the Retirement System by the actuarial accrued liability of the Retirement System. An actuarial valuation will also state an actuarially recommended contribution rate, which is a recommended rate of covered payroll that consists of two components: (1) normal cost, which generally represents the portion of the present value of retirement benefits that are allocable to active members' current year service, and (2) an amortized portion of the UAAL. The amount that the Commonwealth and other participating entities actually contribute to the Retirement Systems is determined by statute and does not follow the recommendations of the actuaries, as discussed above. If additional employer contributions were to be made, they would have to be included in the Governor's budget request and approved by the Legislature.

To calculate the actuarial accrued liability of each of the Retirement Systems, the actuarial valuations use several actuarial assumptions. Some examples of these assumptions include an expected rate of return of assets, age of retirement of active members, future pay increases for current employees, assumed rates of disability and post-employment life expectancies of retirees and beneficiaries. If the experience of the Retirement Systems is different from these assumptions, the UAAL of the Retirement Systems may increase or decrease to the extent of any variances. As discussed below, the actual return of assets of each of the Retirement Systems during fiscal year 2009 was significantly lower than the assumed investment return utilized to prepare the actuarial accrued liability. The actual return of assets of each of the Retirement Systems for fiscal year 2010 and 2011, however, was higher than the assumed investment return used to prepare the actuarial valuations as of June 30, 2010. The Retirement Systems expect that the assumed investment return to be used in the actuarial valuations as of June 30, 2011, which are currently being prepared, will be lower than the assumed investment return used in the actuarial valuations as of June 30, 2010, which in turn will cause an increase in the UAAL.

The actual rate of return on assets of the Retirement Systems depends on the performance of their respective investment portfolios, which can vary materially from the expected rates of return assumed in the actuarial valuations. The investment portfolios of the respective Retirement Systems can be volatile. The value of the securities in the investment portfolios can dramatically change from one fiscal year to the next, which could, in turn, cause substantial increases or decreases in the net assets of the Retirement Systems, which directly impacts the UAAL. For fiscal year 2009, the annual rates of return of the assets of the Employees Retirement System, the Teachers Retirement System and the Judiciary Retirement System was negative 10.0%, negative 16.0% and negative 18.2%, respectively, contributing to the increase in the UAAL of the Retirement Systems between fiscal year 2007 and fiscal year 2009. For fiscal year 2010, the year-end return of the assets of the Employees Retirement System, the Teachers Retirement System and the Judiciary Retirement System was 8.7%, 12.5% and 12.7%, respectively. For fiscal year 2011, the year-end return of the assets of the Employees Retirement System, the Teachers Retirement System and the Judiciary Retirement System was 16.3%, 22.5% and 20.5%, respectively.

The June 30, 2010 actuarial valuations of the Employees Retirement System and Judiciary Retirement System were completed in accordance with the "projected unit credit" method and assumed an investment return of 7.5% per year and yearly salary increases of 3% per year. Under this method, a projected benefit is determined at each active participant's assumed retirement age assuming future compensation increases, and the projected benefit is attributed to each year of service using straight proration based on projected service to each assumed retirement age. The plan's normal cost is the sum of the present value of the portion of each active participant's projected benefit attributable to the current year of service.

The June 30, 2010 actuarial valuation of the Teachers Retirement System was completed in accordance with the "entry age normal" method and assumed an investment return of 8% per year and yearly salary increases of 3.5%. Under this method, a projected benefit is determined at each active participant's assumed retirement age assuming future compensation increases. The plan's normal cost is the sum of each active participant's annual cost for the current year of service determined such that, if it were calculated as a level percentage of his compensation each year, it would accumulate (at the valuation interest rate over his total prior and future years of service to the participant's assumed retirement date) into an amount sufficient to fund the participant's projected benefits.

Any amounts receivable from the Commonwealth with respect to benefits under System Administered Pension Benefits laws (discussed above) are considered in the actuarial valuation process to determine the unfunded pension benefit obligation of the Retirement Systems to the extent receivables are recognized as such by the Systems.

In performing the actuarial valuations, the actuaries rely on data provided by the Retirement Systems. Although the actuaries review the data for reasonableness and consistency, they do not audit or verify the data. If the data were inaccurate or incomplete, the results of the actuarial valuations may also be inaccurate or incomplete, and such defects may be material.

The following tables set forth, according to the actuarial valuations of the Retirement Systems, the actuarial value of assets, actuarial accrued liability, UAAL, funded ratio, covered payroll and UAAL as a percentage of covered payroll. The ratio of the UAAL to covered payroll is a measure of the significance of the UAAL relative to the capacity to pay it. The trend in the ratio provides information as to whether the financial strength of a pension plan is improving or deteriorating over time. As shown in the "Historical Funding Status" table, the steady increase in the UAAL to covered payroll for each of the Retirement Systems shows a significant deterioration in their financial strength.

Funding Status
Actuarial Valuations as of June 30, 2010
(in millions)

	Actuarial Value of Assets[1]	Actuarial Accrued Liability[2]	Unfunded Actuarial Accrued Liability[3]	Funded Ratio[4]	Covered Payroll[5]	UAAL as a Percentage of Covered Payroll[6]
Employees Retirement System	$1,667	$19,502	$17,834	8.5%	$3,818	467.1%
Teachers Retirement System	2,222	9,280	7,058	23.9	1,370	515.0
Judiciary Retirement System	55	338	283	16.4	32	882.0
Total	$3,944	$29,120	$25,175	13.5%	$5,220	482.3%

(1) The actuarial value of assets of each of the Retirement Systems is set forth in the actuarial valuation relating to each Retirement System and is equal to the full market value of the assets held by the Retirement Systems, including expected receivable contributions from the Commonwealth, municipalities and participating public corporations, less bonds payable and other liabilities.

(2) The actuarial accrued liability of each of the Retirement Systems is set forth in the actuarial valuation relating to each Retirement System and is an estimate based on demographic and economic assumptions of the present value of benefits that the Retirement System will pay during the assumed life expectancies of the applicable retired members and active members after they retire.

(3) The UAAL of each of the Retirement Systems is set forth in the actuarial valuation relating to each Retirement System and reflects the amount of the excess of the actuarial accrued liability of a Retirement System over its actuarial value of assets. The indicated amounts reflect the UAAL as calculated pursuant to the requirements of the Government Accounting Standards Board ("GASB") for purposes of presentation in the CAFR.

(4) The Funded Ratio of each of the Retirement Systems is presented in the actuarial valuation relating to each Retirement System and reflects the quotient obtained by dividing the actuarial value of assets of the Retirement System by the actuarial accrued liability of the Retirement System. The indicated percentages reflect the Funded Ratio as calculated pursuant to the requirements of GASB for purposes of presentation in the CAFR.

(5) The covered payroll of each of the Retirement Systems is presented in the actuarial valuation relating to each Retirement System and is equal to the annual salaries paid to active employees on which contributions to the Retirement System are made.

(6) The UAAL as a percentage of covered payroll is presented in the actuarial valuation relating to each Retirement System and reflects the quotient obtained by dividing the UAAL of the Retirement System by the covered payroll of the Retirement System.

Source: Actuarial valuation reports as of June 30, 2010 for each of the Retirement Systems.

Historical Funding Status[1]
Actuarial Valuations as of the Indicated Fiscal Years
(in millions)

Fiscal Year Ending June 30,	Actuarial Value of Assets	Actuarial Accrued Liability	Unfunded Actuarial Accrued Liability	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
Employees Retirement System						
2005	$2,328	$13,969	$11,641	16.7%	$4,126	282.2%
2007	2,892	16,770	13,878	17.2	4,246	326.8
2009	1,851	18,944	17,092	9.8	4,293	398.2
2010	1,667	19,502	17,834	8.5	3,818	467.1
Teachers Retirement System						
2004	$2,403	$ 4,702	$ 2,299	51.1%	$1,294	177.7%
2007	3,163	7,756	4,593	40.8	1,370	335.3
2009	2,158	8,722	6,564	24.7	1,418	462.8
2010	2,222	9,280	7,058	23.9	1,370	515.0
Judiciary Retirement System						
2005	$70	$174	$105	40.0%	$29	356.8%
2007	81	259	177	31.5	31	566.6
2009	51	324	273	15.6	31	893.7
2010	55	338	283	16.4	32	882.0

(1) Please refer to the footnotes of the immediately preceding table for an explanation of the categories set forth in the columns of this table.

Source: Actuarial valuation reports as of June 30 of the fiscal years indicated above for each of the Retirement Systems.

The following table shows the actuarially recommended contributions, actual employer contributions and resulting amount unfunded and percent contributed for each of the Retirement Systems' last four fiscal years.

Schedule of Employer Contributions to Retirement Systems (in millions)

Fiscal Year Ending June 30,	Actuarially Recommended Contributions(1)	Actual Employer Contributions(2)	Amount Unfunded(3)	Percent Contributed
Employees Retirement System				
2008	$1,191	$581	$610	48.8%
2009	1,259	595	664	47.2
2010	1,460	534	926	36.6
2011	1,547	542	1,005	35.0
Teachers Retirement System				
2008	$341	$159	$182	46.6%
2009	394	173	221	43.9
2010	477	166	311	34.9
2011	528	165	363	31.3
Judiciary Retirement System				
2008	$20	$7	$13	36.7%
2009	22	11	11	50.0
2010	28	11	17	39.1
2011	30	11	19	36.1
Total				
2008	$1,553	$748	$805	48.1%
2009	1,675	778	897	46.4
2010	1,965	710	1,255	36.1
2011	2,105	718	1,387	34.1

(1) The actuarially recommended contributions are based on the information contained in the actuarial valuations for the Retirement Systems as of June 30, 2010.

(2) The actual employer contributions for fiscal year 2011 are based on the statutory employer contribution plus the expected pay-as-you-go contributions for System Administered Pension Benefits, as set forth in the actuarial valuations as of June 30, 2010.

(3) Represents the difference between the actuarially recommended pension contribution and the actual contribution from the participating employers.

Source: Information regarding the actuarially recommended contributions was derived from the June 30, 2010 actuarial valuation reports for the Retirement Systems. Information regarding the actual contributions for the Retirement Systems was provided by the Retirement Systems.

Based on the current funding requirements of the Retirement Systems, the UAAL of the Retirement Systems will continue to increase indefinitely into the future instead of being amortized and future scheduled contributions at the current funding rates will not be sufficient to make future benefit payments when due. Additional funding from the Commonwealth will ultimately be necessary to cover such unfunded obligation. It is estimated that the Commonwealth would be responsible for approximately 64% of any such funding deficiency of the Employees Retirement System and approximately 74% of the combined funding deficiency of the Retirement Systems, with the balance being the responsibility of the municipalities and participating public corporations.

Funding Shortfalls. For several fiscal years, actual employer and employee contributions to each of the Retirement Systems have been lower than annual Basic System Pension Benefits payments and administrative expenses. These shortfalls in contributions over the amounts required to pay Basic System Pension Benefits and expenses are referred to herein as "funding shortfalls." The funding shortfalls, however, do not reflect the actual cash flow position of the Retirement Systems, which is affected, among other things, by their investment and financing activities. One type of investment that has particularly contributed to the deterioration of the Retirement Systems' actual cash position has been the increase in personal loans to their members, as discussed below under "*Factors That Have Contributed to Deterioration in Financial Solvency of the Employees Retirement System*."

The Retirement Systems have been forced to cover the funding shortfalls with investment income, loans from financial institutions and various non-recurring sources of funds. In some fiscal years, the funding shortfall has also exceeded the investment income of the Retirement Systems, causing the Systems' assets to decline and adversely affecting the funded status.

Besides using investment income to cover benefit payments, the Employees Retirement System has covered some of its historical funding shortfalls with the sale of investment portfolio assets and proceeds of loans from the Treasury Department or other financial institutions, some of which have been collateralized with the System's assets. During 2008, the Employees Retirement System issued approximately $2.9 billion of Senior Pension Funding Bonds (the "Pension Bonds"), for which repayment the Employees Retirement System pledged all employer contributions made after the issuance of the bonds. The Pension Bonds increased the funds of the Employees Retirement System currently available to pay pension benefits. Although the original expectation was that the Employees Retirement System's investment earnings on the proceeds of the Pension Bonds would exceed the cost of the debt, as further discussed below, the Employees Retirement System's investment earnings on the proceeds of the Pension Bonds have in fact been lower than the cost of the Pension Bonds. As a result of market declines since the issuance of the Pension Bonds, the market value of some of the investments made with Pension Bonds proceeds is below their original cost. Thus, to date, the Pension Bonds transactions have negatively affected the UAAL of the Employees Retirement System.

The table below shows the funding shortfalls for each of the last five fiscal years for each of the Retirement Systems.

Funding Shortfalls
(in millions)

Fiscal Year Ending June 30,	Employer and Member Contributions[1]	Basic System Benefit Payments and Administrative Expenses[2]	Net Funding Shortfall
Employees Retirement System			
2007	713.2	(823.1)	(109.9)
2008	726.4	(1,011.3)	(284.9)
2009	762.4	(1,190.3)	(427.9)
2010	726.5	(1,269.0)	(542.5)
2011	671.5	(1,364.3)	(692.8)
Teachers Retirement System			
2007	256.5	(387.9)	(131.4)
2008	248.8	(439.9)	(191.1)
2009	262.9	(443.9)	(181.0)
2010	249.3	(499.5)	(250.2)
2011	236.1	(504.20	(268.1)
Judiciary Retirement System			
2007	9.5	(14.7)	(5.3)
2008	9.8	(15.4)	(5.6)
2009	13.1	(17.2)	(4.1)
2010	13.1	(18.4)	(5.3)
2011	12.8	(19.2)	(6.5)

(1) Represents the statutory employer and member contributions and does not include amounts received from employers on account of System Administered Pension Benefits.
(2) Includes, in the case of the Employees Retirement System, principal and interest paid on the Pension Bonds for fiscal years 2008, 2009 and 2010 and 2011 in the amounts of $47 million, $187 million, $188 million and $189 million, respectively.
Source: Information obtained from each of the Retirement Systems.

The Employees Retirement System anticipates that, based on the current contributions and benefit structure, its future cash flow needs for disbursement of benefits to participants, administrative expenses and debt service are likely to continue to exceed the sum of the employer and employee contributions received and its investment and other recurring income. For fiscal year 2012, the Employees Retirement System expects to have a funding shortfall (after payment of debt service on the Pension Bonds) of $741 million and this negative trend is expected to continue. Based on the Employees Retirement System's current funding and disbursement projections (which reflect continued funding shortfalls) and other assumptions, the actuarial valuation as of June 30, 2010 states that the System is being rapidly disfunded and projects that its net assets (total assets minus the Pension Bonds and other liabilities) will be depleted by fiscal year 2014 and its gross assets will be depleted by fiscal year 2019. This means that during the period from fiscal year 2014 through fiscal year 2019, benefits are expected to be paid from the proceeds of the Pension Bonds, and that after depletion of the gross assets, there would be no funds remaining to pay pension benefits or debt service on the pension obligation bonds. As a result of the increases in employer contributions adopted in July 2011, as described below, the Administrator of the Retirement Systems projects that the period before depletion of the assets will be extended by three to four years.

The Teachers Retirement System has also covered funding shortfalls during the prior five fiscal years through the sale of investment portfolio assets. For fiscal year 2012, the Teachers Retirement System expects to have a funding shortfall of approximately $287 million, and this negative trend is expected to continue. Based on the Teachers Retirement System's current funding and disbursement projections (which reflect continued funding shortfalls) and other assumptions, the actuarial valuation as of June 30, 2010 states that the System is being gradually disfunded and projects that its net and gross assets will be depleted by fiscal year 2020. As a result of the increases in employer contributions adopted in July 2011, as described below, the Administrator of the Retirement Systems projects that the period before depletion of the assets will be extended by three to four years.

The Judiciary Retirement System has also experienced funding shortfalls during the last five fiscal years and has used investment income to cover some of these shortfalls. For fiscal year 2012, the Judiciary Retirement System expects to have a funding shortfall of approximately $8.5 million, and this negative trend is expected to continue. Based on the Judiciary Retirement System's current funding and disbursement projections (which reflect continued funding shortfalls) and other assumptions, the actuarial valuation as of June 30, 2010 states that the System is being disfunded and projects that its net and gross assets will be depleted by fiscal year 2018.

