NEW ISSUE – BOOK-ENTRY
(See "Book-Entry Only System" under The Bonds)

In the opinion of Bond Counsel, under the provisions of the Acts of Congress now in force, (i) interest on the Bonds will be exempt from federal income tax, subject to certain conditions as described under *Tax Matters* and, in the case of the 2002 Refunding Bonds, assuming among other matters, no Change in Law as described under "Delayed Delivery of the 2002 Refunding Bonds" in *Plan of Financing,* and (ii) the Bonds and the interest thereon will be exempt from state, Commonwealth and local income taxation. However, see *Tax Matters* for a description of alternative minimum tax consequences with respect to interest on the Bonds and other tax considerations.

$1,249,770,000

COMMONWEALTH OF PUERTO RICO

$274,135,000 Public Improvement Bonds of 2001, Series A
$136,835,000 Public Improvement Bonds of 2001, Series B
$337,235,000 Public Improvement Refunding Bonds, Series 2001
$501,565,000 Public Improvement Refunding Bonds, Series 2002
(General Obligation Bonds)

Dated: Date of Delivery — Due: July 1, as shown below

The Bonds are issuable as registered bonds without coupons in denominations of $5,000 or any multiple thereof. Interest on the Public Improvement Bonds of 2001 and the Public Improvement Refunding Bonds, Series 2001 (collectively, the "2001 Bonds"), will be payable beginning on January 1, 2002 and each July 1 and January 1 thereafter. Interest on the Public Improvement Refunding Bonds, Series 2002 (the "2002 Bonds" and together with the 2001 Bonds, the "Bonds"), will be payable beginning on July 1, 2002 and on each January 1 and July 1 thereafter. Certain of the Bonds are subject to redemption prior to maturity as set forth herein, the earliest possible date of redemption being July 1, 2011. See *The Bonds.*

The Bonds are general obligations of the Commonwealth of Puerto Rico. The good faith, credit and taxing power of the Commonwealth are irrevocably pledged for the prompt payment of the principal of and interest on the Bonds. The Constitution of Puerto Rico provides that public debt of the Commonwealth, including the Bonds, constitutes a first claim on available Commonwealth revenues.

The scheduled payment of principal of and interest on the 2001 Bonds when due will be guaranteed under an insurance policy to be issued concurrently with the delivery of the 2001 Bonds by Financial Security Assurance Inc. See *Bond Insurance.*

The principal of and interest on the 2002 Bonds maturing after July 1, 2005 and a portion of the 2002 Bonds maturing on July 1, 2005, as shown in the inside cover, will be insured by a municipal bond new issue insurance policy issued by Financial Guaranty Insurance Company. See *Bond Insurance.*

The Bonds are offered for delivery when, as and if issued and accepted by the Underwriters, subject to the approval of legality by Sidley Austin Brown & Wood LLP, New York, New York, Bond Counsel and certain other conditions. Certain legal matters will be passed upon for the Underwriters by Fiddler González & Rodríguez, LLP, San Juan, Puerto Rico. It is expected that settlement for the 2001 Bonds will occur on or about June 7, 2001 and that settlement for the 2002 Bonds will occur on or about April 4, 2002.

Goldman, Sachs & Co. — **Merrill Lynch & Co.** — **Salomon Smith Barney**

Bear, Stearns & Co. Inc. — **JPMorgan** — **Lehman Brothers**
Morgan Stanley Dean Witter — **Samuel A. Ramírez & Co. Inc.** — **UBS PaineWebber Inc.**

May 24, 2001

$1,249,770,000
Commonwealth of Puerto Rico
$274,135,000 Public Improvement Bonds of 2001, Series A
$136,835,000 Public Improvement Bonds of 2001, Series B
$337,235,000 Public Improvement Refunding Bonds, Series 2001
$501,565,000 Public Improvement Refunding Bonds, Series 2002
(General Obligation Bonds)

$274,135,000 Public Improvement Bonds of 2001, Series A†

Maturity July 1,	Amount	Interest Rate	Yield
2014	$ 5,865,000	5 ½%	4.64%
2015	44,125,000	5 ½	4.74
2016	53,640,000	5 ½	4.81
2017	54,130,000	5 ½	4.86
2018	29,475,000	5 ½	4.91
2019	43,290,000	5 ½	4.94
2020	43,610,000	5 ¼	4.97

$136,835,000 Public Improvement Bonds of 2001, Series B†

Maturity July 1,	Amount	Interest Rate	Price or Yield
2014	$19,045,000	4.70%	4.71%
2015	10,790,000	4.80	4.82
2016	4,110,000	4.90	100
2017	6,910,000	4.95	4.96
2018	15,065,000	5	5.01
2019	3,585,000	5.05	100
2020	6,930,000	5.05	5.08
2021	14,475,000	5	5.09
2021	10,020,000	5.05	5.09
2023	14,045,000	5 ⅛	100

$31,860,000 5% Term Bonds due July 1, 2023; Yield 5.125%

$337,235,000 Public Improvement Refunding Bonds, Series 2001†

$35,210,000 5% Term Bonds due July 1, 2024; Yield 5.13%
$132,035,000 5 ¼% Term Bonds due July 1, 2027; Yield 5.16%*
$169,990,000 5 ⅛% Term Bonds due July 1, 2030; Yield 5.23%

$501,565,000 Public Improvement Refunding Bonds, Series 2002

Maturity July 1,	Amount	Interest Rate	Yield
2003	$11,070,000	5%	3.90%
2004	13,045,000	5	4.10
2005	2,450,000	5	4.20
2005	21,190,000‡	5	4
2006	32,815,000‡	5	4.11
2007	54,450,000‡	5	4.22
2008	53,105,000‡	5	4.34
2009	44,090,000‡	5 ¼	4.46
2010	45,885,000‡	5 ¼	4.56
2011	61,975,000‡	5 ½	4.65
2012	65,370,000‡	5 ½	4.75
2013	68,970,000‡	5 ½	4.84
2014	27,150,000‡	5 ½	4.91

* Yield to July 1, 2011 call date.

† Insured by Financial Security Assurance Inc.