The estimated years for depletion of the assets stated above could vary depending on how actual results differ from the assumptions used in the actuarial valuations, as well as based on any future changes to the contribution and benefits structures of the Retirement Systems.

The consulting actuaries have recommended that the funding requirements of the Retirement Systems be significantly increased in light of (i) the expected negative net cash flows and exhaustion of plan assets, (ii) the forecasted decrease in funded status, and (iii) the actuarially recommended contributions which significantly exceed actual employer contributions.

Factors That Have Contributed to Deterioration in Financial Solvency of the Employees Retirement System. On June 30, 2010, the Employees Retirement System and GDB, as fiscal agent, retained Conway MacKenzie, Inc ("CMI"), a financial advisory firm, to identify and analyze key events and decisions that have contributed to the current financial crisis of the Employees Retirement System, including the deterioration of its funded ratio. CMI issued its report in October 2010. In its report, CMI identified the following five factors as fundamental in the deterioration of the financial health of the Employees Retirement System: (i) historical inadequate funding procedures, (ii) special laws, (iii) early retirement programs, (iv) personal loans, and (v) the 2008 issuances of Pension Bonds.

The report reviews the historical funding levels of the Employees Retirement System and concludes that the Employees Retirement System has been underfunded since its inception in 1951, essentially as a result of statutory funding rates that fall below actuarially determined contribution rates. In addition to inadequate annual contributions, CMI notes that investment returns and other recurring income have been insufficient to cover annual benefit payments and operating expenses, resulting in cash flow shortfalls that have forced the Employees Retirement System to liquidate plan assets.

CMI also identified the enactment of numerous special laws, which have granted incremental retirement benefits to participants beyond those provided by Act 447 and Act 1 of 1990, as having exacerbated the deteriorating financial condition of the Employees Retirement System. Many special laws were adopted without the Government securing a viable, long-term source of funding for such additional benefits, including the adoption of special laws during periods when the Government was incurring in budgetary deficits. As a result, the Employees Retirement System was forced to fund the benefits granted under these special laws, resulting in significant past-due receivables from the Commonwealth and participating public corporations and municipalities.

The adoption of several early retirement programs is also identified as having affected the financial solvency of the Employees Retirement System. These programs were adopted in order to reduce the size of the public workforce and thereby decrease payroll costs. These programs, however, were generally not accompanied by up-front funding of the associated retirement costs and had a negative cash flow impact on the Employees Retirement System as the System funded early retirement benefits without timely reimbursement from the Commonwealth or sponsoring public corporation or municipality. In addition, the CMI report notes that it appears that many of these programs did not ultimately result in their intended goals of reducing the size of the public workforce.

Another factor identified by CMI as having contributed to the deterioration of the Employees Retirement System is the adoption in 2007 of an increase in the maximum loan balance for personal loans to members, from $5,000 to $15,000. This increase has resulted in a significant cash flow drain to the Employees Retirement System, amounting to approximately $600 million during the last four fiscal years. Although the loans are secured by the employee contributions and collected through payroll withholdings, the significant cash flow to provide personal loans has required the liquidation of plan assets. As a result, a significant percentage of the Employees Retirement System's assets are now invested in personal loans that are illiquid investments.

The CMI report also addressed the 2008 issuances of approximately $2.9 billion in Pension Bonds. The Pension Bonds were issued with the intent of increasing the funds available to the Employees Retirement System to pay benefit obligations and to reduce the UAAL. The Employees Retirement System expected to achieve these goals by investing the proceeds of the Pension Bonds at a higher return than the cost of the debt, thereby achieving a positive arbitrage. However, CMI found that potential risks were not thoroughly or properly analyzed. In fact, the investment of the Pension Bonds proceeds have resulted in a negative arbitrage as the Pension Bonds are currently costing the System more than what it is earning on the investment proceeds. Thus, to date, the transactions have worsened the funded ratio of the Employees Retirement System.

Finally, the CMI report addresses governance deficiencies and states that many of the measures described above, and in particular the issuances of Pension Bonds, were adopted and implemented without conducting any rigorous analysis of their impact on the financial condition of the Employees Retirement System and the risks associated with the measures. The report concludes that immediate and dramatic changes to the structure of the Employees Retirement

System are necessary to avoid full depletion of the System's net assets in the near future, as discussed above.

Impact of Funding Shortfall on the Commonwealth. The Commonwealth and other participating employers are ultimately responsible for any funding deficiency in the Retirement Systems. The depletion of the assets available to cover retirement benefits will require the Commonwealth and other participating employers to cover such funding deficiency. Due to its multi-year fiscal imbalances previously mentioned, however, the Commonwealth is currently unable to make the actuarially recommended contributions to the Retirement Systems. If the Commonwealth fails to take action to address the retirement systems' funding deficiency, the continued use of investment assets to pay benefits as a result of funding shortfalls and the resulting depletion of assets could adversely affect the ability of the Retirement Systems to meet the rates of return assumed in the actuarial valuations, which could in turn result in an earlier depletion of the Retirement Systems' assets and a significant increase in the unfunded actuarial accrued liability. Ultimately, since the Commonwealth's General Fund is required to cover a significant amount of the funding deficiency, the Commonwealth would have difficulty funding the annual required contributions unless it implements significant reforms to the retirement systems, obtains additional revenues, or takes other budgetary measures.

Efforts to Address Cash Flow Shortfall and Improve Funding Ratio. The Retirement Systems is evaluating measures to improve the financial solvency of the Retirement Systems. In order to maintain the long-term fiscal integrity of the Retirement Systems and their ability to pay required benefits to their members, a combination of some or all of the following will be required: (i) a substantial increase in contributions by the Commonwealth and the participating employers, and (ii) actions resulting in changes to liabilities of the Retirement Systems. Because of the multi-year fiscal imbalances mentioned above, the Commonwealth is currently unable to make the actuarially recommended contributions to the retirement systems.

In March 2010, the Governor of Puerto Rico established a special commission to make recommendations for improving the financial solvency of the Retirement Systems. The Commission issued its report on October 21, 2010. The Commission's report does not make a consensus set of recommendations for addressing the financial solvency of the Retirement Systems, but rather discusses the principal recommendations made by different members of the Commission in the following areas: (i) employer and employee contributions, (ii) benefit structure, (iii) retirement age, (iv) benefits under special laws, (v) early retirement programs, (vi) mortgage loans and personal loans, and (vii) governance structure. All members of the Commission agreed that there has to be an increase in employer contributions, while some members also recommended an increase in employee contribution rates. One of the proposals was that employer contribution rates be increased by 1% of payroll per year for the next 10 to 15 years. In the benefits areas, the recommendations included various proposals to reduce or limit benefits, such as eliminating merit pensions, establishing caps on benefits, increasing the retirement age in order to receive full benefits and modifying or eliminating some benefits granted under special laws. Some members of the Commission also recommended prohibiting all future early retirement programs unless they are actuarially positive to the Retirement Systems. In order to address the liquidity position of the Retirement Systems, various members of the Commission recommended eliminating the loan programs or restricting their use. Various members also commented that improvements to the governance structure of the Retirement

Systems was necessary, as it appeared that in the past governance had not been as rigorous as it should have been. Other recommendations included increasing penalties for late payments by participating employers and creating other dedicated revenue sources for the Retirement Systems, such as a special lottery drawing or a special tax on government contractors.

The administration assigned to a task force headed by the Secretary of Labor the evaluation of the Commission's recommendations. As a result of the Commission's report and the Government's analysis, the Governor submitted various bills to the Legislative Assembly to address in part the retirement systems' financial condition. One of such bills was enacted as Act Act 96. On June 23, 2011, in accordance with Act 96, $162.5 million of funds on deposit in the Corpus Account of the Puerto Rico Infrastructure Development Fund were contributed to the Employees Retirement System and invested in capital appreciation bonds issued by COFINA maturing annually on August 1, 2043 through 2048 and accreting interest at a rate of 7%. The principal amount of the COFINA bonds will grow to an aggregate amount of approximately $1.65 billion at their maturity dates.

Another bill submitted by the Governor was enacted as Act 114 and Act 116. These Acts provide an increase in employer contributions to the Employee Retirement System and the Teachers Retirement System of 1% of covered payroll in each of the next five fiscal years and by 1.25% of covered payroll in each of the following five fiscal years. As a result of these increases, the Employee Retirement System and the Teachers Retirement System would receive approximately $36 million and $14 million, respectively, in additional employer contributions during fiscal year 2012, and the additional employer contributions are projected to increase gradually each fiscal year (by an average aggregate increase of $71 million per fiscal year) to approximately $494 million and $195 million, respectively, by fiscal year 2021. The additional employer contributions for fiscal year 2012 have been included in the approved budget for such fiscal year. With respect to the increases in the employer contributions corresponding to the municipalities, Act 116 provides that the increases for fiscal years 2012, 2013 and 2014 will be paid for by the Commonwealth from the General Fund budget, representing approximately $6.3 million, $12.8 million and $19.7 million in fiscal years 2012, 2013 and 2014, respectively. The tables below show the projected additional contributions to the Employees Retirement System and the Teachers Retirement System as a result of Act 116 based on the expected payroll assumptions used in the actuarial reports as of June 30, 2010. The Government expects that the portion of the additional employer contributions under Act 114 and Act 116 corresponding to employees whose salaries are reimbursed to the Commonwealth by the Federal government under various programs will also be received from the Federal government and thus will not be an additional burden on the General Fund. The Government is currently evaluating what portion of the additional employer contributions it expects to recover from the Federal government under such programs.

Projected Additional Employer Contributions
Employees Retirement System
($ in millions)

Fiscal Year	Original Employer Contribution Rate	Additional Employer Contribution Rate	Total Employer Contribution Rate	Expected Payroll	Original Employer Contribution	Additional Employer Contribution	Total Employer Contribution
2011	9.275%	0.000%	9.275%	$3,610	$335	$ 0	$335
2012	9.275%	1.000%	10.275%	3,674	341	36	377
2013	9.275%	2.000%	11.275%	3,750	348	75	423
2014	9.275%	3.000%	12.275%	3,826	355	115	470
2015	9.275%	4.000%	13.275%	3,900	362	156	518
2016	9.275%	5.000%	14.275%	3,978	369	199	568
2017	9.275%	6.250%	15.525%	4,055	376	253	629
2018	9.275%	7.500%	16.775%	4,133	383	310	693
2019	9.275%	8.750%	18.025%	4,212	391	368	759
2020	9.275%	10.000%	19.275%	4,295	398	430	828
2021	9.275%	11.250%	20.525%	4,383	406	494	900

Projected Additional Employer Contributions
Teachers Retirement System
($ in millions)

Fiscal Year	Original Employer Contribution Rate	Additional Employer Contribution Rate	Total Employer Contribution Rate	Expected Payroll	Original Employer Contribution	Additional Employer Contribution	Total Employer Contribution
2011	8.500%	0.00%	8.50%	$1,344	$114	$ 0	$114
2012	8.500%	1.00%	9.50%	1,382	117	14	131
2013	8.500%	2.00%	10.50%	1,421	121	28	149
2014	8.500%	3.00%	11.50%	1,459	124	44	168
2015	8.500%	4.00%	12.50%	1,498	127	60	187
2016	8.500%	5.00%	13.50%	1,538	131	77	208
2017	8.500%	6.25%	14.75%	1,578	134	99	233
2018	8.500%	7.50%	16.00%	1,618	137	122	259
2019	8.500%	8.75%	17.25%	1,657	141	145	286
2020	8.500%	10.00%	18.50%	1,695	144	170	314
2021	8.500%	11.25%	19.75%	1,734	147	195	342

Because of the Commonwealth's current budgetary constraints and the significant underfunding of the Retirement Systems discussed above, however, improving the financial solvency of the Retirement Systems will require the adoption of other measures mentioned above and it will take several years before a significant improvement is achieved. The financial situation of the Retirement Systems presents a budgetary challenge to the Commonwealth. The required increase in employer contributions may have an adverse impact on the Commonwealth's budgetary situation.

A fourth bill with respect to the Employees Retirement System was enacted as Act No. 196 of September 18, 2011, which authorized the Employees Retirement System to sell or pledge personal and mortgage loans in its portfolio. This bill also set up a loan program for members of the Employees Retirement System thorough certain financial institutions, while also limiting the amount of employee contributions that a member can pledge as collateral for a loan.

In addition to these measures, on August 8, 2011, the Board of Trustees of the Employees Retirement System adopted a new regulation regarding the rules relating to the concession of personal loans to its members, which, among other changes, lowered the maximum amount of those loans from $15,000 to $5,000. This change is expected to improve gradually the Employees Retirement System's liquidity.

On July 2, 2010, the Government enacted Act 70 ("Act 70"), which is designed to reduce Government expenditures by providing a voluntary early retirement window for central government employees. At the same time, Act 70 is expected to have a positive actuarial impact on the UAAL of the Employees Retirement System and the Teachers Retirement System. Under Act 70, central government employees meeting certain years of service criteria who opted for early retirement by January 14, 2011 receive a higher pension benefit rate than they would otherwise be entitled to receive based on their current years of service, but such pension rate is lower than what they would have been entitled to if they had waited to meet the full vesting requirements. Pursuant to Act 70, the Commonwealth, as employer, will continue making the applicable employer contributions to the Employees Retirement System and the Teachers Retirement System, as well as make payments to cover the annuity payments to the employees opting for the early retirement window, until both the years of service and age requirements for full vesting would have occurred, at which time the applicable Retirement System will continue making the annuity payments. As of September 30, 2011, approximately 3,373 employees participated of the benefits provided by Act 70.

Statements of Plan Net Assets and Changes in Plan Net Assets. The following tables present the Statement of Plan Net Assets and Statement of Changes in Plan Net Assets of each of the Retirement Systems for fiscal years 2008, 2009, 2010 and 2011.

The Commonwealth of Puerto Rico
Employees' Retirement System
Statements of Plan Net Assets*
As of June 30, 2008, 2009, 2010 and 2011**
(in thousands)

ASSETS	June 30, 2011 **	2010	2009	2008
CASH AND SHORT TERM INVESTMENTS				
Deposits at Commercial Banks	220,852	$ 54,175	$ 21,792	$ 84,439
Deposits with Treasury Department	134,319	110,931	103,527	23,099
Deposits with GDB:				
Unrestricted	51,396	51,446	79,500	54,438
Restricted	411,946	741,082	1,028,878	1515,042
Restricted Cash Bonds	333,153	172,226	193,537	--
Total Cash and Short Term Investment	1,151,666	1,129,860	1,427,234	1,677,018
SECURITIES LENDING, COLLATERAL INVESTED				
Marketable Securities:				
Notes and Bonds	963,414	563,454	565,366	547,414
Stocks	1,270,736	1,492,386	1,477,945	2,018,090
Master Repo		--	--	--
Private Equity Investments	65,457	55,307	34,922	42,294
Total Investments	2,299,607	2,111,147	2,078,233	2,607,798
LOANS TO PLAN MEMBERS				
Mortgage	148,155	141,588	128,365	116,022
Personal	1,048,982	1,018,498	916,934	771,367
Cultural Trips	75,197	63,729	50,317	38,344
PEC	3,044	2,340	1,827	1,098
Total Loans to Plan Members	1,275,380	1,226,155	1,097,443	926,831
Investment in PRTA Holdings	0	--	--	--
Total cash, investments and loans to plan members	4,726,653	4,467,162	4,602,910	5,211,647
RECEIVABLES:				
Employers	184,152	273,139	289,427	246,167
General Fund	6,147	11,222	7,833	854
Judiciary Retirement System	881	19,138	17,942	16,714
Investment Sales	9,546	12,189	24,509	9,800
Accrued Interest	7,594	6,597	6,939	3,279
Dividend Receivable		--	--	--
Other	4,595	3,893	5,081	58,210
Total Receivables	212,915	326,178	351,731	335,024
CAPITAL ASSETS	8,951	8,964	9,171	9,839
OTHER ASSETS	6,375	7,224	8,892	8,292
Prepaid Bond Cost	32,172	33,267	34,363	35,462
Total assets	4,987,067	4,842,795	5,007,067	5,600,264
LIABILITIES				
Book overdraft	62,843	22,933	37,961	--
Short Term Obligations		--	--	--
Payables for securities lending	134,319	110,931	103,527	--
Funds of Mortgage Loans and Guarantee Insurance Reserve for Loans	9,596	6,597	6,372	3,863
Investment Purchases	1,854	5,277	13,926	12,694
Accounts Payable and Accrued Liabilities	12,923	12,250	14,228	9,310
Line of Credit		--	--	--
Bonds Payable	3,003,482	2,981,775	2,961,359	2,942,183
Other Liabilities	24,363	21,798	13,675	12,946
Bonds Interest Payable	13,876	13,876	13,876	12,182
Total Liabilities	3,263,256	3,175,437	3,164,924	2,993,178
Net Assets Held in Trust for Pension Benefits	**1,723,811**	**$1,667,358**	**$1,842,143**	**$2,607,086**

* Totals may not add due to rounding.

** Preliminary, unaudited numbers.

The Commonwealth of Puerto Rico
Employees' Retirement System
Statements of Changes in Plan Net Assets*
As of June 30, 2008, 2009, 2010 and 2011**
(in thousands)

ADDITIONS:	June 30, 2011**	2010	2009	2008
Contributions:				
Employer	349,207	$ 381,243	$ 400,405	$ 380,833
Participating employees	322,008	345,265	362,040	345,614
Other Special Laws		171,842	175,254	141,724
Early Retirement	305	3,399	47,146	16,789
Special Laws 127	187,369	188,843	17,000	884,961
Total Contributions	858,889	918,750	1,001,845	799,282
Investment (loss) Income:				25,129
Realized Gain or Loss	472,076	148,173	(152,583)	(238,509)
Unrealized Gain or Loss		67,838	(405,969)	10,347
Dividend Income	7,334	10,663	15,774	115,763
Interest Income	335,283	179,586	198,734	(87,270)
Total	814,703	406,259	(344,044)	446,910
Less Investment Expense	6,483	(7,649)	(7,589)	6,197
Insurance Premium				24,927
Other Income	49,257	31,783	35,878	(62,904)
Net Investment Income	857,477		430,393	(315,755)
				822,034
Total Additions	1,716,366	1,349,143	686,090	1,253,124
DEDUCTIONS:				932,701
Annuities	1,133,926	1,047,695	970,843	16,789
Special Laws 127		17,000	17,000	18,712
Benefits under Special Laws	187,369	171,842	175,254	
Death Benefits	7,932	12,968	11,532	3,020
Refunds of Contributions:				37,346
Employers	992	1,469	2,013	--
Participating Employees	90,203	43,677	32,517	1,092
Personal Loans Adjustment		--	--	18,204
Insurance Claims on Loans				
Other Expenses	13,199	7,888	22,415	46,996
Administrative Expenses	34,583	33,063	32,590	
Interest on Bonds	189,342	188,055	186,869	1,106,472
Total Deductions	1,657,546	1,523,928	1,451,033	(284,415)
Net (decrease) Increase	58,820	(174,785)	(764,943)	350,170
				2,891,501
Net Assets Held in Trust for Pension Benefits:				
Beginning of the Year	1,664,991	1,842,143	2,607,086	$ 380,833
End of Year	**$1,723,811**	**$1,667,358**	**$1,842,143**	**$2,891,501**

* Totals may not add due to rounding.
** Preliminary, unaudited numbers.

The Commonwealth of Puerto Rico
Teachers Retirement System
Statements of Plan Net Assets*
As of June 30, 2008, 2009, 2010 and 2011**
(in thousands)

	June 30, 2011**	2010	2009	2008
ASSETS				
Cash:				
Cash and cash equivalents	$ 168,206	$ 72,692	$ 65,885	$ 324,846
Cash with fiscal agent	110	-	450	297
Cash restricted		-	-	-
Cash deposited with Government Development Bank for Puerto Rico	3,291	3,288	3,276	3,255
Total Cash	171,608	75,980	69,611	328,398
Investments, at fair value:				
Bonds and notes	591,769	397,109	425,911	490,007
Stocks	1,211,084	1,295,232	1,259,169	1,796,817
Total investment at fair value	1,802,853	1,692,341	1,685,080	2,286,824
Other investments:				
Mortgage notes acquired from third parties				
Private equity investments	25,630	26,683	26,139	37,630
Total investments	1,828,483	1,719,024	1,711,219	2,324,454
Loan to plan members:				
Mortgage	128,312	119,937	109,508	103,759
Personal	276,692	288,463	288,410	271,510
Cultural trips	1,660	1,481	1,462	1,355
Total loans to plan members	406,664	409,881	399,380	376,624
Total investments and loans	2,235,147	2,128,905	2,180,210	3,029,476
Accounts receivable:				
Receivable for investments sold	2,320	332	23,231	4,693
Accrued interest and dividends receivable	3,982	4,584	5,445	6,395
Other	44,883	56,085	2,930	15,141
Total accounts receivable	51,185	61,001	31,606	26,229
Property and equipment, net	22,204	22,970	26,167	26,223
Other assets	472	832	876	451
Total Assets	2,480,616	2,289,688	2,238,859	3,082,379
LIABILITIES				
Investments purchased	1,701	2,722	18,981	7,952
Payable for securities lending	70,938	48,673	46,751	274,372
Cash overdraft in cash with fiscal agent		2,199	-	-
Accounts payable	1,530	1,476	4,188	3,688
Obligation under capital lease		-	-	12
Accrued expenses	13,321	6,184	5,925	5,361
Line of credit		-	-	-
Escrow fund of mortgage loans and guarantee	6,322			
insurance reserve for loans to plan members		5,763	4,580	4,641
Bonds payable		-	-	-
Other liabilities	941	694	841	1,007
Total liabilities	94,753	67,711	81,266	297,033
Net Assets Held in Trust for Pension Benefits	2,385,863	$2,221,977	$2,157,593	$2,785,346

* Totals may not add due to rounding.
** Preliminary, unaudited numbers.

The Commonwealth of Puerto Rico
Teachers Retirement System
Statements of Changes in Plan Net Assets*
As of June 30, 2008, 2009, 2010 and 2011**
(in thousands)

	June 30, 2011**	2010	2009	2008
ADDITIONS:				
Contributions:				
Participating Employees	123,297	$129,888	$136,305	$127,566
Employer	112,071	118,127	125,165	117,065
Contributions transferred from other	828			
systems**		1,265	1,479	4,181
Special	47,753	46,572	75,548	68,085
Total contributions	283,949	295,852	338,497	316,897
Investment Income:				
Interest income	57,008	61,303	66,927	67,825
Dividend Income	6,915	10,111	13,194	15,629
Net appreciation (depreciation) in fair value of investments	421,923	203,265	(518,862)	(276,573)
Total investment income	485,845	274,679	(438,741)	(193,119)
Less investment expense	4,682	4,735	4,660	6,847
Net investment income	481,163	269,944	(443,401)	(199,966)
Other income	968	53,771	2,444	1,735
Total additions	766,080	$ 619,567	($ 131,794))	$ 118,666
DEDUCTIONS:				
Benefit paid to participants:				
Annuities and death benefits	513,874	470,683	442,542	414,334
Special benefits	48,286	47,870	51,951	49,742
Refunds of contributions	8,465	7,847	5,313	6,427
Administrative expenses	31,570	28,783	25,485	25,537
Total deductions	602,195	555,183	525,291	496,040
Net increase in net assets held in trust for	163,885			
pension benefits		64,384	(627,753)	(377,374)
Net assets held in trust for pension benefits	2,221,977			
Beginning of year	2,385,863	2,157,593	2,785,346	3,162,720
End of year	2,221,977	$2,221,977	$2,157,593	$2,785,346

* Totals may not add due to rounding.
** Preliminary, unaudited numbers.

The Commonwealth of Puerto Rico
Judiciary Retirement System
Statements of Plan Net Assets*
As of June 30, 2008, 2009, 2010 and 2011**
(in thousands)

ASSETS	**June 30,2011****	**2010**	**2009**	**2008**
Cash and Investments:				
Cash and Cash Equivalents	6,409	$ 4,008	$ 3,985	$ 2,519
Cash Deposited with GDB or Treasury	1,011			
Department:		28	2,353	267
Collateral from Securities Lending	3,218	1	1,482	
Total Cash	10,638	4,037	7,820	2,786
Receivables:				
Accrued Interest	263	271	215	237
Investment Sales		41	117	196
Other	27	27	28	25
Total receivables	290	339	360	458
Marketable Securities:				
Notes and Bonds	39,954	25,973	22,805	22,169
Stocks	22,136	50,275	44,634	61,377
Total Investments	62,090	76,248	67,439	83,546
Loans and Interest Receivable from Members:				
Mortgage	17	20	8	8
Personal	750	702	462	394
Cultural Trips	77	47	60	45
Total Loans to Plan Members	844	769	530	448
Total cash, investments and loans to plan members	73,863	81,393	76,149	87,239
LIABILITIES				
Due to Treasury Department	5,560	5,842	4,513	--
Due to the Employee's Retirement System of the	881			
Government of Puerto Rico		19,138	17,942	16,714
Collateral from Securities ending	3,218		1,482	
Escrow Funds to plan Members and Guarantee	66			
Insurance		63	59	56
Investment Purchases	2	868	867	345
Other Liabilities	161	72	720	812
Total Liabilities	9,888	25,983	25,583	17,927
Net Assets Held in trust for Pension Benefits	**63,975**	**$ 55,410**	**$ 50,566**	**$ 69,311**

* Totals may not add due to rounding.
** Preliminary, unaudited numbers.

The Commonwealth of Puerto Rico
Judiciary Retirement System
Statements of Changes in Plan Net Assets*
As of June 30, 2008, 2009, and 2010 and 2011**
(in thousands)

	June 30, 2011**	2010	2009	2008
ADDITIONS:				
Contributions:				
Employer	9,966	$10,021	$9,970	$6,705
Participating employees	2,789	3,104	3,138	3,076
Special Laws	629	629	691	
Total Contributions	13,384	13,754	13,799	9,781
Investment Income:				
Realized Gain or Loss	12,928	5,644	(3,158)	1,031
Unrealized Gain		1,741	(13,582)	(8,988)
Dividend Income	176	211	218	267
Interest Income	1,352	1,284	1,313	1,553
Total	14,456	8,880	(15,209)	(6,137)
Less Investment Expense	162	164	(170)	(197)
Other Income	10	804	50	--
Net Investment Income	14,304	9,520	(15,329)	(6,333)
Total Additions	27,688	23,274	(1,530)	3,448
DEDUCTIONS:				
Annuities	18,617	17,268	15,538	14,419
Benefits Under Special Laws		629	691	
Refunds to Participating Employees		--	--	169
Administrative Expenses	506	533	986	1,022
Total Deductions	19,123	18,430	17,215	15,610
Net Increase	8,565	4,844	(18,745)	(12,162)
Net Assets Held in Trust for Pension Benefits:				
Beginning of the Year	55,410	50,566	69,311	81,473
End of Year	**63,975**	**$55,410**	**$50,566**	**$69,311**

* Totals may not add due to rounding.
** Preliminary, unaudited numbers.

POST-EMPLOYMENT BENEFITS OTHER THAN PENSIONS

In addition to the pension benefits, the Commonwealth provides non-pension post-employment benefits that consist of a medical insurance plan contribution for retired employees meeting the service credit eligibility requirements. These benefits are administered by the Retirement Systems. The medical insurance plan contribution is a payment of up to $100 per month to the eligible medical insurance plan selected by the retiree or disabled member.

The Commonwealth funds these post-employment benefits on a "pay-as-you-go" basis from the General Fund, which means that the Commonwealth does not pre-fund, or otherwise establish a reserve or other pool of assets against the medical insurance plan contribution expenses that the Commonwealth may incur in future years. For fiscal year 2011, the Commonwealth paid $123.4 million for these benefits for the eligible retirees of the Retirement Systems (including retirees of public corporations and municipalities, which are also paid for by the Commonwealth). For fiscal year 2012, these benefits are expected to amount to $138.9 million.

In accordance with the provisions of GASB Statement No. 45, the Commonwealth is required to quantify and disclose its obligations to pay non-pension post-employment benefits to current and future retirees. The most recent actuarial valuation reports of these benefits are dated as of June 30, 2010. Many of the actuarial assumptions used to project the actuarial accrued liability for these benefits are the same as those used to determine the accrued actuarial liabilities of the Retirement Systems. The following table sets forth, according to the actuarial valuations, the actuarial accrued liability, UAAL, covered payroll and UAAL as a percentage of covered payroll for the non-pension post-employment benefits of the active and retired members of each of the Retirement Systems. Since these benefits are not pre-funded, as discussed above, the UAAL is equal to the actuarial accrued liability.

Post-Employment Benefits Other Than Pensions
Actuarial Valuations as of the Indicated Fiscal Years
(in millions)

Fiscal Year Ending June 30,	Actuarial Value of Assets	Actuarial Accrued Liability[1]	Unfunded Actuarial Accrued Liability	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
Employees Retirement System						
2007	-	$1,557	$1,557	0%	$4,246	36.7%
2009	-	1,633	1,633	0	4,293	38.0
2010	-	1,646	1,646	0	3,818	43.1
Teachers Retirement System						
2007	-	$652	$652	0%	$1,370	47.6%
2009	-	750	750	0	1,418	52.9
2010	-	694	694	0	1,370	50.7
Judiciary Retirement System						
2007	-	$5	$5	0%	$31	15.0%
2009	-	6	6	0	31	18.5
2010	-	6	6	0	32	18.1

(1) The actuarial accrued liability is the liability or obligation for benefits earned by active and retired employees through the valuation date based on certain actuarial methods and assumptions.

The following table shows the actuarially recommended contributions, actual employer contributions and resulting amount unfunded and percent contributed for the post-employment benefits other than pensions administered by each of the Retirement Systems' for the last three fiscal years and the current fiscal year.

Schedule of Employer Contributions to Retirement Systems on Account of Post-Employment Benefits Other Than Pensions (in millions)

Fiscal Year Ending June 30,	Actuarially Recommended Contributions[1]	Actual Employer Contributions[2]	Amount Unfunded[3]	Percent Contributed
Employees Retirement System				
2008	$111	$80	$31	72.1%
2009	112	87	25	77.7
2010	128	85	43	66.6
2011	128	90	38	70.3
Teachers Retirement System				
2008	$37	$26	$11	70.6%
2009	38	28	10	73.1
2010	42	28	14	66.7
2011	40	32	8	80.7
Judiciary Retirement System				
2008	$0.4	$0.2	$0.2	55.4%
2009	0.4	0.3	0.1	62.0
2010	0.5	0.3	0.2	61.5
2011	0.5	0.3	0.2	60.4
Total				
2008	$148.4	$106.2	$42.2	71.6%
2009	150.4	115.3	35.1	76.7
2010	170.5	113.3	57.2	66.5
2011	168.5	122.3	46.2	72.6

(1) The actuarially recommended contributions are based on the information contained in the actuarial valuations for the Retirement Systems as of June 30, 2010.

(2) The actual employer contributions for fiscal year 2011 are based on the expected pay-as-you-go amounts for the post-employment benefits other than pensions, as set forth in the actuarial valuations as of June 30, 2010.

(3) Represents the difference between the actuarially recommended pension contribution and the actual contribution from the participating employers.

COMMONWEALTH AUDITED FINANCIAL STATEMENTS

General

For fiscal year 2010, the basic financial statements of the Commonwealth were audited by Deloitte & Touche LLP. Deloitte & Touche LLP did not audit the financial statements of certain activities, funds, and component units identified separately in its report dated April 27, 2011 (which report expresses an unqualified opinion and includes emphasis of matter paragraphs regarding investments held by the Pension Trust Funds whose fair values have been estimated in the absence of readily determinable fair values and the Pension Trust Funds' unfunded actuarial accrued liability and funded ratio as of June 30, 2010). Those financial statements were audited by other independent auditors whose reports were furnished to Deloitte & Touche LLP, and its opinion on the basic financial statements, insofar as it relates to the amounts included in the basic financial statements pertaining to such activities, funds and component units, is based solely on the reports of the other auditors.