‡ Insured by Financial Guaranty Insurance Company

Commonwealth of Puerto Rico

Governor
Sila M. Calderón

Chief of Staff
César Miranda

Members of the Cabinet

Ferdinand Mercado
Secretary of State

Anabelle Rodríguez
Secretary of Justice

Juan A. Flores
Secretary of the Treasury

César Rey
Secretary of Education

Víctor Rivera Hernández
Secretary of Labor and Human Resources

Johnny Rullán
Secretary of Health

Fernando Toledo
Secretary of Agriculture

José Izquierdo
Secretary of Transportation And Public Works

Ramón Cantero-Frau
Secretary of Economic Development and Commerce

Yolanda Zayas
Secretary of Family Affairs

Ileana Echegoyen
Secretary of Housing

Carlos Manuel Padín
Secretary of Natural and Environmental Resources

Fernando Torres Ramírez
Secretary of Consumer Affairs

Jorge Rosario
Secretary of Sports and Recreation

Víctor Rivera González
Secretary of Correction and Rehabilitation

Legislative Officers

Antonio Fas Alzamora
President, Senate

Carlos Vizcarrondo
Speaker, House of Representatives

Fiscal Officers

Melba Acosta
Director, Office of Management and Budget

Juan Agosto Alicea
President, Government Development Bank for Puerto Rico

Other Officials

Frederick Muhlach
President, Planning Board

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No dealer, broker, sales representative or other person has been authorized by the Commonwealth or the Underwriters to give any information or to make any representations other than those contained herein and if given or made such other information or representations must not be relied upon as having been authorized by the Commonwealth or any Underwriter. 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 any person in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale. The information set forth herein has been obtained from the Commonwealth, Financial Security Assurance Inc., Financial Guaranty Insurance Company and other official sources that are believed to be 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 Commonwealth since the date hereof. The Underwriters have provided the following three sentences for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with and as 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.

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

Other than with respect to information concerning Financial Security Assurance Inc. ("FSA Insurance") and Financial Guaranty Insurance Company ("FGIC Insurance") contained under the caption "*Bond Insurance*" and *Appendices III* and *IV* herein, none of the information in this Official Statement has been supplied or verified by FSA Insurance or FGIC Insurance, and they make no representation or warranty, express or implied, as to (i) the accuracy or completeness of such information; (ii) the validity of the Bonds; or (iii) the tax exempt status of the interest on the Bonds.

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$1,249,770,000

Commonwealth of Puerto Rico

$274,135,000 Public Improvement Bonds of 2001, Series A
$136,835,000 Public Improvement Bonds of 2001, Series B
$337,235,000 Public Improvement Refunding Bonds, Series 2001
$501,565,000 Public Improvement Refunding Bonds, Series 2002
(General Obligation Bonds)

INTRODUCTORY STATEMENT

This Official Statement of the Commonwealth of Puerto Rico (the "Commonwealth" or "Puerto Rico") which includes the cover page, the inside cover page and the appendices hereto, provides certain information in connection with the sale of $274,135,000 Commonwealth of Puerto Rico Public Improvement Bonds of 2001, Series A, $136,835,000 Commonwealth of Puerto Rico Public Improvement Bonds of 2001, Series B (collectively, the "Public Improvement Bonds"), $337,235,000 Commonwealth of Puerto Rico Public Improvement Refunding Bonds, Series 2001 (the "2001 Refunding Bonds") and $501,565,000 Commonwealth of Puerto Rico Public Improvement Refunding Bonds, Series 2002 (the "2002 Refunding Bonds"; the 2002 Refunding Bonds and the 2001 Refunding Bonds are herein collectively called the "Refunding Bonds"; and the Public Improvement Bonds, the 2001 Refunding Bonds and the 2002 Refunding Bonds are herein collectively called the "Bonds"). The Public Improvement Bonds and the 2001 Refunding Bonds will be insured by an insurance policy (the "FSA Bond Insurance Policy") issued by Financial Security Assurance Inc. ("FSA Insurance"). The 2002 Refunding Bonds maturing after July 1, 2005 and the 2002 Refunding Bonds in the aggregate principal amount of $21,190,000 maturing on July 1, 2005 (the "2002 Insured Bonds") will be insured by an insurance policy (the "FGIC Bond Insurance Policy"; and collectively with the FSA Bond Insurance Policy, the "Policies") issued by Financial Guaranty Insurance Company ("FGIC Insurance").

The Public Improvement Bonds are being issued under the provisions of Act No. 118 of the Legislature of Puerto Rico, approved July 13, 2000 ("Act No. 118"), and pursuant to a resolution authorizing the issuance of the Public Improvement Bonds (the "Public Improvement Bond Resolution") adopted by the Secretary of the Treasury and approved by the Governor of Puerto Rico on May 24, 2001. The Refunding Bonds are being issued under the provisions of Act No. 33 of the Legislature of Puerto Rico, approved December 7, 1942 ("Act No. 33", and Act No. 118 together with Act No. 33, the "Act") and pursuant to a resolution authorizing the issuance of the Refunding Bonds (the "Refunding Bond Resolution", and together with the Public Improvement Bond Resolution, the "Bond Resolution") adopted by the Secretary of the Treasury and approved by the Governor of Puerto Rico on May 24, 2001.

Under the Act, the good faith, credit and taxing power of the Commonwealth are irrevocably pledged for the prompt payment of the principal of and interest on the Bonds. The Constitution of Puerto Rico provides that public debt of the Commonwealth, including the Bonds, constitutes a first claim on available Commonwealth revenues.

This Official Statement also incorporates by reference the Comprehensive Annual Financial Report of the Commonwealth for the fiscal year ended June 30, 2000 prepared by the Department of the Treasury (the "Commonwealth's Annual Financial Report"), which report includes the general purpose financial statements of the Commonwealth for the fiscal year ended June 30, 2000, together with the independent auditor's report thereon, dated December 29, 2000, of Deloitte & Touche LLP, independent auditors, and is incorporated by reference herein in reliance upon the reports of such firm given their authority as experts in accounting and auditing. The Commonwealth's Annual Financial Report has been filed by the Commonwealth with each nationally recognized municipal securities information repository ("NRMSIR"). Any appendix of an Official Statement of the Commonwealth or of any instrumentality of the Commonwealth containing the Commonwealth's Annual Financial Report filed with each NRMSIR and the Municipal Securities Rulemaking Board (the "MSRB") or any other document containing the Commonwealth's Annual Financial Report filed with each NRMSIR 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 herein or in any of the above described documents incorporated herein by reference shall be deemed to be modified or superseded for purposes of this Official Statement to the extent that a statement contained herein or in any 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.

The Commonwealth will provide, without charge to any person to whom this Official Statement is delivered, on the written request of such person, a copy of the Commonwealth's Annual Financial Report incorporated herein by reference. Requests should be directed to Director-New York Office, Government Development Bank for Puerto Rico, 140 Broadway, 38th Floor, New York, NY 10005, telephone number (212) 422-6420, or to Director-General Obligations Division, Government Development Bank for Puerto Rico, P.O. Box 42001, San Juan, PR 00940, telephone number (787) 722-7060.

A copy of the Commonwealth's Annual Financial Report may be obtained by contacting a NRMSIR. The address of each NRMSIR is set forth in *Continuing Disclosure* below.

OVERVIEW

The following is a summary of certain information regarding the Commonwealth contained in the Commonwealth of Puerto Rico Financial Information and Operating Data Report, dated April 30, 2001 (the "Commonwealth Report"), attached hereto as *Appendix I*. This summary does not purport to be complete and is qualified in its entirety by reference to more detailed information appearing in the Commonwealth Report, which should be read in its entirety.