The CAFR for fiscal year 2010, which includes the basic financial statements of the Commonwealth for fiscal year 2010, was filed by the Commonwealth with the Municipal Securities Rulemaking Board ("MSRB") through its Electronic Municipal Markets Access System ("EMMA") on April 29, 2011.

The CAFR for fiscal year 2011 is expected to be filed prior to May 1, 2012, which is the deadline under its continuing disclosure undertakings pursuant to Rule 15c2-12 of the Securities and Exchange Commission promulgated under the Securities Exchange Act of 1934, as amended.

Prior Non-Compliance with Continuing Disclosure Obligations

The Commonwealth has made continuing disclosure undertakings in connection with its bond issuances, and has complied with all such covenants, except as hereinafter noted.

The Commonwealth's audited financial statements for the fiscal year ended June 30, 2002 were filed after the Commonwealth's filing deadline of May 1, 2003 because of delays in finalizing such financial statements resulting from the implementation of GASB Statement No. 34 ("GASB 34"). The Commonwealth's audited financial statements for the fiscal year ended June 30, 2003 were also filed after the Commonwealth's filing deadline of April 30, 2004, because of delays in finalizing the financial statements of certain of the Commonwealth's reporting units due to the implementation of GASB 34. The Commonwealth's audited financial statements for the fiscal years ended June 30, 2004, 2006, 2007 and 2008 were also filed after the Commonwealth's respective filing deadlines of May 1, 2005, 2007, 2008 and 2009, because various governmental agencies did not submit their audited financial statements to the central government's external auditors on time, thereby delaying submission of the Commonwealth's audited financial statements. The Commonwealth's audited financial statements for the fiscal year ended June 30, 2009 was also filed after the Commonwealth's filing deadline of May 1, 2010 due to delays in the engagement and transition of new external auditors, the implementation of new government accounting pronouncements, and the restatement of the financial statements of certain discretely presented component units. The Commonwealth's audited financial statements for fiscal years ended June 30, 2004, 2006, 2007 and 2008 were filed by the end of the first quarter of the following fiscal year, while the Commonwealth's audited financial statements for the fiscal year ended June 30, 2009 was filed on October 25, 2010.

The Commonwealth Report for the fiscal year ended June 30, 2008 containing the information described in paragraph 1 above, was filed after the Commonwealth's filing deadline of May 1, 2009. Such Commonwealth Report was filed on June 1, 2009. Except for such Commonwealth Report, the Commonwealth has timely filed the Commonwealth Report for all other fiscal years.

As of the date of this Report, the Commonwealth is in compliance with its continuing disclosure filing requirements related to its outstanding general obligation bonds.

The Commonwealth has established new policies and procedures that it believes will ensure full and timely compliance with all continuing disclosure obligations in the future. Such new policies and procedures include: (i) the assignment of additional resources from local and international audit firms to those component units whose financial statements have not been timely provided to the Commonwealth; (ii) the assignment of dedicated external and internal resources to (a) assist the Central Accounting Division at the Treasury Department in the preparation of complex financial information that has historically delayed the audit and (b) provide periodic and consistent follow up on component unit financial statement deliverables and deadlines; (iii) the execution of a memorandum of understanding between the Treasury Department, OMB and GDB for the coordination of all financial statement related tasks and the designation of GDB, in its role as fiscal agent, to review and monitor the progress of certain component units; and (iv) the establishment of an Audit Oversight Committee comprised of the Treasury Department and GDB personnel in order to continuously monitor the status of the audit and the Commonwealth's financial statements.

PUERTO RICO TAXES, OTHER REVENUES, AND EXPENDITURES

The Secretary of the Treasury has custody of the funds of the central government and is responsible for the accounting, disbursement and investment of such funds. Central government funds are grouped into three major categories or "types" of funds, as follows: (i) Governmental Fund Types, which include the General, Special Revenue, Debt Service (also referred to herein as Redemption), and Capital Project Funds; (ii) Proprietary Fund Types, which include the Enterprise and Internal Service Funds; and (iii) Fiduciary Fund Types, which include the Trust and Agency Funds. These funds do not include funds of the municipalities, because the municipalities are governmental entities with independent treasuries. The Special Revenue Fund is incorporated into the General Fund for financial reporting purposes (but not for budgetary purposes).

The General Fund is the primary operating fund of the Commonwealth. General Fund revenues are broadly based and include revenues raised internally as well as those from non-Puerto Rico sources. Internal revenues consist principally of income, excise and sales and use taxes. Revenues from non-Puerto Rico sources are derived from federal excise taxes and customs duties returned to the Commonwealth. The primary expenditures of the Commonwealth through the General Fund are for grants and subsidies, and personal and other services.

Summary and Management's Discussion of General Fund Results

The following table presents the actual revenues and expenditures of the General Fund on a cash basis for fiscal years 2007, 2008, 2009, 2010 and the preliminary revenues and expenditures for fiscal year 2011. Once the audited financial statements have been completed, the Commonwealth will provide the actual General Fund revenue and expenditure data for fiscal year 2011. The numbers for fiscal year 2011 have not been audited and are subject to audit related adjustments.

The amounts shown in the following table as expenditures may be different than those reflected in the budget or in the Commonwealth's financial statements because the table shows only cash disbursements, while the budget includes all authorized expenditures, regardless of when the related cash is actually disbursed. In addition, transfers to the Redemption Fund (used to pay debt service on the Commonwealth's bonds), which are included in the budget under "debt service," are shown as a deduction from total revenues in calculating "adjusted revenues" in the table and are not included under "expenditures." Finally, certain expenditures incurred in excess of budgeted amounts may not be reflected in the table as expenditures to the extent they are paid from reserve funds, such as moneys in the Budgetary Fund. A discussion of the budget for fiscal years 2011 and 2012 appears below under "Budget of the Commonwealth of Puerto Rico."

Amounts listed under "Other Income" represent recurring General Fund revenues not appropriately attributable to other revenue line items, such as repayment of General Fund advances to municipalities and government agencies and funds. "Other Expenditures" represent recurring General Fund expenditures not appropriately attributable to other expenditures line items, such as advances to government agencies and municipalities, which advances are to be reimbursed to the General Fund by law. Amounts listed under "Capital Outlays and Other Debt Service" represent debt service on obligations and capital expenditures for which the Legislative Assembly has by resolution agreed to appropriate funds. General Fund revenues, expenditures, and transfers as presented in the table differ from the General Fund revenues, expenditures, and transfers as presented in the financial statements of the Commonwealth, as the financial statements reflect an expanded General Fund entity in accordance with generally accepted accounting principles.

Commonwealth of Puerto Rico
General Fund Revenues, Expenditures, and Changes in Cash Balance
(in thousands)

	2007	2008	2009	2010	2011
Revenues:					
Income Taxes:					
Individuals	3,071,655	2,759,305	2,648,261	2,593,598	$2,186,187
Corporations	2,002,718	1,565,534	1,375,596	1,682,321	1,674,087
Partnerships	2,960	1,942	1,839	1,688	3,249
Withheld from non-residents	933,728	1,087,782	1,081,739	830,352	1,000,428
Tollgate taxes	25,083	21,610	19,372	15,034	12,607
Interest	12,112	13,657	11,738	9,902	6,985
Dividends	138,859	59,770	48,663	29,774	26,756
Total income taxes	6,187,115	5,509,600	5,187,208	5,162,669	4,910,299
Sales and use tax	582,560	911,000	797,194	540,348	547,629
Commonwealth excise taxes:					
Alcoholic beverages	279,028	268,094	277,401	284,796	280,963
Foreign (Act 154)	-	-	-	-	677,829
Cigarettes	132,399	119,124	129,429	182,501	201,965
Motor vehicles	396,667	366,341	310,920	350,764	364,188
Other excise taxes	314,340	110,014	86,874	77,978	77,986
Total Commonwealth excise taxes	1,122,434	863,573	804,624	896,039	1,602,931
Property taxes	800	219	1,011	227,812	246,630
Inheritance and gift taxes	4,663	6,600	5,064	3,617	3,101
Licenses	97,610	87,690	96,423	95,768	81,393
Other:					
Lottery	73,014	46,636	51,480	42,826	46,164
Electronic lottery	71,815	105,298	75,213	80,006	55,690
Miscellaneous non-tax revenues	330,064	466,741	284,436	314,754	343,062
Total Other	474,893	618,675	411,129	770,843	444,916
Total revenues from internal sources	8,470,075	7,997,357	7,302,653	7,363,839	7,836,899
Revenues from non-Commonwealth sources:					
Federal excise taxes[1]	377,872	356,827	404,265	352,301	328,527
Customs	14,504	4,846	3,269	-	-
Total revenues from non-Commonwealth sources	392,376	361,673	407,534	352,301	328,527
Total revenues	8,862,451	8,359,030	7,710,187	7,716,140	8,165,426
Other Income (refunds)[2]	(8,335)	(10,797)	148,966	(57,241)[8]	(180,362)
(Transfer) Refunding to Redemption Fund[3]	(512,197)	(202,954)	(607,305)	(447,312)	(86,834)
Proceeds of notes and other borrowings[4]	1,872,096	2,710,000	3,982,893	2,375,000	1,850,000
Repayment of notes and other borrowings[5]	(1,926,273)	(2,580,764)	(3,858,393)	(2,698,818)	(1,850,000)
Receipt of COFINA Bond Proceeds	-	-	3,051,008	2,501,053[9]	1,243,898
Adjusted revenues	8,287,742	8,274,515	10,427,356	9,388,822	976,702
Expenditures:					
Grants and subsidies	3,387,199	3,471,922	3,117,817	3,581,751	3,996,469
Personal services	4,590,962	4,563,192	5,273,590	4,355,111	4,143,299
Other services	594,345	685,112	859,323	822,019	746,755
Materials and supplies	79,186	99,486	109,386	85,906	72,663
Equipment purchases	27,965	49,498	51,204	44,381	60,257
Capital outlays and other debt service	21,576	11,222	211,499	110,850	46,822
Prior year disbursements	92,770	-	-	-	-
Total expenditures	8,794,003	8,880,432	9,622,818	9,000,018	9,066,265
Adjusted revenues less expenditures	(506,261)	(605,917)	804,538	388,804	75,863
Ending cash balance	(506,261)	(1,112,178)	(307,640)	81,164	157,027

(1) Excludes transfers to the Conservation Trust Fund and amounts deposited into a separate account for the promotion of Puerto Rico rums in foreign markets.
(2) Consists of net revenues from the General Fund's non-budgetary funds plus a reserve for future tax refunds reduced by estimated tax refunds.
(3) Consists of amounts to pay principal of and interest on general obligation bonds and notes of the Commonwealth. Does not include amounts deposited directly into the Redemption Fund from non-General Fund revenues.
(4) Consists of proceeds of borrowings from GDB and a syndicate of commercial banks, and proceeds from Commonwealth's Tax and Revenue Anticipation Notes.
(5) Consists of repayments of borrowings from GDB and a syndicate of commercial banks, and repayments of Commonwealth's Tax and Revenue Anticipation Notes.
(6) Includes proceeds of $100 million generated by the issuance of the Commonwealth's Public Improvement Refunding Bonds, Series 2006 A, which were privately placed.
(7) Includes $50 million from the Emergency Fund used for operating expenses.
(8) Includes $201 million transferred to the Commonwealth from the sale of securities in PRIFA's Corpus Account.
(9) Represents the COFINA bond proceeds deposited in the Stabilization Fund

Source: Treasury Department

General Fund Preliminary Revenues for Fiscal Year 2011 Compared to Fiscal Year 2010

General Fund preliminary total revenues (including lottery revenues) for fiscal year 2011 were $8.165 billion, representing an increase of $449.3 million, or 5.8%, from fiscal year 2010 revenues. The major changes from fiscal year 2010 were: (i) decreases in income taxes from individuals of $407.4 million or 15.7%, resulting from the implementation of the tax reform (ii) an increase of $170.1 million in taxes withheld from non-residents, and (iii) an additional $677.8 million from the a new excise tax imposed on entities that purchase products manufactured in Puerto Rico by their affiliates under the provisions of Act 154, discussed below.

General Fund preliminary total expenses (on a cash basis) for fiscal year 2011 amounted to $9.153 billion, which were composed of $9.1 billion of operational expenses and $86.8 million transferred to the redemption fund. The difference between preliminary revenues and expenses for fiscal year 2011 of $900.8 million was covered principally with proceeds from a COFINA bond issue.

General Fund Revenues for Fiscal Year 2010 Compared to Fiscal Year 2009.

General Fund total revenues (including lottery revenues) for fiscal year 2010 were $7.716 billion, representing an increase of $6 million from fiscal year 2009 revenues and an increase of $46 million from budgeted revenues for fiscal year 2010. The principal changes in sources of revenues from fiscal year 2009 include a decrease in the sales and use tax received by the General Fund of $256.8 million due to the increased allocation of this tax to COFINA, as discussed in "Major Sources of General Fund Revenues – Sales and Use Taxes" below. This decrease in the amount of sales and use taxes allocated to the General Fund was fully offset, however, by increases in property taxes and excise taxes on cigarettes and alcoholic beverages of approximately $226.8 million and $60.5 million, respectively, as a result of the temporary and permanent revenue raising measures implemented as part of the Commonwealth's fiscal stabilization plan under Act 7. See "Major Sources of General Fund Revenues – Income Taxes" below. Revenues from income taxes for fiscal year 2010 were approximately the same as in fiscal year 2009, reflecting the continuing impact of the ongoing economic recession.

General Fund total expenses (on a cash basis) for fiscal year 2010 amounted to $9.447 billion, which were composed of $9.0 billion of operational expenses and $447.3 million transferred to the redemption fund. The difference between revenues and expenses for fiscal year 2010 of $1.3 billion was covered principally with proceeds from a COFINA bond issue.

General Fund Revenues for Fiscal Year 2009 Compared to Fiscal Year 2008

General Fund total revenues (including lottery revenues) for fiscal year 2009 were $7.710 billion, representing a decrease of $648.8 million, or 7.8%, from fiscal year 2008 revenues. The major changes from fiscal year 2008 were: (i) decreases in income taxes from individuals of $111 million and in corporate income taxes of $189.9 million, (ii) a decrease of $58.9 million in excise taxes, (iii) a decrease of $182.3 million in miscellaneous non-tax revenues, and (iv) a decrease of $113.8 million in the sales and use tax revenues due primarily to a one-time change in the manner sales and use tax collections are reported by the Treasury Department. Please refer to "Major Sources of General Fund Revenues – Sales and Use Taxes" below further information regarding this reporting change. The decreases in revenues in these categories for fiscal year 2009 as compared to fiscal year 2008 reflect the acceleration of the economic recession during that fiscal year.

General Fund total expenses (on a cash basis) for fiscal year 2009 amounted to $10.230 billion, which were composed of $9.623 billion of operational expenses and $607 million transferred to the redemption fund. The difference between revenues and expenses for fiscal year 2009 of $2.5 billion was covered principally by proceeds from COFINA bond issues.

Fiscal Year 2008 Compared to Fiscal Year 2007

General Fund total revenues (including lottery revenues) for fiscal year 2008 were $8.359 billion, representing a decrease of $234.4 million, or 2.7%, from actual revenues for fiscal year 2007 (excluding the collection of $269 million from special temporary tax measures in fiscal year 2007). The major changes from fiscal year 2007 were: (i) decreases in income taxes from individuals of $312.4 million and in corporate income taxes of $437.2 million, (ii) a decrease of $258.9 million in excise taxes, and (iii) an increase of $328.4 million in the sales and use tax revenues, which had only been in effect for seven and a half months during fiscal year 2007. The decrease in 2008 revenues was principally due to the ongoing economic recession and high oil prices, which directly affected income and excise tax collections.

General Fund total expenses (on a cash basis) for fiscal year 2008 amounted to $9.083 billion, which were composed of $8.880 billion of operational expenses and $203 million transferred to the redemption fund. The difference between adjusted revenues and expenses for fiscal year 2008 of $605.9 million was covered principally by cash-management procedures such as delaying payments to certain vendors and a GDB loan of $190 million.