Puerto Rico is located approximately 1,600 miles southeast of New York City. The U.S. Census Bureau has determined Puerto Rico's population to be 3,808,610 for the year 2000. Puerto Rico's political status is that of a commonwealth. The United States and the Commonwealth share a common defense, market, currency and citizenship. The Commonwealth exercises virtually the same control over its internal affairs as is exercised by the state governments of each of the fifty states over their respective internal affairs, with similar separation of powers among the executive, legislative and judicial branches; however, it differs from the states 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 who has a voice in the House of Representatives but no vote. Most federal taxes, except those such as Social Security taxes which are imposed by mutual consent, 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. The official languages of Puerto Rico are Spanish and English.

Economic Trends

Puerto Rico has enjoyed seventeen years of uninterrupted economic expansion. Factors contributing to this expansion include government-sponsored economic development programs, periodic declines in the exchange value of the United States dollar which is the currency used in the

Commonwealth, increases in the level of federal transfers, the relatively low cost of borrowing, and until recently, low oil prices.

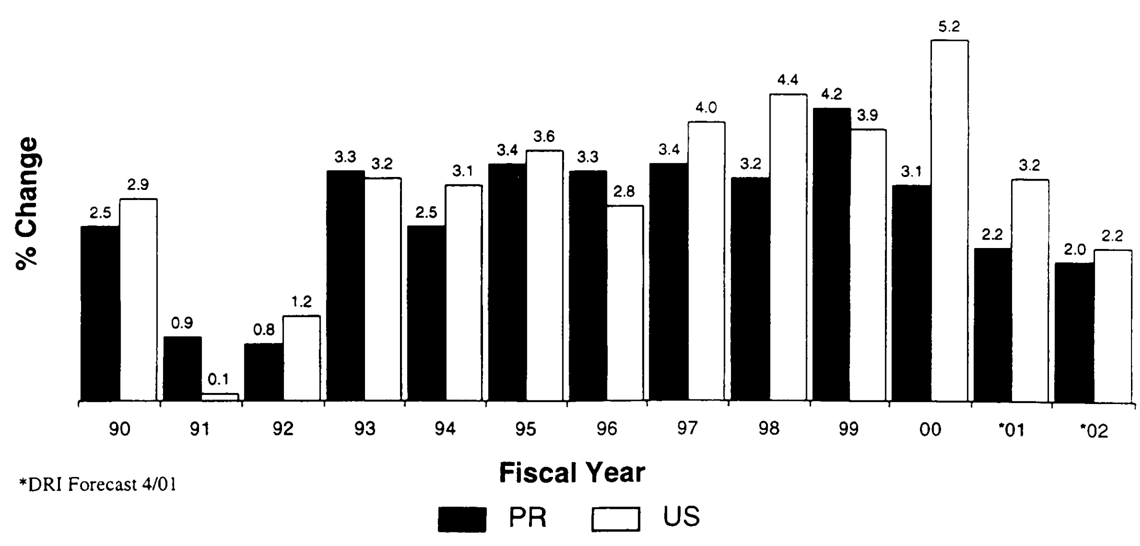
Gross product in fiscal 2000 was $41.4 billion ($34.8 billion in 1996 prices) and in fiscal 1996 was $30.4 billion. This represents an increase in gross product of 36.3% from fiscal 1996 to 2000 (14.7% in 1996 prices). Since fiscal 1985, personal income, both aggregate and per capita has increased consistently each fiscal year. In fiscal 2000, aggregate personal income was $38.2 billion ($34.6 billion in 1996 prices) and personal income per capita was $9,870 ($8,925 in 1996 prices). The difference in the statistics of 1996 for gross product and personal income is attributable to the different price deflators used for each.

Average employment increased from 1,092,200 in fiscal 1996, to 1,159,470 in fiscal 2000. Average unemployment decreased from 13.8% in fiscal 1996 to 11.0% in fiscal 2000. According to the Labor Department's Household Employment Survey, during fiscal 2000 total employment increased 1.1% over fiscal 1999. Total monthly employment averaged 1,159,470 in fiscal 2000, compared to 1,146,660 in fiscal 1999. The seasonally adjusted unemployment rate for March 2001 was 10.6%.

According to the Labor Department's Household Employment Survey, during the first nine months of fiscal 2001, total employment increased 1.0% over the same period in fiscal 2000. Monthly employment averaged 1,160,220 during the first nine months of fiscal 2001, compared to 1,149,700 for the same period in fiscal 2000.

The Planning Board's gross product forecast for fiscal 2001, made in March 2001, projected an increase of 2.2% over fiscal 2000 and an increase of 2.0% for fiscal 2002. The performance of the economy during fiscal 2001 and 2002 will be affected principally by the performance of the United States economy and by the increase in oil prices and the level of interest rates. The change in the Federal Reserve monetary policy to lower interest rates embodies a positive impact for the Commonwealth's economy, primarily its construction industry. Since Puerto Rico is heavily dependent on oil imports for its energy needs, if the level of oil prices remains at its current high level for a long period of time, that could have an adverse effect on the level of economic activity in Puerto Rico during the remainder of fiscal 2001 and during fiscal 2002.

Real GNP Growth Rate



Puerto Rico has a diversified economy with the manufacturing and services sectors comprising the principal sectors. Manufacturing is the largest sector in terms of gross domestic product. According to the Planning Board's figures, in fiscal 2000 manufacturing generated $27.4 billion, or 43.5%, of gross domestic product and accounted for 13.7% of total employment, as compared with fiscal 1999, when it generated $26.6 billion, or 44.4%, of gross domestic product and accounted for 13.9% of total employment. See "Economic Performance by Sector" under *The Economy* in the Commonwealth Report. Manufacturing in Puerto Rico is now more diversified than during the earlier phases of its industrial development and includes several industries less prone to business cycles. In the last two 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 the heavy investment in the pharmaceutical, scientific instruments, computers, medical products and electrical products industries in Puerto Rico over the last decade. One of the factors assisting the development of the manufacturing sector has been the tax incentives offered by the federal and Puerto Rico governments. Federal legislation enacted in 1996, however, which amended Internal Revenue Code Section 936, phased out the federal tax incentives during a ten-year period. See "Tax Incentives - Incentives Under the Code" under *The Economy* in the Commonwealth Report.

The services sector, which includes hotel and related services and currently accounts for approximately 50.7% of total employment, generated $24.0 billion, or 38.1%, of Puerto Rico's gross domestic product in fiscal 2000, as compared with $22.3 billion, or 37.2%, of gross domestic product in fiscal 1999.

Growth in construction contributed to increased economic activity in fiscal 2000. The growth in the construction industry was evidenced by a nominal increase of 7.3% in construction investment for fiscal 2000 over fiscal 1999.