Major Sources of General Fund Revenues

Income Taxes

The historical revenue data presented in this Report is based on collections realized or accrued under the provisions of the Internal Revenue Code of 1994, as amended (the "PR Code"), which applied to taxable years beginning after June 30, 1995 and ending before January 1, 2011. The PR Code was replaced by the Internal Revenue Code for a New Puerto Rico, enacted as Act 1 of 2011, which will apply for taxable years commencing after December 31, 2010. See "Tax Reform" below. Many of the provisions of Act 1 of 2011 are identical to the equivalent provisions of the PR Code. Thus, unless otherwise noted, the discussion below refers to the provisions of both the PR Code and Act 1 of 2011.

The PR Code imposed a tax on the income of individual residents of Puerto Rico, trusts, estates, and domestic and foreign (if engaged in a trade or business in Puerto Rico) corporations and partnerships at graduated rates. A flat tax was imposed on certain payments made to non-residents of Puerto Rico, which was collected through an income tax withholding.

Individuals. Resident individuals are subject to tax on their taxable income from all sources. The PR Code had four tax brackets for individuals with tax rates of 7%, 14%, 25%, and 33%. The highest income tax bracket applicable to individuals under the PR Code was $50,000.

Under Act 1 of 2011, the highest income tax bracket gradually increases every year for the next six years from $60,000 to $121,500. For taxable years starting before January 1, 2016, the income tax rates applicable to individuals remain unaltered under Act 1 of 2011. After January 1, 2016, the top individual rate is lowered to 30%. See "Tax Reform" below for certain requirements that must be satisfied in order for tax benefits under Act 1 of 2011 to enter into effect for taxable years starting after December 31, 2013. Dividend income from Puerto Rico corporations and certain qualifying foreign corporations is taxed at an income tax rate of 10%.

Gains realized from the sale or exchange of a capital asset by resident individuals, if held for more than six months, is taxed at an income tax rate of 10%.

Interest income in excess of $2,000 on deposit with Puerto Rico financial institutions is taxed at an income tax rate of 10%; the first $2,000 of interest income from such institutions is exempt from taxation. Interest income on certain qualifying debt obligations issued by Puerto Rico corporations and certain qualifying foreign corporations and paid to resident individuals, trusts, estates, corporations and partnerships qualifies for an income tax rate of 10%.

Corporations. Puerto Rico corporations are subject to tax on income from all sources; foreign corporations that are engaged in a trade or business in Puerto Rico are subject to tax on their income from Puerto Rico sources and on income from sources outside Puerto Rico that is effectively connected with the conduct of their trade or business in Puerto Rico. Unless a corporation qualifies for partial exemption from corporate income and other taxes under the tax incentives programs (see "Tax Incentives" under "The Economy" above), it is subject to tax at graduated rates.

In general, the PR Code provided for six income tax brackets for corporations and partnerships, with the highest rate (39%) applicable to net taxable income in excess of $300,000. Gains realized from the sale or exchange of a capital asset, if held for more than six months, were taxed at a maximum regular income tax rate of 15%. Under Act 1 of 2011, for taxable years commencing after December 31, 2010, the highest corporate income tax rate is lowered to 30% for net taxable income in excess of $1,750,000 (it will be reduced to 25% for taxable years starting after December 31, 2013 subject to the satisfaction of certain conditions) and the alternative minimum tax is also reduced from a rate of 22% to the greater of (i) the amount produced by applying a minimum rate of 20% to the alternative minimum net income or, (ii) subject to certain exceptions, the amount produced by applying a 1% excise tax on the purchase from related parties of tangible personal property to be used in a Puerto Rico trade or business applicable to persons with gross sales of $50 million or more during any of three preceding taxable years. Dividends received by Puerto Rico corporations and partnerships from foreign corporations engaged in trade or business in Puerto Rico are subject to general income tax rates. A dividends received credit may be available when the corporation or partnership making the distribution is organized in Puerto Rico. Interest income on certain qualifying debt obligations issued by Puerto Rico corporations and certain qualifying foreign corporations and paid to corporations and partnerships qualifies for a special tax rate of 10%.

In general, corporations and the partners of partnerships operating under a new grant of tax exemption issued under the Economic Incentives Act are subject to a maximum income tax rate of 4% during their basic exemption period. Corporations and the partners of partnerships covered by the Tourism Development Act are subject to a maximum tax rate of 39% on their taxable income after applying the 90% exemption granted under the Tourism Development Act, which results in a maximum effective tax rate of 3.9% on their net tourism development income. Under Act 1 of 2011, the net income of corporations and partnerships covered under the Tourism Development Act is subject generally to a maximum effective tax rate of 3%.

The PR Code and Act 1 of 2011 generally impose a branch profits tax on resident foreign corporations whose gross income qualifies as income effectively connected with a Puerto Rico trade or business. The branch profits tax is 10% of an annual dividend equivalent amount, and it applies without regard to the Puerto Rico source of income rules.

Interest from Puerto Rico sources paid by Puerto Rico resident borrowers to non-resident non-affiliated corporate recipients is not subject to any income or withholding tax. Interest paid by Puerto Rico resident borrowers to certain related non-resident recipients is subject to a withholding tax of 29%. Dividends paid to non-resident corporate recipients are subject to a withholding tax of 10%. Dividends distributed by corporations operating under new grants of tax exemption issued under the Economic Incentives Act and the Green Energy Incentives Act are not subject to Puerto Rico income tax. However, royalty payments made by corporations covered under the Economic Incentives Act to non-resident recipients are subject to an income tax withholding of 2% or 12%, depending on certain elections made by the grantee, and in the case of corporations covered by the Green Energy Incentives Act, royalty payments to non-residents are subject to an income tax withholding of 12%.

Subject to certain exceptions, payments in excess of $1,500 during a calendar year made by the Commonwealth and persons engaged in a trade or business in Puerto Rico in consideration of the receipt of services rendered in Puerto Rico are subject to a 7% income tax withholding.

Act No. 7 – Special Tax Measures Implemented as part of the New Administration's Fiscal Stabilization Plan. Act 7 was enacted as part of the new administration's Fiscal Plan, and sought, among other things, to increase the tax revenues of the Puerto Rico government by imposing certain permanent and temporary tax increases.

With respect to income taxes, Act 7 included the following temporary measures that are applicable for taxable years commenced after December 31, 2008 and before January 1, 2012:

(i) taxable corporations and individuals whose adjusted gross income equal or exceeds $100,000 (for single individuals) or $150,000 (in the case of married persons filing jointly) are subject to a surtax of 5% on their total tax liability (for taxable years commencing after December 31, 2010, Act 1 of 2011 eliminates this surtax);

(ii) international banking entities that do not operate as bank units will be subject to a 5% income tax on their entire net income computed in accordance with the PR Code (international banking entities operating as bank units are subject to this 5% tax on their net income that does not constitute excess net income);

(iii) credit unions, their subsidiaries, and affiliates are subject to a 5% tax on the amount of net taxable income in excess of $250,000 (these entities were totally exempt before the enactment of Act 7), however, if the Government of Puerto Rico collects $690 million prior to January 1, 2012, the 5% tax will not be applicable for the remaining period;

(iv) the Cooperative Bank, its subsidiaries, and affiliates are subject to a 5% tax on the amount of net taxable income in excess of $250,000 (these entities were totally exempt before the enactment of Act 7);

(v) insurance cooperatives are subject to a 5% tax on the amount of net taxable income in excess of $250,000 (these entities were totally exempt before the enactment of Act 7); and

(vi) international insurers and holding companies of international insurers are subject to a 5% tax on their net income (these entities were totally exempt before the enactment of Act 7).

Notwithstanding the above, Act 1 of 2011 limited the duration of the 5% surtax on income derived by certain individuals and corporations and the special property tax to two years.

Act 7 also provided as a permanent measure a change in the method of computing the net income subject to alternative minimum tax ("AMT") in the case of individuals by including in the computation various categories of exempt income and income subject to preferential tax rates under the PR Code, such as: (a) long-term capital gains, which enjoy a preferential tax rate of 10% under the PR Code; (b) dividends that are taxable at the rate of 10% under the PR Code; (c) interest on bank deposits and individual retirement accounts subject to the special 10% and 17% preferential income tax rates, respectively; and (d) interest from notes or bonds eligible for the special 10% tax rate provided by the PR Code.

Another change introduced by Act 7, for taxable years commenced after December 31, 2008 and before January 1, 2012 was an adjustment to the calculation of the net income subject to the AMT in the case of entities taxed as corporations that denies a deduction for expenses paid or accrued for services rendered outside of Puerto Rico by a related party. Lastly, different income tax credits awarded to investors under certain special laws for activities such as revitalization of urban centers (only in part), venture capital, solid waste, housing infrastructure, and rehabilitation of social-interest housing (only projects without qualification certifications as of March 9, 2009), among others, may not be claimed or granted for taxable years commenced after December 31, 2008 and before January 1, 2012. Tax credits associated to manufacturing, tourism, and cinematographic projects, however, were not affected by Act 7.

Tax Reform

The tax reform consists of two phases focused on providing tax relief to individual and corporations, promoting economic development and job creation, simplifying the tax system and reducing tax evasion. The tax reform is projected to provide taxpayers aggregate annual savings of $1.2 billion for each of the next six fiscal years, commencing on taxable year 2011.

The first phase, enacted as Act No. 171 of November 15, 2010, applies to the 2010 tax return and provides a tax credit to each individual and corporate taxpayer. The tax credit applicable to individuals and determined by reference to the tax liability ranges from 7% for those taxpayers in higher brackets to 15% for taxpayers in the lowest bracket. Corporate taxpayers will also be entitled to a 7% tax credit determined by reference to the tax liability; provided, that such taxpayer paid the statutorily required Christmas bonus for 2010. Also, the corporate net operating loss carry forward is extended from 7 years to 10 years. This first phase is expected to provide individual and corporate taxpayers with aggregate savings of $309 million for taxable year 2010.

The second phase, enacted as Act 1 of 2011, (i) promotes employment by doubling the earning income credit and increasing the maximum applicable income to qualify for such credit; (ii) provides a $400 tax credit to individuals over 65 years of age with an income below $15,000; (iii) significantly reduces individual income tax rates and only allow the following five deductions (a) mortgage interest up to 30% of adjusted gross income, (b) charitable contributions up to 50% of adjusted gross income, (c) medical expenses in excess of 6% of adjusted gross income, (d) interest on student loans, and (e) contributions to retirement plans and accounts, including individual retirement accounts, health savings accounts and education savings accounts; and (iv) significantly reduces corporate income tax rates.

The reduction in income tax revenues resulting from the implementation of the tax reform is expected to be offset by the additional revenues produced by (i) an expanded income tax source rule and a new excise tax imposed on entities that purchase products manufactured in Puerto Rico by their affiliates under the provisions of Act 154, discussed below, (ii) enhanced enforcement efforts, including the statutorily required reporting of certain client information by financial institutions to the Treasury Department, and (iii) increased economic activity produced by the tax relief measures. The combined effect of the tax reform measures and the revenue and enforcement measures is expected to be revenue positive. Act 1 of 2011 conditions the implementation of the tax reductions applicable to individuals and corporations after fiscal year 2014 on the Commonwealth's ability to continue its path towards fiscal stability. Specifically, the tax relief provisions for individuals and corporations for taxable years 2014 through 2016 will only be implemented if (i) OMB certifies that the expense control target has been met, (ii) the Treasury Department certifies that General Fund revenue target has been met and (iii) the Planning Board certifies a year-over-year target increase in gross domestic product. There is no assurance that sufficient revenues will be collected to partially offset the reduction in income tax revenues expected from the implementation of the tax reform.

Act 154 – Expanded Income Taxation and New Excise Tax. Act 154, approved on October 25, 2010, as amended, seeks, among other things, to balance the tax burden among the taxpayers and increase the tax revenues of the Government. Act 154 modified the income taxation of certain nonresident alien individuals, foreign corporations and foreign partnerships (each a taxpayer) by expanding the circumstances in which such persons would be subject to Puerto Rico income taxation, and the act imposed an excise tax on the acquisition of certain personal property manufactured or produced in whole or in part in Puerto Rico and on the acquisition of certain manufacturing services carried out in Puerto Rico. Act 154 applies to income realized and acquisitions occurring after December 31, 2010.

The Act provides that, in certain circumstances, taxpayers will be deemed to be engaged in trade or business in Puerto Rico and taxable in Puerto Rico with respect to a portion of taxpayer's income where the taxpayers engage in significant transactions with other persons that are members of the same controlled group. Where a person engages in significant transactions with a member of the same controlled group that has gross receipts of seventy-five million dollars or more in any of the last three years and that manufactures or produces goods in Puerto Rico, or provides services in connection with the manufacture or production of goods in Puerto Rico, the person will not be subject to income tax, will instead be subject to the excise tax in lieu of any income tax. The excise tax will apply for a period of six years. The excise tax is based on the value of the personal property or services acquired and will be 4% for calendar year 2011, declining to 3.75% in 2012, 2.75% in 2013, 2.5% in 2014, 2.25% in 2015 and 1% in 2016. On December 29, 2010, the Treasury Department adopted regulations that provide certain tax credits against the temporary excise tax that lessen its impact on affected taxpayers subject to the temporary excise tax. These regulations became effective on January 1, 2011. The regulations address implementation and interpretation issues and include provisions regarding certain applicable credits against the tax subject to maintaining a baseline employment and other conditions. The Government estimates that this excise tax will affect foreign corporations or partnerships that are principally engaged in the manufacturing of pharmaceuticals and electronics. The Government expects to raise approximately $1.4 billion from the excise tax during the first year of implementation of Act 154 and $5.6 billion for the six year period that the excise tax is in place.

While the Government expects that certain taxpayers subject to the excise tax will be able to credit all or a portion of the excise tax paid against their U.S. federal income tax liabilities, it is uncertain how this new tax will affect each individual taxpayer. The long-term effects of the excise tax on the manufacturing sector of the Puerto Rico economy are also uncertain.

The first monthly excise tax payment was due in February 2011. The collections for the first nine monthly excise tax payments (from February through October 2011) were $1.325 billion. These amounts are consistent with the Government's projection of annual collections from the excise tax.

Based on its analysis, the Government believes that the revenue projections from the taxes imposed by Act 154 are reasonable. However, since such taxes only became effective on January 1, 2011, there can be no assurance that the revenues therefrom, together with the other revenue enhancement measures included in the tax reform, will be sufficient to fully offset the reduction in income tax revenues expected from other aspects of the tax reform.

In connection with the expansion of the taxation of foreign persons by Act 154, the Government obtained a legal opinion regarding the creditability of the excise tax for U.S. federal income tax purposes. The opinion concludes that this excise tax should be creditable against U.S. federal income tax. That conclusion was based in part upon a determination that the expansion of the taxation of foreign persons and the imposition of the excise tax more likely than not satisfy the constitutional requirements of due process and the Commerce Clause of the United States Constitution, for reasons discussed therein.

On March 30, 2011, the IRS issued Notice 2011-29 addressing the creditability of the new excise tax imposed by Act 154. Notice 2011-29 provides that the provisions of the new Puerto Rico excise tax are novel and the determination of its creditability requires the resolution of a number of legal and factual issues. Pending the resolution of those issues, the IRS will not challenge a taxpayer's position that the excise tax is a tax in lieu of an income tax under Section 903. The IRS also provided that any change in the foregoing tax credit treatment of the excise tax after resolution of the pending issues will be prospective and will apply to excise tax paid or accrued after the date that further guidance is issued.

Act 154 has not been challenged in court; consequently, no court has passed on the constitutionality of Act 154. There can be no assurance that its constitutionality will not be challenged and that, if challenged, the courts will uphold Act 154. To the extent a court determines that the imposition of the excise tax or the expansion of the income tax or both are unconstitutional, the Government's revenues may be materially adversely affected.

Sales and Use Taxes

Act No. 117 of July 4, 2006 ("Act 117") amended the PR Code to provide, among other things, for a general sales and use tax of 5.5% to be imposed by the central government (the "Commonwealth Sales Tax"). Act 117 also authorized each municipal government to impose a municipal sales and use tax of 1.5% (the "Municipal Sales Tax" and, together with the Commonwealth Sales Tax, the "Sales Tax"). In general, the Municipal Sales Tax has the same tax base, exemptions (except for unprocessed foods) and limitations as those provided for the Commonwealth Sales Tax. Act 117 also provides certain income tax reductions to address the regressive effect of the Sales Tax on taxpayers in lower income tax brackets.

The Sales Tax is imposed on the sale, use, consumption and storage of taxable items, which include tangible personal property, taxable services, admission rights and certain other types of transactions covering separable and identifiable taxable items which are sold for a single price, subject to certain exceptions and limitations. The Sales Tax does not apply to, among other things: (i) motor vehicles, (ii) non-prepared food, (iii) healthcare services and prescription medicines, (iv) certain bakery goods, (v) crude oil and its derivatives, including gasoline, (vi) hotel room charges, (vii) financial services, (viii) services provided by the Commonwealth, including electricity and water, and (ix) local sales of goods to be used as content in a manufactured good, whether or not bound for export.

Act 117 also repealed the 5% general excise tax imposed on imported goods and the 3.6% general excise tax imposed on goods manufactured in Puerto Rico. Other items, such as fuel, crude oil and petroleum products, and vehicles, however, remain subject to the excise tax previously applicable to such items, and are not subject to the Sales Tax.

The Sales Tax became effective on November 15, 2006 and the effective date of the repeal of the 5% general excise tax was October 16, 2006. Municipalities were authorized to implement the Municipal Sales Tax starting on July 1, 2006. The revenues derived from the Sales Tax are distributed as follows: 5.5% goes to the central government and 1.5% to Puerto Rico's municipalities. One half of the 5.5% Commonwealth Sales Tax is transferred to the Dedicated Sales Tax Fund, created by Act 91 of 2006, as amended, and the balance goes to the

General Fund. The 1.5% Municipal Sales Tax is divided as follows: (i) 1% goes to the municipalities, and (ii) 0.5% goes to the Municipal Improvements Fund. The increase in revenues generated by the Sales Tax has been partly offset by the elimination of the 5% general excise tax and the effect of the income tax reduction measures included in Act 117.

The Treasury Department has reported and recorded Commonwealth Sales Tax revenues on a "modified cash basis." This means that the figures for each month represent the sales taxes corresponding to sales made by merchants and retailers and sales tax collected by such merchants and retailers during that month, but reported and remitted to the Treasury Department during the following month.

Effective fiscal year 2010, the Treasury Department began reporting Commonwealth Sales Tax revenues on a cash basis in order to report these revenues on the same basis and at the same time as it reports all other tax revenues. Accordingly, for fiscal year 2010, Commonwealth Sales Tax revenues were reported in the month in which such revenues were received by the Treasury Department. The new reporting method became effective as of July 1, 2009. Thus, the figures for sales tax collections previously reported in June 2009 were transferred to July 2009.

The Sales Tax generated revenues for the General Fund of approximately $547.6 million for fiscal year 2011.

The Treasury Department has also sponsored legislation to limit or close certain gaps that existed in Act 117, as amended. In this regard, one of the amendments incorporated in Act 7 require a merchant or retailer to file his or her Commonwealth Sales Tax monthly return on or prior to the tenth day of the following month, rather than the twentieth day (as originally required in Act 117). Such amendment also provides that the Commonwealth Sales Tax exemption applicable to resellers applies only to merchants and retailers (i) with gross sales greater than or equal to $500,000 or (ii) that do not meet the $500,000 sales threshold but meet certain other requirements imposed by the Treasury Department. A merchant or retailer that meets neither the $500,000 threshold nor the other requirements imposed by the Treasury Department would still be entitled to a credit on sales tax paid on merchandise acquired for resale that must be claimed in each monthly filing. This measure is intended to enable responsible taxpayers to take advantage of the exemption while preventing non-compliant merchants and retailers from abusing the exemption.

Excise Taxes

The PR Code imposes an excise tax on certain articles and commodities, such as cigarettes, alcohol, sugar, cement, motor vehicles, heavy equipment, boats and certain petroleum products, which are taxed at different rates.

Under Act 7, the excise tax was increased on certain articles (cigarettes and certain alcoholic beverages) and was expanded with respect to others (motor vehicles). With respect to cigarettes, the increase was approximately 81% per taxable unit. For certain alcoholic beverages, the increase ranges between $0.30 and $0.70 per standard gallon. Motor vehicles, motorcycles, all terrain vehicles and "scooters," which used to be subject to the Sales Tax, are now subject to an excise tax of 10%.

Property Taxes

Personal property, which accounts for approximately 46% of total collections of taxable property, is self-assessed. Real property taxes are assessed based on 1958 property values. No real property reassessment has been made since 1958, and construction taking place after that year has been assessed on the basis of what the value of the property would have been in 1958. Accordingly, the overall assessed valuation of real property for taxation purposes is substantially lower than the actual market value. Also, an exemption on the first $150,000 of assessed valuation in owner-occupied residences is available.

Property taxes are assessed, determined and collected for the benefit of the municipalities by the Municipal Revenues Collection Center ("CRIM"), a government instrumentality of the Commonwealth. However, 1.03% of the property tax based on the assessed value of all property (other than exempted property) is used for purposes of paying the Commonwealth's general obligation debt and is deposited in the Commonwealth's Redemption Fund.

One of the amendments incorporated in Act 7 was that, for fiscal years 2010 through 2013, the appraisal values of real property in Puerto Rico were increased tenfold and the real personal property tax rates applicable to such values were reduced tenfold so as to offset any increased tax that would have otherwise been applicable due to the increase in appraisal values. This temporary amendment, which is expected to be revenue neutral, was intended to increase the borrowing capacity of Puerto Rico's municipalities.

Act 7 did impose, however, an additional real property tax on residential and commercial real properties with appraised values in excess of approximately $210,000. This tax will apply during fiscal years 2010, 2011 and 2012, or until $690 million is collected. The additional real property tax, to be collected by the Treasury Department, will be equal to 0.591% of such properties' appraised value as determined by CRIM. Act 1 of 2011 eliminated this additional real property tax for fiscal year 2012.

The following table presents the assessed valuations and real and personal property taxes collected for fiscal years 2007 to 2011.

Commonwealth of Puerto Rico
Assessed Valuations and Real and Personal Property Taxes
(Commonwealth and Municipalities Combined)
(in thousands)

Fiscal Years Ended June 30,	Assessed Valuations[(1)]	Taxes Levied	Collections of Current Year	Collections of Previous Years	Total Collections[(2)]
2007	26,898,519	982,400	813,700	79,720	893,420
2008	27,941,285	1,031,277	788,364	119,062	907,426
2009	28,903,996	1,032,570	634,040	244,411	878,451
2010	175,025,782	1,093,769	666,429	269,857	936,286
2011	187,293,462	1,152,718	712,706	225,280	937,986

(1) Valuation set as of July 1 of each fiscal year.
(2) During fiscal year 2004 a property tax amnesty was approved by the Legislative Assembly and implemented by CRIM. In addition to the amounts shown, under the amnesty program a total of $105.3 million was collected in fiscal year 2004 and $21.1 million in fiscal year 2005.

Source: Municipal Revenues Collection Center.

Other Taxes and Revenues

Motor vehicle license plate and registration fees comprise the major portion of license tax receipts.

Non-tax revenues consist principally of lottery proceeds, documentary stamps, permits, fees and forfeits, proceeds of land sales and receipts from public corporations in lieu of taxes.

Revenues from Non-Commonwealth Sources

Revenues from non-Commonwealth sources include customs duties collected in Puerto Rico and excise taxes on shipments of rum from Puerto Rico to the United States mainland. The customs duties and excise taxes on shipments are imposed and collected by the United States and returned to the Commonwealth. The excise tax on shipments of rum from Puerto Rico and other rum producing countries is currently $13.50 per gallon. Of this amount, the lesser of $10.50 per proof gallon and the actual excise tax imposed is currently returned ("covered over") to the Commonwealth. Since 1999, however, the U.S. Congress has enacted special supplementary legislation increasing the maximum amount covered over to the Commonwealth to $13.25 per proof gallon. For fiscal year 2011, the total excise taxes on rum shipments returned to the Commonwealth was $430 million, of which $329 million went to the General Fund.

In June 2008, the Government of the United States Virgin Islands (the "USVI") signed an agreement with Diageo USVI, Inc ("Diageo") for the construction and operation of a new rum distillery in St Croix, USVI, that will manufacture Captain Morgan branded products to be sold in the United States beginning in January 2012. Currently, all rum used in Captain Morgan products sold in the United States is procured through a supply contract with Serralles Destillery ("Serralles") in Puerto Rico which expires on December 31, 2011. The Government estimates that the exports of Captain Morgan rum produced in Puerto Rico by Serrallés during calendar year 2009 were 9,403,224 proof gallons. These rum exports of Captain Morgan resulted in an estimated $124.5 million in excise tax on rum shipments returned by the United States to Puerto Rico during fiscal year 2009. As a result of the termination of the contract between Serrallés and Diageo, it is expected that after 2011, the income received by the Commonwealth from the federal excise tax on rum shipments will decrease unless Serrallés is able to find other clients in the United States for the volume of bulk rum previously purchased by Diageo for its Captain Morgan products.

In an effort to maintain the local rum industry, as a result of the threat posed by the USVI's agreement with Diageo, and preserve or increase the amount of federal excise taxes on rum shipments returned to the Commonwealth under the cover-over program, the Governor signed Act No. 178 of December 1, 2010 ("Act 178"), which increases from 10% to 25% the portion of the monies from the federal excise tax that the Commonwealth may invest to provide incentives to and promote the Puerto Rican rum industry. The law also authorizes the Governor to increase this percentage up to 46% after December 31, 2011, through an Executive Order. In order to promote the Puerto Rican rum industry in general, the amount received from such refund will be transferred to a special account of the General Fund, which may be used for marketing, production and infrastructure investment incentives. Effective January 1, 2011, Act 1 of 2011 replaced Act No. 178 and contains identical provisions.

As permitted under Act 1 of 2011, the Government has entered into a definitive agreement with two rum producers and is currently in negotiations with other producers to provide them a series of subsidies and incentives by allowing such companies to benefit from the cover-over program rebate. These agreements are expected to promote and encourage the export of rum produced in Puerto Rico. As a result of these agreements, during fiscal year 2012 the Treasury Department expects to disburse approximately $72 million of total revenues from the federal excise tax on rum shipments for these subsidies and incentives. This amount is expected to be partially offset by the economic activity generated by the increased investment in Puerto Rico by these rum producers.

Administrative Measures to Increase Collections of Income, Sales, and Excise Taxes and Property Taxes

The Treasury Department has elaborated a strategic plan designed to improve tax collections. The plan includes initiatives to foster tax compliance, implement effective enforcement measures, and attack tax evasion. To promote taxpayers' compliance, the Treasury Department has liberalized the procedures to enter into payment plans, offers-in-compromise agreements, and encouraged voluntary disclosures agreements.

In addition, the Treasury Department has developed initiatives focused on effective enforcement methods, such as improving the efficiency of its audit selection process, the creation of technological solutions to improve collections, and the establishment of cooperation agreements with federal and local governmental agencies. The Treasury Department is also integrating its databases and establishing a tax intelligence project to identify tax evasion and improve its audit selection process.

Specifically, the Treasury Department has developed various initiatives directed towards increasing collections of income taxes and the Commonwealth sales tax through the implementation of various enforcement and compliance programs. Among these revenue raising initiatives is a voluntary disclosure program that provides taxpayers that meet certain criteria the opportunity to pay taxes and interests owed on unreported income and, in certain circumstances, avoid the payment of surcharges and penalties. Under this program, which began on July 1, 2009, the Treasury Department has reviewed 568 cases and collected approximately $64.2 million. In May 2010, the Treasury Department also began to deliver letters to taxpayers identified by the tax intelligence program to encourage the use of the voluntary disclosure program. As of October 15, 2010, the Treasury Department had sent approximately 7,900 letters and had received responses from 2,000 taxpayers. Moreover, the Treasury Department sent 1,000 additional letters in March 2011 and 2,200 additional letters in April 2011 as a second notice to taxpayers that did not respond to the first letter of May 2010.

Other programs are geared towards the use of technology to detect noncompliance. For example, the Treasury Department completed in November 2010 the integration of its general computer systems with the sales tax database in order to better detect non-compliance. The Treasury Department has also implemented a program whereby its officers use hand held scanning devices to cross-check merchant licenses. Recently, the Treasury Department discontinued the use of the hand held scanning devices and will provide tablet computers to its agents, beginning in December 2011, that will allow them to review a broader range of compliance criteria, such as merchant licenses, Commonwealth Sales Tax sales and point of sale system compliance.

On September 28, 2010, the Treasury Department signed an agreement for the implementation of a new point of sale system that is intended to strengthen its sales tax enforcement efforts. The system is designed to: (i) transmit daily to the Treasury Department information on all sales tax transactions; (ii) reconcile transmitted transactional information with information reported by merchants; (iii) provide wireless transmission devices for use by street vendors; and (iv) capture a greater percentage of cash sales through the implementation of a special lottery using sales receipts as lottery tickets (the "IVU Loto"). The Treasury Department began a two phase implementation of this new point of sale system in December 1, 2010, through a pilot program in which 200 merchants in the Municipality of Ponce were selected to participate. The second phase, which includes the initial implementation of the point of sale system throughout the island, started in March 2011. Implementation of the new system is expected to be completed by the end of Fiscal Year 2011-2012 and is expected to increase sales tax collections by $200 million during the first year. As of November 7, 2011, the point of sale devices captured approximately 187.4 million transactions which resulted in sales of $4.4 billion and Commonwealth Sales Tax collections of $155.6 million. The Treasury Department adopted regulations on December 14, 2010 requiring that all qualifying merchants register for participation in the point of sale system program on or prior to April 30, 2011. As of October 27, 2011, 191,037 locations had registered in the program and 59,884 of such locations will be required to acquire and use the new point of sale system.

The Treasury Department has begun to detect inconsistencies between the information captured by the point of sale system and that reported by merchants and retailers. The principal inconsistencies are: (i) merchants and retailers that report sales through the point of sale system but do not file monthly returns, (ii) sales reported through the point of sale system are higher than those reported in the monthly returns, (iii) cash credits claimed through the point of sale system are equal to the sales reported, and (iv) merchants and retailers are not reporting cash sales. In order to address these possible instances of non-compliance, the Treasury Department has created a task force consisting of fiscal auditors and agents from the Sales and Use Tax Bureau and the Tax Evasion Bureau. The fiscal auditors are responsible for investigating inconsistencies reported by the point of sale system, determine tax deficiencies and issue preliminary deficiency notices. The agents of the Sales and Use Tax Bureau provide assistance to the fiscal auditors in connection with any additional information requirements and visit merchants and retailers to investigate the status of their permits and point of sale systems. Finally, the agents from the Tax Evasion Bureau are responsible for investigating any tax crimes discovered by the fiscal auditors and/or agents from the Sales and Use Tax Bureau. As a result of this initiative, as of October 5, 2011, the Treasury Department had identified approximately 33,481 unfiled monthly returns and sent notices to approximately 5,125 merchants and retailers. As of October 31, 2011, approximately 1,181 merchants and retailers had responded to the notices and approximately 2,577 unfiled monthly returns were filed resulting in taxable sales reported of approximately $24.7 million and sales and use tax collections of $1.4 million. Merchants and retailers that filed monthly returns reporting no sales will receive a deficiency notice and all other merchants and retailers that have not responded will be referred to a fiscal auditor or the Tax Evasion Bureau.

In addition, the Treasury Department established “IVU Alerta” in order to enhance Commonwealth Sales Tax compliance. The “IVU Alerta” is an internet and telephone hotline through which customers and merchants can report violations related to the Commonwealth Sales Tax. This initiative started in November 29, 2010 and, as of November 4, 2011, has received 5,610 complaints, which 4,229 have been investigated resulting in fines of approximately $5.5 million.

Other initiatives include the establishment of tax liens pursuant to the procedures of Act No. 12 of January 20, 2010, which enables the creation of tax liens through an expedited process. As of October 2011, the Treasury Department has established 16,000 liens in favor of the Commonwealth over approximately $742.5 million in assets. The Treasury Department is also enforcing a provision of Act 7 that allows the Treasury Department to revoke a certificate of exemption held by a merchant or retailer that fails to pay sales taxes collected in full by the 10th day of the month. Also, the Treasury Department will begin to seize the assets of businesses that are delinquent on their sales tax payments. In addition, the Treasury Department has entered into agreements with various municipalities to conduct simultaneous field visits and joint audits in order to increase the effectiveness of sales tax enforcement efforts as the ones described above.