Tourism continues to make a significant contribution to economic activity. More than 4.6 million visitors spent $2.4 billion in Puerto Rico in fiscal 2000. San Juan has become the largest home port for cruise ships in the Caribbean and the second largest home port for cruise ships in the world. Twenty-six U.S. and international airlines offer scheduled service to and from San Juan and American Airlines uses San Juan as a hub for its intra-Caribbean operations. This reflects the importance of Puerto Rico as a tourist destination and as a transportation hub in the Caribbean.

Fiscal Management

Fiscal responsibility for the Commonwealth is shared among the Department of the Treasury, the Office of Management and Budget and the Government Development Bank for Puerto Rico ("Government Development Bank"). The Department of the Treasury is responsible for collecting most of the Commonwealth's revenues, overseeing preparation of its financial statements and contributing to the preparation of the budget. The Office of Management and Budget prepares the Commonwealth budget and has the responsibility for monitoring expenditures. Government Development Bank is the fiscal agent and financial advisor to the Commonwealth and its agencies, public corporations and municipalities and coordinates the management of public finances.

Section 7 on Article VI of the Constitution of Puerto Rico 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 financial statements of the Commonwealth for fiscal 2000 were audited by Deloitte & Touche LLP, whose report thereon is dated December 29, 2000. For a summary of the Commonwealth's significant accounting policies, see Note 1 to the Commonwealth's general purpose financial statements included in the Commonwealth's Annual Financial Report. Preparation of the audited financial statements of the Commonwealth involves the collection and combination of audited financial statements from 50 separate reporting entities.

Debt Management

The Constitution of Puerto Rico limits the amount of general obligation debt that can be issued. The Commonwealth's policy has been and continues to be to maintain the level of such debt within a prudent range below the constitutional limitation. See "Debt Limitation" under *The Bonds*.

Historically, the Commonwealth has maintained a fiscal policy which provides for a prudent relationship between the growth of public sector debt and the growth of the economic base required to service that debt. Since fiscal 1996, however, public sector debt increased at a rate greater than the growth of gross product due to an increase in the amount of debt incurred to finance certain key infrastructure projects which are important to the development of the economy and are expected to produce long term economic benefits. This increase in debt has been partially offset by debt incurred to refinance outstanding debt that has enabled Puerto Rico to benefit from the historically low levels of interest rates and realize debt service savings. See "Trends of Public Sector Debt" under *Debt* and "Economic Performance by Sector - Construction" under *The Economy* in the Commonwealth Report.

PLAN OF FINANCING

The Public Improvement Bonds

The net proceeds of the Public Improvement Bonds will be deposited in (i) the 2001 Public Improvements Fund established under Act No. 118 to carry out the capital improvement programs authorized by the Legislature, including but not limited to highways and transportation facilities, aqueduct and sewer facilities, schools, health and social welfare facilities, agricultural and tourism facilities, park and other recreation facilities, flood control and solid waste facilities, housing, municipal projects, and other governmental projects, and (ii) the Extraordinary Maintenance Fund established under Act No. 66 of the Legislature of Puerto Rico, approved August 14, 1991, to be used, among various purposes, to cover the costs of permanent improvements related to water resources.

The Public Improvement Bonds are being issued in two series in the respective aggregate principal amounts of $274,135,000 and $136,835,000 and designated "Public Improvement Bonds of 2001 of the Commonwealth of Puerto Rico, Series A" and "Public Improvement Bonds of 2001 of the Commonwealth of Puerto Rico, Series B" (the "Public Improvement Series A Bonds" and the "Public Improvement Series B Bonds", respectively).

The Refunding Bonds

2001 Refunding Bonds. The 2001 Refunding Bonds will be issued for the purpose of: (a) refunding at par on July 31, 2001, $164,222,000 principal amount of special promissory notes issued on behalf of the Commonwealth by the Secretary of the Treasury to Government Development Bank (the "Promissory Notes") for the purpose of making a portion of the monthly deposits to the Commonwealth's Redemption Fund (hereinafter mentioned) and (b) refunding certain general obligation bonds of the Commonwealth as follows (the "2001 Refunded Bonds"):

Public Improvement Bonds	Principal Amount to be Refunded	Interest Rate	Maturity Date	Redemption Date	Redemption Price
1993	$ 8,495,000	5.60%	July 1, 2006	July 1, 2002	101.50%
1993	8,995,000	5.60%	July 1, 2007	July 1, 2002	101.50%
1993	9,530,000	5.70%	July 1, 2008	July 1, 2002	101.50%
1994	8,155,000	6.20%	July 1, 2007	July 1, 2004	101.50%
1997, Series B	25,000,000*	5.50%	July 1, 2002	N/A	N/A
2000	100,000,000	6.00%	July 1, 2029	July 1, 2005	101.00%

* $37,860,000 currently outstanding.

2002 Refunding Bonds. The 2002 Refunding Bonds will be issued on or about April 4, 2002 for the purpose of redeeming on July 1, 2002, at a redemption price of 101.5%, $504,760,000 aggregate principal amount of the Commonwealth's Public Improvement Refunding Bonds, Series 1992A (the "2002 Refunded Bonds"; and together with the 2001 Refunded Bonds, the "Refunded Bonds"), stated to mature as set forth below:

Principal Amount to be Refunded	Interest Rate	Maturity Date (July 1)
$ 11,310,000	5.875%	2005
10,090,000	6.00%	2006
26,700,000	N/A	2008 (ARNs)
26,700,000	N/A	2008 (YCNs)
28,750,000	5.75%	2009
30,925,000	6.25%	2010
180,485,000	6.00%	2014
94,900,000	N/A	2020 (ARNs)
94,900,000	N/A	2020 (YCNs)

Making and Effect of Escrow Deposits - The 2001 Refunding Bonds. The Secretary of the Treasury will deposit the net proceeds of the 2001 Refunding Bonds into two escrow funds with Banco Popular de Puerto Rico (the "Escrow Agent"). One of said funds will relate to the refunding of the Public Improvement Bonds of 1993 and 2000 as described above (the "1993 and 2000 Escrow Fund"), and the other will relate to the refunding of the Promissory Notes and the Public Improvement Bonds of 1994 and 1997, Series B as described above (the "1994 and 1997B Escrow Fund"). A portion of the net proceeds of the 2001 Refunding Bonds will be invested in noncallable United States Treasury obligations (in the case of the 1994 and 1997B Escrow Fund) and in legally permitted investments consisting of a guaranteed investment contract with Transamerica Occidental Life Insurance Company, which agreement is insured by AMBAC Assurance Corporation (in the case of the 1993 and 2000 Escrow Fund), the principal of and interest (or other payments) on which, with any uninvested moneys, will be sufficient to pay the principal of and premium, if any, on the 2001 Refunded Bonds on the maturity or redemption dates set forth above, which redemption dates will be irrevocably designated by the Secretary of the Treasury in the Refunding Bond Resolution, and to pay the interest thereon (after July 1, 2001) to such dates. The sufficiency of the amount so deposited, with investment earnings thereon, to accomplish the refunding of the Refunded Bonds referred to above in this paragraph, will be verified by Samuel Klein and Company (the "Verification Agent"). Upon the deposit of cash and the noncallable United States Treasury obligations into the 1994 and 1997B Escrow Fund with the Escrow Agent referred to above and upon the payment by the Commonwealth on July 1, 2001 of the debt service on said Refunded Bonds, the Public Improvement Bonds of 1994 and 1997, Series B being so refunded will cease to be outstanding under the terms of their respective authorizing resolutions. In the opinion of Sidley Austin Brown & Wood LLP, Bond Counsel, once the actions described in the preceding sentence have occurred, the Public Improvement Bonds of 1994 and 1997, Series B being refunded will be deemed not to be outstanding for the purpose of applying the debt limitation under Section 2 of Article VI of the Constitution of Puerto Rico.