Act No. 172 of November 15, 2010, established that taxpayers which apply for a voluntary disclosure program on or before April 15, 2011 will be eligible for a 20% flat income tax rate on the gross amounts reported and will not be subject to interest, surcharges and penalty fees. This legislation extends the benefits of the program to municipal license tax declarations for which taxpayers will pay principal on the municipal tax determined, but will not be subject to interest, surcharges and penalty fees. Declarations by taxpayers must relate to tax years commenced after July 1, 2003 and ending on or before December 31, 2009, and payment of tax determined under the program must be paid no later than June 30, 2011. Recently, the Governor signed Act No. 64 of April 19, 2011, which extended the disclosure period until June 30, 2011.

The Treasury Department has also implemented a temporary measure to collect on payroll and employer withholding debts. This measure allows employers to enter into payment plans with the Treasury Department, subject to employer making a down payment of 25%, in the case of payroll debts, and 40%, in the case of employer withholding debts, of the total outstanding debt. The payment plans do not provide for the abatement of interest, surcharges and penalties and the same must be initiated on or before June 30, 2011. As of June 31, 2011, 216 employers entered into payment plan agreements in the amount of $5.5 million and made down payments in the amount of $1.7 million.

Transfers to General Obligation Redemption Fund

These consist of transfers from the General Fund to the Redemption Fund for the amortization of the principal of and interest on general obligation bonds and notes of the Commonwealth.

Components of General Fund Expenditures

Grants and Subsidies

This category includes grants and contributions to municipalities, public corporations with independent treasuries, and charitable institutions. It also includes items for or included in court awards, damage awards for personal injury or property damage, and payment of taxes and payments in lieu of taxes.

Personal Services

This category includes compensation paid for personal services rendered to the Commonwealth and its public instrumentalities by individuals or firms in the form of salaries, wages, per diems, fees, commissions, or other forms of compensation.

Other Services

This category includes compensation for services other than the services referred to above, including advertising, printing, communications, legal expenses, utilities, building and equipment rental and maintenance expenses, insurance premiums and miscellaneous services.

Materials and Supplies

This category includes all articles that ordinarily have a short life and durability, lose their characteristic identity in the process of use, have only nominal value ($25 or less), or are not otherwise chargeable as equipment.

Equipment Purchases

This category includes items that have three special characteristics distinguishing them from materials: durability, long useful life, and high unit cost. In addition, these items are subject to centralized inventory control as fixed assets.

Capital Outlays and Other Debt Service

Capital outlays are made primarily for land acquisition or interests in land, construction of buildings, roads, bridges and other structures, and permanent improvements and additions. Other debt service includes payments on notes held by GDB to be paid from the General Fund and payments for the amortization of the principal of and interest on non-general obligation debt payable from Commonwealth appropriations.

Transfers to Agencies

These transfers include the repayment of loans and advances to other funds, certain refunds, advances from other funds and other receipts, repayment of advances from other funds, grants and contributions to other funds under the custody of the Secretary of the Treasury and other items. The major portion of grants and contributions in recent fiscal years has consisted of transfers to cover the costs of health reform and advances to the municipalities.

Other Expenditures

This category represents recurring General Fund expenditures not appropriately attributable to other expenditure line items, such as advances to government agencies and municipalities, which advances are by law reviewed to be reimbursed to the General Fund.

Federal Grants

Puerto Rico receives grants under numerous federal programs. Federal grants to the agencies and instrumentalities of the Commonwealth government are estimated to be $4.784 billion for fiscal year 2012, a decrease of $111 million, or 2%, from fiscal year 2011. This decrease in federal grants is due to the termination of the ARRA program. The following table presents revenues from federal grants by broad program areas, which are accounted in the central accounting system of the Treasury Department. The figures for fiscal years 2008 through 2011 are actual figures. The figures for fiscal year 2012 are the amounts included in the adopted budget.

Puerto Rico expects to receive a total of approximately $7.022 billion in stimulus funds from ARRA, of which $508 million, $2.68 billion and $2.18 billion were disbursed by the government during fiscal years 2009, 2010 and 2011, respectively. The amount of $1.36 million is expected to be disbursed by the government during fiscal year 2012. As of October 14, 2011, the Commonwealth had disbursed $5.533 billion in ARRA funds, or 78.8%, of awarded funds. The table below only included the portion of these funds disbursed by agencies whose accounting systems are centralized in the Treasury Department.

The Commonwealth of Puerto Rico
Federal Grants*
(in thousands)

	2008	2009	2010	2011[(1)]	2012[(2)]
Education	$992,087	$1,813,455	$1,377,389	$1,254,959	$1,128,176
Social Services	2,054,897	2,453,605	2,484,920	2,440,457	2,437,661
Health	465,466	583,190	655,060	482,524	502,744
Labor and Human Resources[(3)]	140,186	277,127	138,425	109,391	109,391
Crime	20,319	64,155	29,459	29,900	24,819
Housing[(4)]	363,589	416,667	534,987	425,940	424,413
Drug and Justice	19,394	53,067	23,175	21,730	24,813
Agriculture and Natural Resources	11,054	114,920	26,886	14,466	14,661
Contributions to Municipalities	49,543	47,656	60,559	52,087	52,087
Other	15,782	67,017	72,875	63,574	65,506
TOTAL	$4,132,317	$5,890,859	$5,403,735	$4,895,028	$4,784,271

* Does not include grants received by agencies whose accounting systems are not centralized at the Treasury Department.
(1) Preliminary, unaudited.
(2) Adopted budget.
(3) Amounts include grants to the Right to Work Administration and the Occupational Development and Human Resources Council.
(4) Amounts include grants to the Public Housing Administration.

Source: Office of Management and Budget

BUDGET OF THE COMMONWEALTH OF PUERTO RICO

Office of Management and Budget

OMB's predominant mission is to assist the Governor in overseeing the preparation of the budget of the Commonwealth and supervise its administration in the agencies of the Executive Branch. In helping to formulate the Governor's budget, OMB evaluates the effectiveness of agency programs, policies, and procedures, assesses competing funding demands among agencies, and sets funding priorities.

In addition, OMB oversees and coordinates the administration's initiatives in financial management, information technology, general management and organizational structure, and supervises the agencies' compliance with the Governor's program and regulatory policies. In each of these areas, OMB's role is to help improve administrative management, develop better performance measures and coordinating mechanisms, and promote efficiency in the use of public funds.

Budgetary Process

The fiscal year of the Commonwealth begins each July 1. The Governor is constitutionally required to submit to the Legislative Assembly an annual balanced budget of revenues, capital improvements, and operating expenses of the central government for the ensuing fiscal year. The annual budget is prepared by OMB, in coordination with the Planning Board, the Treasury Department, and other government offices and agencies. Section 7 of Article VI of the Constitution provides that "The appropriations made for any fiscal year shall not exceed the total revenues, including available surplus, estimated for said fiscal year unless the imposition of taxes sufficient to cover said appropriations is provided by law."

The annual budget, which is developed utilizing elements of program budgeting, includes an estimate of revenues and other resources for the ensuing fiscal year under (i) laws existing at the time the budget is submitted, and (ii) legislative measures proposed by the Governor and submitted with the proposed budget, as well as the Governor's recommendations as to appropriations that in his judgment are necessary, convenient, and in conformity with the four-year investment plan prepared by the Planning Board.

The Legislative Assembly may amend the budget submitted by the Governor but may not increase any items so as to cause a deficit without imposing taxes to cover such deficit. Upon passage by the Legislative Assembly, the budget is referred to the Governor, who may decrease or eliminate any item but may not increase or insert any new item in the budget. The Governor may also veto the budget in its entirety and return it to the Legislative Assembly with the Governor's objections. The Legislative Assembly, by a two-thirds majority in each house, may override the Governor's veto. If a budget is not adopted prior to the commencement of a fiscal year, the budget for such fiscal year shall be the annual budget for the preceding fiscal year as originally approved by the Legislative Assembly and the Governor until a new budget is approved. This permits the Commonwealth to continue making payments of its operating and other expenses until a new budget is approved.

Financial Control and Adjustment Procedures

Revenue estimates for budgetary purposes are prepared by the Treasury Department, except for estimates of federal grants, which are prepared by OMB based on information received from the various departments and other recipients of such grants. Revenue and federal grant estimates are under continuous review and, if necessary, are revised at least quarterly during the fiscal year. Fiscal control over expenditures is exercised by the Governor, through the Director of OMB, and the Secretary of the Treasury.

During any fiscal year in which the resources available to the Commonwealth are insufficient to cover the appropriations approved for such year, the Governor may take administrative measures to reduce expenses and submit to both houses of the Legislative Assembly a detailed report of any adjustment necessary to balance the budget, or make recommendations to the Legislative Assembly for new taxes or authorize borrowings under provisions of existing legislation or take any other necessary action to meet the estimated deficiency. Any such proposed adjustments shall give effect to the "priority norms" established by law for the disbursement of public funds in the following order of priority; first, the payment of the interest on and amortization requirements for public debt (Commonwealth general obligations and guaranteed debt for which the Commonwealth's guarantee has been exercised); second, the fulfillment of obligations arising out of legally binding contracts, court decisions on eminent domain, and other unavoidable obligations to protect the name, credit and good faith of the Commonwealth; third, current expenditures in the areas of health, protection of persons and property, education, welfare, and retirement systems; and fourth, all other purposes.

A Budgetary Fund was created by Act No. 147 of June 18, 1980, as amended (the "Budgetary Fund"), to cover the appropriations approved in any fiscal year in which the revenues available for such fiscal year are insufficient, to secure the payment of public debt, and to provide for unforeseen circumstances in the provision of public service. An amount equal to one percent of the General Fund net revenues of the preceding fiscal year is required to be deposited annually into the Fund. In addition, other income (not classified as revenues) that is not assigned by law to a specific purpose is also required to be deposited in the Budgetary Fund. The maximum balance of the Budgetary Fund may not exceed 6% of the total appropriations included in the budget for the preceding fiscal year. During the last fiscal years, the Legislative Assembly approved joint resolutions to halt temporarily the deposit of funds into the Budgetary Fund, and such funds were used instead to cover the budgetary deficits. As of June 30, 2011, the balance in the Budgetary Fund was $844,925.

An Emergency Fund was created by Act No. 91 of June 21, 1966 ("Act 91 of 1966"), as amended (the "Emergency Fund"), to cover unexpected public needs caused by calamities, such as wars, hurricanes, earthquakes, droughts, floods and plagues, and to protect people's lives and property and the public sector credit. The Emergency Fund is capitalized annually with an amount totaling no less than one percent of the General Fund net revenues of the preceding fiscal year. Act No. 91 was amended in 2003 to set an upper limit to the Emergency Fund of $150 million at the beginning of the fiscal year. Act No. 91 was further amended in 2005 to authorize the disbursement of funds from the Emergency Fund to cover certain General Fund expenditures and operational costs of the State Emergency Management Agency and authorized GDB to lend to the Commonwealth up to $150 million to replenish the Emergency Fund to provide funding for emergency and disaster needs. As of June 30, 2011, the balance in the Emergency Fund was $1.4 million and $0.5 million was available to be borrowed from GDB. Joint Resolution No. 60 of July 1, 2011 authorized the conversion of this loan into a revolving line of credit with the same authorized limit of $150 million.

Appropriations

Appropriations in the central government budget of Puerto Rico consist of the following:

(i) *General Fund appropriations for recurring ordinary operating expenses of the central government and of the Legislative Assembly.* These are made by a single annual law known as the Joint Resolution of the General Budget.

(ii) *General Fund appropriations for special operating expenses, for contributions to municipalities, the University of Puerto Rico and the Judicial Branch, and for capital expenditures*. These are authorized by separate law.

(iii) *Disbursements of Special Funds for operating purposes and for capital improvements.* For the most part, these do not require annual legislative authorization, because they are authorized by previous legislation or by the United States Congress. Federal grants constitute the major part of the resources of the Special Funds.

(iv) *Bond Fund appropriations for capital expenditures financed by bonds*. Expenditures of these funds occur in one or more years.

In Puerto Rico, the central government performs many functions, which in the fifty states are the responsibility of local governments, such as providing public education, police and fire protection. The central government also provides significant annual grants to the University of Puerto Rico and to the municipalities. In addition, the Commonwealth appropriates annually to the Judicial Branch an amount equal to 4% of the average annual revenue from internal sources for each of the two preceding fiscal years. This percentage may be increased upon review, with scheduled reviews every five years.

For fiscal year 2011, approximately 25% of the General Fund was committed to the payment of fixed charges such as municipal subsidies, grants to the University of Puerto Rico, mandated funding for the Judicial Branch, rent payments to PBA, and debt service on the direct debt of the Commonwealth. This proportion was expected to remain stable in fiscal year 2012.

For fiscal year 2009, over 64% of the controllable funds portion of the General Fund was committed for the payment of the central government payroll (not including the University of Puerto Rico and the Judicial Branch). In fiscal year 2011 and 2012, the Commonwealth decreased this proportion to an average of 56% due mainly to the savings in operational expenses from the implementation of the Fiscal Plan. The following table shows a breakdown between controllable and non-controllable General Fund expenses for fiscal years 2009 through 2012.

Expenses Breakdown for the General and Stabilization Funds
(in millions)

	2009	2010	2011[(1)]	2012[(2)]
Non-Controllable Expenses				
Mandated Expenses (Formula)				
Contributions to Municipalities	368	335	355	380
University of Puerto Rico	835	729	691	704
Judicial Branch	348	348	348	328
Rent Payments to Public Buildings Authority	206	299	217	215
General Obligation Debt Service	288	289	201	179
Other Debt Service	105	373	517	492
Total of Non-Controllable Expenses	2,150	2,000	2,329	2,298
Percent of Total General Fund Expenses	23%	20%	25%	25%
Controllable Expenses				
Payroll and Related Costs[(3)]	7,334	8,170	6,821	6,962
Payroll as a Percentage of Controllable Expenses	4,695	3,785	3,789	3,863
	64%	46%	56%	55%
Total General Fund Expenses	9,484	10,170	9,150	9,260
Other Expenses				
Total Non-Budgeted Expenses	1,406 [(4)]	0	0	0
Total Expenses	10,890	10,170	9,150	9,260

(1) Preliminary.
(2) Estimated.
(3) Excludes University of Puerto Rico and Judicial Branch.
(4) Represents non-budgeted operating expenses that have been identified and that were paid for with proceeds of COFINA bond issues.

Source: *Office of Management and Budget*

Budget for Fiscal Year 2011

The following table presents a summary of the Commonwealth's central government budget for the fiscal year ending June 30, 2011.