Making and Effect of Escrow Deposits - The 2002 Refunding Bonds. The Secretary of the Treasury will deposit the net proceeds of the 2002 Refunding Bonds into an escrow fund with the Escrow Agent. A portion of the net proceeds of the 2002 Refunding Bonds will be invested in legally permitted investments consisting of guaranteed investment agreements with Trinity Plus Funding Company, LLC ("Trinity") and with AIG Matched Funding Corp. the payments on which, with any uninvested moneys, will be sufficient to pay the principal of and premium on the 2002 Refunded Bonds on July 1, 2002, which redemption date will be irrevocably designated by the Secretary of the Treasury in the Refunding Bond Resolution, and to pay the interest thereon after the issuance of the 2002 Refunding Bonds to such date. The sufficiency of the amount so deposited, with investment earnings thereon, to accomplish the refunding of the 2002 Refunded Bonds, will be verified by the Verification Agent.

Trinity is a limited liability company one of whose common members is FGIC MRCA Corp., an affiliate of FGIC Insurance whose policy is insuring a portion of the 2002 Refunding Bonds. The FGIC Bond Insurance Policy does not in any way cover Trinity's obligations under its investment agreement with the Escrow Agent in respect of the 2002 Refunded Bonds, nor will FGIC Insurance be liable to cover any defaults by Trinity under said guaranteed investment agreement. See *Bond Insurance*, below.

Sources and Uses of Funds

Sources:

Principal amount of the Bonds	$1,249,770,000.00
Net original issue premium	38,413,893.90
Total sources	$1,288,183,893.90

Uses:

Deposit into the 2001 Public Improvements Fund	$ 400,500,000.00
Deposit into the Extraordinary Maintenance Fund	21,250,000.00
Deposit into Escrow Fund for 2001 Refunded Bonds	329,370,465.35
Deposit into Escrow Fund for 2002 Refunded Bonds	518,987,192.62
Underwriting discount, insurance premiums and other financing expenses	18,076,235.93
Total uses	$1,288,183,893.90

Delayed Delivery of the 2002 Refunding Bonds

Only the 2001 Bonds are expected to be issued in 2001. The 2002 Refunding Bonds are expected to be issued on or about April 4, 2002. The Commonwealth is required to issue the 2002 Refunding Bonds and the Underwriters are required to purchase the 2002 Refunding Bonds unless (1) the Underwriters are not permitted to purchase the 2002 Refunding Bonds because of a Change in Law (as defined below) or (2) the Commonwealth and the Underwriters do not receive (a) the opinion of Bond Counsel described below, and certain opinions of counsel to the Commonwealth and counsel to the Underwriters, (b) a supplement to this Official Statement (the "2002 Supplement"), together with a certificate of the Commonwealth as to the accuracy of this Official Statement as so supplemented, and (c) a certificate of the Commonwealth to the effect that it is not aware of the existence of any default under the Resolution (the "No-Default Certificate").

ADVERSE CHANGES (FINANCIAL OR OTHER) IN THE AFFAIRS OF THE COMMONWEALTH WILL NOT EXCUSE THE UNDERWRITERS FROM PAYING FOR AND TAKING DELIVERY OF THE 2002 REFUNDING BONDS UNLESS ANY SUCH ADVERSE CHANGE HAS NOT BEEN ACCURATELY AND COMPLETELY DESCRIBED IN OR INCORPORATED BY REFERENCE IN THE 2002 SUPPLEMENT OR THE COMMONWEALTH IS UNABLE TO DELIVER THE NO-DEFAULT CERTIFICATE DESCRIBED ABOVE.

It is a condition of the issuance of the 2002 Refunding Bonds that Bond Counsel deliver its approving opinion on the 2002 Refunding Bonds substantially in the form set forth in *Appendix II.* Bond Counsel's ability to deliver this opinion is subject to its review and analysis at the time the 2002 Refunding Bonds are to be issued of certain matters, including, among others, (1) the application of the proceeds of the 2002 Refunding Bonds, (2) pertinent provisions of law, including, but not necessarily limited to, Puerto Rico law and federal income tax and securities laws then in effect or proposed to be in effect and (3) certifications and representations delivered or made by the Commonwealth and the Underwriters at the time of issuance of the 2002 Refunding Bonds. Bond Counsel has advised the Commonwealth and the Underwriters that, (A) if the Commonwealth and the Underwriters satisfy their respective obligations set forth in the contract of purchase for the 2002 Refunding Bonds (the "Contract of Purchase") and (B) if there is no change in any applicable law, or in any other facts or circumstances (tax or otherwise) that, in Bond Counsel's view, affect or are material to its opinion, and (C) if such certifications and representations are delivered or made to Bond Counsel's satisfaction, Bond Counsel expects to be able to deliver an approving opinion substantially in the form attached hereto as *Appendix II.* No assurances can be given that there will be no change in applicable law prior to the time the 2002 Refunding Bonds are to be issued, that the facts and circumstances that are material to such opinion will not differ at the time the 2002 Refunding Bonds are to be issued from those currently expected, or that such certifications and representations will be delivered and made. As a consequence, no assurance can be made that an approving opinion on the 2002 Refunding Bonds will be delivered by Bond Counsel.

FAILURE TO DELIVER THE 2002 SUPPLEMENT OR THE OPINIONS AND CERTIFICATES IN THE FORM AND SUBSTANCE PROVIDED FOR IN THE CONTRACT OF PURCHASE (UNLESS SUCH FAILURE IS WAIVED BY THE UNDERWRITERS) WILL MEAN THAT THE 2002 REFUNDING BONDS WILL NOT BE ISSUED AND DELIVERED. THE UNDERWRITERS HAVE THE RIGHT, BUT ARE UNDER NO OBLIGATION, TO WAIVE ANY SUCH FAILURE.

In addition, the Underwriters are not required to purchase the 2002 Refunding Bonds if at any time on or prior to the date the 2002 Refunding Bonds are to be issued, as a result of a Change in Law, the Underwriters are or would be prohibited from lawfully purchasing the 2002 Refunding Bonds or lawfully selling the 2002 Refunding Bonds to the public.

As defined in the Contract of Purchase, "Change in Law" means (i) any change in federal, Puerto Rico or state law or any changes in regulations or other pronouncements or interpretations by federal, Puerto Rico or state agencies, (ii) the enactment, introduction or proposal of any federal legislation (if it has a proposed effective date that is on or before the date the 2002 Refunding Bonds are to be issued), (iii) the enactment, introduction or proposal of any law, rule or regulation by any other governmental body, department or agency (federal, Puerto Rico or state) (if it has a proposed effective date that is on or before the date the 2002 Refunding Bonds are to be issued) or (iv) the handing down of a judgment, ruling or order issued by any court or administrative body, which in each case would prohibit (or have the retroactive effect of prohibiting, if enacted, adopted, passed or finalized) the Underwriters from purchasing or selling the 2002 Refunding Bonds to the public (or would make the Commonwealth's issuance, sale or delivery illegal, if enacted, adopted, passed or finalized); provided, however, that such change in law, rule or regulation or judgment, ruling or order shall have become effective or been enacted, introduced, proposed or issued, as the case may be, after the date of this Official Statement.

Events that may occur prior to the issuance of the 2002 Refunding Bonds may have significant consequences to persons who have agreed to purchase the 2002 Refunding Bonds. The market prices of the 2002 Refunding Bonds on the date the 2002 Refunding Bonds are issued are unlikely to be the same as the purchase prices therefor, and such differences may be substantial. Several facts may adversely affect such prices, including (but not limited to) a general increase or decrease in market interest rates, any threatened or adopted change in the federal income tax laws affecting the relative benefits of owning tax-exempt securities versus other types of investments, or any adverse development with respect to the

Commonwealth's financial condition or prospects or with respect to the ratings on the Commonwealth's indebtedness, including the ratings on the 2002 Refunding Bonds. In addition, although the delivery of the approving opinion of Bond Counsel is a condition to the issuance and delivery of the 2002 Refunding Bonds and is subject to a number of conditions to be fulfilled at the time of such delivery as described above, changes or proposed changes in federal income tax laws or regulations or interpretations thereof could affect the market value of tax-exempt securities, including the 2002 Refunding Bonds, without preventing the delivery of such opinion or the delivery of the 2002 Refunding Bonds.

THE BONDS

General

The Bonds will be dated, bear interest at such rates, be payable at such times, and mature on the dates and in the principal amounts set forth on the inside cover page of this Official Statement. Certain Bonds are subject to redemption at the times and at the prices set forth below in "Redemption".

Book-Entry Only System

The following information concerning The Depository Trust Company ("DTC"), New York, New York and DTC's book-entry system has been obtained from DTC. Neither the Commonwealth nor the Underwriters take any responsibility for the accuracy thereof.

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

DTC 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 securities that its participants (the "Direct Participants") deposit with DTC. DTC also facilitates the settlement among Direct Participants of securities transactions, such as transfers and pledges, in deposited securities through electronic computerized book-entry changes in Direct Participants' accounts, thereby eliminating the need for physical movement of securities certificates. Direct Participants include securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is owned by a number of its Direct Participants and by the New York Stock Exchange, Inc., the American Stock Exchange, Inc. and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as securities brokers and dealers, banks and trust companies that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (the "Indirect Participants" and together with the Direct Participants, the "Participants"). The Rules applicable to DTC and its Participants are on file with the Securities and Exchange Commission.

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 a Bond (a "Beneficial Owner") will in turn be recorded in the Direct or Indirect Participants' records. Beneficial Owners will not receive written confirmations from DTC of their purchases, but Beneficial Owners are expected to receive written confirmation 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 will be accomplished by entries made on the books of Direct and Indirect Participants acting on behalf of the

Beneficial Owners. Beneficial Owners will not receive definitive 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 nominee as may be requested by an authorized representative of DTC. The deposit of Bonds with DTC and their registration in the name of Cede & Co. effect no 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 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.

Redemption notices will be sent to Cede & Co. If less than all of the Bonds within a maturity and issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in the Bonds to be redeemed.

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

Principal, redemption premium, if any, and interest payments on the Bonds will be made to DTC or to such other nominee as may be requested by DTC. DTC's practice is to credit Direct Participants' accounts on the payable date in accordance with their respective holdings shown on DTC's records unless DTC has reason to believe that it will not receive payment on the payment date. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name", and will be the responsibility of such Participant and not of DTC, the Commonwealth or Banco Popular de Puerto Rico as paying agent and registrar (the "Registrar"), subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal, redemption premium, if any, and interest to DTC is the responsibility of the Commonwealth or the Registrar, disbursement of such payments to Direct Participants shall be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners shall be the responsibility of Direct and Indirect Participants.

DTC may discontinue providing its services as securities depository with respect to the Bonds at any time by giving reasonable notice to the Commonwealth or the Registrar. Under such circumstances, in the event that a successor securities depository is not obtained, definitive Bonds are required to be printed and delivered, to or for the account of the respective Beneficial Owners.

The Commonwealth may decide to discontinue use of the system of book-entry transfers through DTC (or a successor securities depository). In that event, definitive Bonds will also be printed and delivered, to or for the account of the respective Beneficial Owners.

Payments and Transfers

No assurance can be given by the Commonwealth that DTC will make prompt transfer of payments to the Participants or that Participants will make prompt transfer of payments to Beneficial

Owners. The Commonwealth is not responsible or liable for payment by DTC or Participants or for sending transaction statements or for maintaining, supervising or reviewing records maintained by DTC or Participants.

For every transfer and exchange of the Bonds, the Beneficial Owners may be charged a sum sufficient to cover any tax, fee or other charge that may be imposed in relation thereto.

Discontinuance of the Book-Entry Only System

In the event that the book-entry only system is discontinued, the following provisions will apply: principal of and redemption premium, if any, on the Bonds shall be payable in lawful money of the United States of America at the corporate trust office of the Registrar in San Juan, Puerto Rico. Interest on the Bonds will be payable by check mailed to the respective addresses of the registered owners determined as of the applicable record date thereof provided in the Bond Resolution as shown on the registration books of the Commonwealth maintained by the Registrar. The Bonds will be issued only as registered Bonds without coupons in denominations of $5,000 or any multiple thereof. The transfer of the Bonds will be registrable and they may be exchanged at the corporate trust office of the Registrar in San Juan, Puerto Rico, upon the payment of any taxes or other governmental charges required to be paid with respect to such registration of transfer or exchange.