Commonwealth of Puerto Rico
Summary of Central Government Annual Budget
Fiscal Year Ending June 30, 2011
(in thousands)*

	General and Stabilization Fund	Bond Fund	Special Funds	Total
Revenues from internal sources:				
Property taxes	$238,000	-	$115,743	$353,743
Personal income taxes	2,348,000	-	-	2,348,000
Retained non-resident income tax	951,500	-	-	951,500
Corporate income taxes	1,566,000	-	-	1,566,000
Partnership income taxes	3,000	-	-	3,000
Tollgate taxes	9,000	-	-	9,000
17% withholding tax on interest	8,000	-	-	8,000
10% withholding tax on dividends	27,000	-	-	27,000
Inheritance and gift taxes	5,000	-	-	5,000
Sales and use taxes	555,000	-	-	555,000
Excise taxes:				
Alcoholic beverages	289,000	-	-	289,000
Foreign (Act 154)	609,000	-	-	609,000
Motor vehicles and accessories	369,000	-	-	369,000
Cigarettes	210,000	-		210,000
Other (excise taxes)	79,000	-	637,625	716,625
Licenses	77,000	-		77,000
Miscellaneous non-tax revenues:				
Contributions from lottery fund	43,000	-	-	43,000
Electronic lottery	79,000	-	-	79,000
Registration and document certification fees	152,000	-	-	152,000
Other	175,000	-	340,978	515,978
Total revenues from internal sources	7,792,500		1,094,346	8,886,846
Revenues from non-Commonwealth sources:				
Federal excise taxes on off-shore shipments	337,000		-	337,000
Federal grants(1)	0	-	4,895,028	4,895,028
Customs	4,000	-	-	4,000
Total revenues from non-Commonwealth sources	341,000	-	4,895,028	5,236,028
Total revenues	8,133,500	-	5,989,374	14,122,874
Other:				
Balance from previous year	0	-	1,805,803	1,805,803
COFINA Stabilization Fund	1,016,000	-	0	1,016,000
Bonds authorized	-	-	-	0
Total other sources	1,016,000	-	1,805,803	2,821,803
Total resources	9,149,500	-	7,795,177	16,944,671
Appropriations:				
Current expenses:				
General government	883,215	-	55,125	938,340
Education	2,945,862	-	1,847,992	4,793,854
Health	1,576,377	-	611,249	2,187,626
Welfare	466,677	-	2,781,594	3,248,271
Economic development	253,021	-	103,305	356,326
Public safety and protection	1,443,594	-	125,785	1,569,379
Transportation and communication	140,374	-	34,701	175,075
Housing	20,526	-	402,118	422,644
Contributions to municipalities	367,132	-	6,766	373,898
Special pension contributions	334,553	-	0	334,553
Debt service	200,813	-	115,743	316,556
Other debt service (appropriations)	517,156	-	659,435	1,176,591
Total appropriations – current expenses	9,149,300	-	6,743,813	15,893,113
Capital improvements	200	-	192,686	192,886
Total appropriations	9,149,500	-	6,936,499	16,085,999
Year-end balance	0	-	858,678	858,678
Total appropriations and year-end balance	9,149,500	-	7,795,177	16,944,677

* Totals may not add due to rounding.
(1) Does not include grants received by agencies whose accounting systems are not centralized in the Treasury Department.
Sources: Treasury Department and Office of Management and Budget

The budget for fiscal year 2011 provided for total resources of $16.9 billion and total General Fund revenues of $9.150 billion, compared to General Fund revenues of $10.191 billion for fiscal year 2010. The budgeted General Fund revenues of $9.150 billion included base revenues of $7.525 billion, $609 million from tax enforcement and compliance measures and $1.016 billion in additional revenues from COFINA Stabilization Fund.

The principal changes in budgeted General Fund revenues compared to the fiscal year 2010 budget were accounted mainly by projected increases in new temporary excise tax under Act 154 (up $609.0 million), retained non-resident income taxes (up $121.2 million), excise taxes on motor vehicles and accessories (up $24.6 million), cigarettes taxes (up $27.5 million), sales and use taxes (up $16.1 million) and property taxes (up $10.5 million) and projected decreases in federal excise taxes on offshore shipments (down $15.3 million), corporate income tax (down $111.7 million) and personal income taxes (down $226.8 million).

The fiscal year 2011 budget provided for total expenditures of $9.150 billion, consisting of General Fund expenditures of $8.134 billion and additional expenditures of $1.016 billion that were covered from proceeds of COFINA deposited in the Stabilization Fund. The budgeted total expenditures for fiscal year 2011 were $9.150 billion, or 10%, lower than budgeted total expenditures of $10.170 billion for fiscal year 2010, and $1.740 billion, or 16%, lower than total expenditures of $10.890 billion for fiscal year 2009.

Budgeted expenses and capital improvements for the central government of all budgetary funds totaled $16.1 billion, a decrease of $1,043.8 million from fiscal year 2010 budgeted appropriations. The principal changes in General Fund expenditures by program areas in fiscal year 2011 compared to the fiscal year 2010 budget were mainly due to increases in other debt service appropriations (up $144.0 million), economic development (up $59.9 million), and special pension contributions (up $20.9 million) and decreases in general government (down $834.1 million), welfare (down $5.2 million), public safety and protection (down $37.9 million), general obligation bonds debt service (down $88.9 million), health (down $102.4 million) and education (down $120.8 million).

Budget for Fiscal Year 2012

The following table presents a summary of the Commonwealth's central government budget for the fiscal year ending June 30, 2012.

Commonwealth of Puerto Rico
Summary of Central Government Annual Budget
Fiscal Year Ending June 30, 2012
(in thousands)*

	General and Stabilization Fund	Bond Fund	Special Funds	Total
Revenues from internal sources:				
Property taxes	$ 76,000	-	$ 116,321	$ 192,321
Personal income taxes	2,109,000	-	-	2,109,000
Retained non-resident income tax	980,000	-	-	980,000
Corporate income taxes	1,515,000	-	-	1,515,000
Partnership income taxes	2,000	-	-	2,000
Tollgate taxes	5,000	-	-	5,000
17% withholding tax on interest	8,000	-	-	8,000
10% withholding tax on dividends	28,000	-	-	28,000
Inheritance and gift taxes	5,000	-	-	5,000
Sales and use taxes	680,000	-	-	680,000
Excise taxes:		-	-	
Alcoholic beverages	298,000	-	-	298,000
Foreign (Act 154)	1,578,000	-	-	1,578,000
Motor vehicles and accessories	361,000	-	-	361,000
Cigarettes	210,000	-	-	210,000
Other (excise taxes)	78,000	-	724,573	802,573
Licenses	79,000	-	-	79,000
Miscellaneous non-tax revenues:		-	-	
Contributions from lottery fund	45,000	-	-	45,000
Electronic lottery	83,000	-	-	83,000
Registration and document certification fees	154,000	-	-	154,000
Other	85,000	-	423,978	508,978
Total revenues from internal sources	8,379,000	-	1,264,872	9,643,872
Revenues from non-Commonwealth sources:				
Federal excise taxes on off-shore shipments	271,000	-	-	271,000
Federal grants(1)	0	-	4,784,271	4,784,271
Customs	0	-	-	0
Total revenues from non-Commonwealth sources	271,000	-	4,784,271	5,055,271
Total revenues	8,650,000	-	6,049,143	14,699,143
Other:				
Balance from previous year	0	-	858,678	858,678
COFINA Stabilization Fund	610,000	-	-	610,000
Bonds authorized	0	-	-	0
Total other sources	610,000	-	858,678	1,468,678
Total resources	9,260,000	-	6,907,821	16,167,821
Appropriations:				
Current expenses:				
General government	831,984	-	61,252	893,236
Education	3,077,281	-	1,728,895	4,806,176
Health	1,367,187	-	541,763	1,908,950
Welfare	444,645	-	2,685,719	3,130,364
Economic development	359,373	-	110,088	469,461
Public safety and protection	1,523,677	-	104,387	1,628,064
Transportation and communication	150,561	-	38,107	188,668
Housing	18,814	-	402,647	421,461
Contributions to municipalities	395,644	-	5,643	401,287
Special pension contributions	420,312	-	0	420,312
Debt service	179,359	-	116,321	295,680
Other debt service (appropriations)	491,163	-	735,181	1,226,344
Total appropriations – current expenses	9,260,000	-	6,530,003	15,790,003
Capital improvements	0	-	153,123	153,123
Total appropriations	9,260,000	-	6,683,126	15,943,126
Year-end balance	0	-	224,695	224,695
Total appropriations and year-end balance	$9,260,000	-	$6,907,821	$16,167,821

* Totals may not add due to rounding.
(1) Does not include grants received by agencies whose accounting systems are not centralized in the Treasury Department.
Sources: Treasury Department and Office of Management and Budget

The budget provides for total resources of $16.2 billion and General Fund total revenues of $9.260 billion. The budgeted General Fund total revenue of $9.260 billion includes base revenues of $7.072 billion, $1.578 billion from tax enforcement and compliance measures and $610.0 million in additional revenues from COFINA Stabilization Fund.

The principal changes in budgeted General Fund revenues compared to the fiscal year 2011 budget are accounted mainly by the projected collections from the new temporary excise tax under Act 154 (up $969.0 billion), sales and use taxes (up $125.0 million), withholding taxes on non-residents (up $28.5 million), alcoholic beverage (up $9.0 million), and projected decreases in excise taxes on motor vehicles and accessories (down $8.0 million), corporate income tax (down $51.0 million), federal excise taxes on offshore shipments (down $66.0 million), property taxes (down $162 million) and personal income taxes (down $239.0 million).

The fiscal year 2012 budget provides for total expenditures of $9.260 billion, consisting of General Fund expenditures of $8.650 billion and additional expenditures of $610 million that are expected to be covered from proceeds of COFINA bonds deposited in the Stabilization Fund. The budgeted total expenditures for fiscal year 2012 are $9.260 billion, or 1.2%, higher than budgeted total expenditures of $9.150 billion for fiscal year 2011, and $910.0 million, or 8.9%, lower than total expenditures of $10.170 billion for fiscal year 2010.

Budgeted expenses and capital improvements for the central government of all budgetary funds total $15.9 billion, a decrease of $142.9 million from fiscal year 2011 budgeted appropriations. The principal changes in General Fund expenditures by program in fiscal year 2012 compared to the fiscal year 2011 budget are mainly due to increases in education (up $131.4 million), economic development (up $106.4 million), special pension contributions (up $85.8 million), contributions to municipalities (up $28.5 million) public safety and protection (up $80.1 million), and decreases in general obligation bonds debt service (down $21.5 million), welfare (down $22.0 million), other debt service appropriations (down $26.0 million) and health (down $209.2 million).

Differences between Budget and Basic Financial Statements

Revenues and expenditures, as reported by the Treasury Department in its Basic Financial Statements, may differ substantially from resources and appropriations in the annual budget for a number of reasons, including the following:

(i) The budgetary accounts are on a cash basis, while financial statements prepared by the Treasury Department include accruals and other adjustments as required by government accounting standards.

(ii) Expenditures for current purposes in a particular fiscal year may include amounts appropriated for earlier periods but not previously expended or amounts not budgeted for a particular fiscal year, but expended during that year, and, conversely, may exclude amounts appropriated for such fiscal year but not expended until later periods.

(iii) Bonds are authorized by the Commonwealth in accordance with a four-year capital improvement program. Since bond sales are determined by bond market conditions and other factors, the amounts of bonds sold for these improvements are financed by advances from the General Fund to the Capital Projects Fund, which are later reimbursed from proceeds of bond or notes sales.

LITIGATION

General. The Commonwealth is a defendant in numerous legal proceedings pertaining to matters incidental to the performance of routine governmental operations. Under Act No. 104 of June 25, 1955, as amended ("Act 104"), persons are authorized to sue the Commonwealth only for causes of actions specified in said Act. The Commonwealth may be liable under Act 104 for damages up to a maximum amount of $75,000, or $150,000 if the suit involves actions for damages to more than one person or where a single injured party is entitled to several causes of action.

Under certain circumstances, as provided in Act No. 9 of November 26, 1975, as amended, the Commonwealth may provide its officers and employees, including directors of public corporations and government instrumentalities and mayors of the municipalities of the Commonwealth, with legal representation, as well as assume the payment of any judgment that may be entered against them. There is no limitation on the amount of the judgment that may be paid under the Act in cases before federal court, but in all other cases the Puerto Rico Secretary of Justice may determine whether, and to what extent, the Commonwealth will assume payment of such judgment.

With respect to pending and threatened litigation, excluding the litigation mentioned in the following paragraphs, as of June 30, 2010, the Commonwealth has included in its financial statements reported liabilities of approximately $421 million for awarded and anticipated unfavorable judgments. Such amount represents the amount estimated at the time as a probable liability or a liability with a fixed or expected due date, which would require future available financial resources for its payment. The amounts claimed exceed $7 billion; however, the ultimate liability cannot be presently determined. The Commonwealth believes that the claims are excessive and that the ultimate liability in excess of amounts provided in the financial statements, if any, would not be significant.

Recovery of Medicaid Funds. The Commonwealth is a defendant in two lawsuits filed, one in Commonwealth court and one in the U.S. District Court for the District of Puerto Rico, by certain Federally Qualified Health Centers ("FQHC") seeking to recover from the Commonwealth approximately $800 million in Medicaid wraparound payments which the Department of Health failed to make since 1997. In June 2004, the Superior Court of the Commonwealth in San Juan determined that the Commonwealth must make Medicaid "wraparound" payments to the health centers to cover the difference between the reimbursement they are owed and what they are paid by managed care organizations. The Court of Appeals of Puerto Rico, however, upheld a partial ruling allowing the Commonwealth to deduct from the payments due to the FQHCs certain grants received by these centers from the federal government. Currently, attorneys in the case filed in Commonwealth court are trying to determine the amounts due to FQHCs thereunder.

With respect to the federal case, in February 2005, the U.S. Court of Appeals (First Circuit) upheld a preliminary injunction issued by the U.S. District Court for the District of

Puerto Rico requiring the Commonwealth to make Medicaid "wraparound" payments to the health centers. In December 2008, the U.S. Court of Appeals determined that the U.S. District Court erred when it vacated the preliminary injunction entered against two of the FQHCs and determined that the Department of Health had met its obligations to establish and implement a payment system for FQHCs in compliance with the federal Medicaid statute. The U.S. Court of Appeals reversed the District Court's order vacating the preliminary injunction and remanded the case for further proceedings.

Recently, the Court entered a preliminary injunction as to the remaining 15 health centers, and granted a request by the Department of Health for Eleventh Amendment sovereign immunity. The plaintiff FQHCs immediately filed an appeal regarding the issue of Eleventh Amendment.

Meanwhile, the Department of Health filed a counter appeal regarding the Court's interpretation of certain components of the wraparound formula that must be used under the preliminary injunction to calculate wraparound payments owed to the plaintiffs. The Department has already made approximately $12 million in uncontested wraparound payments owed under the injunction. However, the Court granted the Department's request for a stay pending appeal regarding payment of an additional $14.5 million that are owed under the Court's wraparound formula. This sum has been consigned with the Court pending appeal, but may have to be increased to reflect the difference between the amounts owed under the Court's formula and the Department's formula since the consignment.

As of June 30, 2010, the Commonwealth accrued $280 million in its financial statements for this legal contingency.

Special Education Students. The Commonwealth is also a defendant in a class action presented in 1980 by parents of special-education students before Commonwealth courts alleging that the Puerto Rico Department of Education had failed to provide legally required special education and related services. In February 2002, the court issued a judgment approving the stipulations reached by the parties regarding the manner special education services should be provided. Since December 2002, the Department of Education has paid fines for not complying with the stipulations reached. The fines were originally set in the amount of $1,000 daily, and were raised to $2,000 daily in January 2006. In February 8, 2010, the court issued a resolution advancing its intention to establish a new scheme of fines ranging from $0.25 to $0.75 daily per registered student. As of February 2010, there were 121,339 students registered in the Special Education Program. Said resolution also creates a new scheme of monitoring compliance with the stipulations, including the added participation of 12 experts (each party has the right to designate 2 experts) in 6 areas of expertise. Said monitoring scheme began on July 1, 2010.

The February 2002 judgment only disposed of the injunctive relief sought by plaintiffs. Still pending before the court are the claims for damages regarding the failure to provide adequate services. In 2005, the Court of First Instance denied damages for the class as a whole. The plaintiffs appealed the decision and, in October 2005, the Court of Appeals decided that there could be no general damages award, but that every member of the class must come forward and prove their individual damages within this case. Assuming the Court grants damages to the plaintiffs, the Commonwealth estimates that each plaintiff could receive at least

$5,000. Based on a current enrollment of 120,000 students, the total award could amount to at least $600 million. The Commonwealth plans to defend vigorously each case.

The plaintiffs approached the Commonwealth to inquire about its disposition to reach a settlement agreement regarding the damages phase. At the Commonwealth's request, the plaintiffs submitted a settlement offer. Settlement conversations stopped after the parties reached an impasse during negotiations.

As of June 30, 2010, the Commonwealth had accrued $600 million in its financial statements for this legal contingency.

Other. The Commonwealth and various component units are defendants in other lawsuits alleging violations of civil rights, breach of contract, and other damage claims. Preliminary hearings and discovery proceedings are in progress. No provision for any liability that may result upon adjudication of these lawsuits has been recognized by the Commonwealth. The Commonwealth believes that the ultimate liability, if any, would not be significant.

PUERTO RICO INFRASTRUCTURE FINANCING AUTHORITY • REVENUE BONDS (PORTS AUTHORITY PROJECT), SERIES 2011

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