Authorization

Section 2 of Article VI of the Constitution of Puerto Rico provides that the power of the Commonwealth to contract and to authorize the contracting of debts shall be exercised as determined by the Legislature. Pursuant to this power, the Legislature enacted the Act, which authorizes the issuance of the Bonds.

Redemption

Optional Redemption. The Public Improvement Series A Bonds are not subject to optional redemption.

At the option of the Secretary of the Treasury and upon at least 30 days' notice, the outstanding Public Improvement Series B Bonds and the 2001 Refunding Bonds are subject to redemption, from any moneys that may be available for that purpose (other than moneys set aside in respect of an amortization requirement), prior to maturity, on or after July 1, 2011, as a whole or in part, as directed by the Secretary of the Treasury, at any time at the principal amount together with the interest thereon to the date fixed for redemption, without premium.

The 2002 Refunding Bonds are not subject to optional redemption.

Mandatory Redemption. The term Public Improvement Series B Bonds maturing July 1, 2023, and the 2001 Refunding Bonds maturing July 1, 2024, July 1, 2027 and July 1, 2030 are subject to redemption on or before July 1, 2022 and on or before each July 1 thereafter in respect of each fiscal year for which there is an amortization requirement, to the extent of the respective amortization requirements therefor set forth below (less the amount applied to the purchase of any such 2001 Refunding Bonds and otherwise subject to adjustment as described below), upon at least 30 days' notice at a redemption price of par plus accrued interest to the dates fixed for redemption.

	Amortization Requirements			
Year	Public Improvement Series B Term Bonds due July 1	2001 Refunding Term Bonds due July 1		
	2023	2024	2027	2030
2022	$ 25,725,000			
2023	6,135,000	$ 6,830,000		
2024		28,380,000		
2025			$ 29,795,000	
2026			40,880,000	
2027			61,360,000	
2028				$ 64,580,000
2029				67,890,000
2030				37,520,000
Average Life (years):	21.3	22.9	25.3	27.9

If the amount of the term Bonds purchased or redeemed pursuant to an amortization requirement during any fiscal year exceeds the amount of the amortization requirement for such Bonds for such fiscal year, the amortization requirement for such Bonds may be decreased for such subsequent fiscal years and in such amounts aggregating the amount of such excess as the Secretary of the Treasury shall determine.

Notice and Effect of Redemption on Bonds

Any redemption of the Bonds, either in whole or in part, shall be made upon at least thirty (30) days' prior notice by mail to DTC or, if the book-entry only system as described above has been discontinued, by first class mail postage prepaid to all registered owners in the manner and under the terms and conditions provided in the Bond Resolution. On the date designated for redemption notice having been given as provided in the Bond Resolution and moneys for payment of the principal of and redemption premium, if any, and accrued interest on the Bonds or portions thereof so called for redemption being held by the Registrar, interest on the Bonds or portions thereof so called for redemption shall cease to accrue. Subject to certain provisions of the Bond Resolution, Bonds and portions of Bonds which have been duly called for redemption under the provisions of the Bond Resolution or with respect to which irrevocable instructions to call for redemption or to pay at maturity have been given, and for the payment of the principal of and redemption premium if any, and the accrued interest on which sufficient moneys or investments permitted by law shall be held in separate trust for the owners of the Bonds or portions thereof to be paid or redeemed, shall not be deemed to be outstanding under the Bond Resolution and the registered owners thereof shall have no rights in respect thereof except to receive payment of the principal thereof and the redemption premium, if any, and the accrued interest thereon from said separate trust.

Each notice of redemption shall contain, among other things, the CUSIP identification number of the Bonds (or portion thereof) being called for redemption, the redemption date and price and the address at which such Bonds are to be surrendered for payment of the redemption price. Any defect in such notice or the failure so to mail any such notice to DTC in respect of or to the registered owner of any Bond will not affect the validity of the proceedings for the redemption of any other Bond.

If less than all the Bonds of any maturity and issue are called for redemption, the particular Bonds so called for redemption shall be selected by the Registrar by such method as it deems fair and appropriate except that so long as the book-entry only system shall remain in effect in the event of any such partial redemption, DTC shall reduce the credit balances of the applicable DTC Participants in respect of the Bonds and such DTC Participants shall in turn select those Beneficial Owners whose ownership interests are to be extinguished by such partial redemption, each by such method as DTC or such DTC Participant as the case may be in its sole discretion deems fair and appropriate.

Security

Provision for Payment of Public Debt

The Act provides that the good faith, credit and taxing power of the Commonwealth are irrevocably pledged for the prompt payment of the principal of and interest on the Bonds. The Secretary of the Treasury is authorized and directed under the Act to pay the principal of and interest on the Bonds as the same become due and payable from any funds available for such purpose with the Department of the Treasury in the fiscal year in which such payment is due. The provisions contained in the Act regarding the payment of the principal of and interest on the Bonds are considered to be a continuous appropriation for the Secretary of the Treasury to make such payments even though no specific appropriations are made for such purposes. Such payments are required to be made pursuant to the provisions of the laws of the Commonwealth that regulate the disbursement of public funds.

The Constitution of Puerto Rico provides that public debt of the Commonwealth will constitute a first claim on available Commonwealth revenues. Public debt includes general obligation bonds and notes of the Commonwealth and any payments required to be made by the Commonwealth under its guarantees of bonds and notes issued by its public instrumentalities.

The Commonwealth has allocated certain motor vehicle fuel taxes, crude oil and derivative products excise taxes and license fees to the Puerto Rico Highway and Transportation Authority (the "Highway Authority"). The amounts so allocated, however, are subject to first being applied to payment of the principal of and interest on the Commonwealth public debt, but only if and to the extent that all other available revenues of the Commonwealth are insufficient for that purpose. The Commonwealth has never applied such amounts to the payments of its public debt.

Since fiscal 1989, the Commonwealth has pledged to Puerto Rico Infrastructure Financing Authority certain federal excise taxes imposed on alcoholic beverages and tobacco products produced in Puerto Rico and sold in the United States which taxes are returned to the Commonwealth. The amounts so pledged, however, are subject to first being applied to payment of the principal of and interest on the Commonwealth public debt, but only if and to the extent that all other available revenues of the Commonwealth are insufficient for that purpose. The Commonwealth has never applied such amounts to the payment of its public debt.

The Constitution expressly empowers a holder of bonds and notes evidencing public debt to bring suit against the Secretary of the Treasury to require application of available revenues, including surplus, to the payment of principal of and interest on public debt when due.

Special Fund for General Obligation Debt Service

Act No. 83 of the Legislature of Puerto Rico, approved August 30, 1991, as amended, provides for the levy of an annual special tax of 1.03% of the assessed value of all real and personal property not exempt from taxation. The proceeds of said tax are credited to the Special Fund for the Amortization and Redemption of General Obligations Evidenced by Bonds and Promissory Notes (the "Redemption Fund"), for application to the payment of general obligation bonds and notes of the Commonwealth.

Act No. 39 of the Legislature of Puerto Rico, approved May 13, 1976, as amended ("Act No. 39"), requires the Secretary of the Treasury to transfer each month from available funds of the

Commonwealth to the Redemption Fund such amounts which, together with certain funds otherwise deposited therein, will be equal to the sum of one-sixth of the interest to be paid in the next six months and one-twelfth of the principal to be paid or required to be amortized within the next twelve months on all bonds and notes of the Commonwealth for which its faith and credit are pledged as the same become due and for which the guaranty of the Commonwealth has been exercised. Moneys in the Redemption Fund are held in trust by Government Development Bank. Act No. 39 provides that the obligation of the Secretary of the Treasury to make the above transfers is cumulative and the amount of any deficiency in any month shall be added to the amount of transfers required in future months until such deficiency has been fully paid. As of May 9, 2001, the amount on deposit in the Redemption Fund was $388,830,122.46, which was the required amount.

Act No. 39 expressly relates to direct obligations of the Commonwealth. It may also apply to the payment of Commonwealth guaranteed obligations of public corporations outstanding prior to the date of its adoption but not to the payment of bonds and other obligations of such public corporations guaranteed by the Commonwealth issued after the date of its adoption.

Payment Record

The Commonwealth has never defaulted on the payment of principal of or interest on any of its debt.

Debt Limitation

Section 2 of Article VI of the Constitution of Puerto Rico 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 and interest on such bonds and notes and on all such bonds and notes theretofore issued which is payable in any fiscal year, together with any amount paid by the Commonwealth in the preceding fiscal year on account of bonds or notes guaranteed by the Commonwealth, exceeds 15% of the average annual revenues raised under the provisions of Commonwealth legislation and covered into the Treasury of Puerto Rico (hereinafter "internal revenues") in the two fiscal years preceding the then current fiscal year. 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.

Internal revenues consist principally of income taxes, property 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 the Treasury of Puerto Rico, and motor vehicle fuel taxes and license fees, which are allocated to the Highway 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.

On December 21, 1995, Aqueduct and Sewer Authority issued $400,340,000 Puerto Rico Aqueduct and Sewer Authority Refunding Bonds, guaranteed by the Commonwealth (the "PRASA Guaranteed Bonds"). On January 1, 1997, the Commonwealth began to make payment of debt service on the PRASA Guaranteed Bonds under the full faith and credit guarantee of the Commonwealth. In fiscal 1999, the Commonwealth appropriated funds to help make debt service payments on $1.9 million outstanding principal amount of Puerto Rico Housing Bank and Finance Agency Special Obligation Refunding Bonds (Series H), which are guaranteed by the Commonwealth and have a final maturity of October 1, 2001 (the "Housing Bank Guaranteed Bonds"). In fiscal 2000, no appropriations were made for the payment of debt service on Housing Bank Guaranteed Bonds, and none is expected to be made for fiscal year 2001. The amount paid by the Commonwealth under the PRASA Guaranteed Bonds and the Housing Bank Guaranteed Bonds will be taken into account for purposes of computing the above described 15% constitutional debt limitation.

After giving effect to the issuance of the Public Improvement Bonds and the 2001 Refunding Bonds and the refunding of the Public Improvement Bonds of 1994 and 1997, Series B being refunded (since the debt service on said Refunded Bonds is treated as no longer outstanding because the moneys in the 1994 and 1997B Escrow Fund will be invested in United States Treasury obligations, as described above in *Plan of Financing*), maximum annual debt service for the Commonwealth's outstanding general obligation debt is $555,614,237 for the fiscal year ending June 30, 2003. Debt service for the PRASA Guaranteed Bonds paid by the Commonwealth during fiscal 2000 (including for this purpose debt service payments due July 1, 2000) was $33,198,372.50. The sum of these two amounts is equal to 9.053% of the average of the adjusted internal revenues for the two fiscal years ended June 30, 2000. See, "Debt Service Requirements for Commonwealth General Obligation Bonds and Certain Commonwealth Guaranteed Debt" under *Public Sector Debt of the Commonwealth*, below. If, the debt service on the refunded Public Improvement Bonds of 1993 and 2000 is treated as no longer outstanding (notwithstanding that the proceeds of a portion of the 2001 Refunding Bonds will be invested in two guaranteed investment contracts as described in *Plan of Financing* above, rather than in United States Treasury obligations), then the percentage referred to above would be 8.937%.

On April 4, 2002, upon the issuance of the 2002 Refunding Bonds and the refunding of the 2002 Refunded Bonds (assuming currently projected internal revenues for the year ending June 30, 2001, as set forth on page I-34 of *Appendix I* to this Official Statement), the percentage referred to in the third sentence of the preceding paragraph would be 9.181% (assuming no other general obligation bonds of the Commonwealth are issued or retired in the interim). This percentage would be 8.642% if the 2002 Refunded Bonds are treated as not outstanding (notwithstanding that the proceeds of the 2002 Refunding Bonds will be invested in two guaranteed investment contracts as described in *Plan of Financing* above, rather than in United States Treasury obligations).

Maturity Limitation

The Constitution provides that no bonds or notes of the Commonwealth shall mature later than 30 years from their date of issue, except bonds or notes for housing facilities, which shall mature in no more than 40 years from their date of issue.

BOND INSURANCE

Financial Security Assurance Inc.

Bond Insurance Policy. Concurrently with the issuance of the Public Improvement Bonds and the 2001 Refunding Bonds, FSA Insurance will issue the FSA Bond Insurance Policy. The FSA Bond Insurance Policy guarantees the scheduled payment of principal of and interest on the Public Improvement Bonds and the 2001 Refunding Bonds when due as set forth in the form of policy included as *Appendix III* to this Official Statement.

The FSA Bond Insurance Policy is not covered by any insurance security or guaranty fund established under New York, California, Connecticut or Florida insurance law.

Financial Security Assurance Inc. FSA Insurance is a New York domiciled insurance company and a wholly owned subsidiary of Financial Security Assurance Holdings Ltd. ("Holdings"). Holdings is an indirect subsidiary of Dexia, S.A., a publicly held Belgian corporation. Dexia, S.A., through its bank subsidiaries, is primarily engaged in the business of public finance in France, Belgium and other European countries. No shareholder of Holdings or FSA Insurance is liable for the obligations of FSA Insurance.

At March 31, 2001, FSA Insurance's total policyholders' surplus and contingency reserves were approximately $1,430,595,000 and its total unearned premium reserve was approximately $730,490,000 in accordance with statutory accounting principles. At March 31, 2001, FSA Insurance's total shareholders' equity was approximately $1,547,252,000 and its total net unearned premium reserve was approximately $600,774,000 in accordance with generally accepted accounting principles.

The financial statements included as exhibits to the annual and quarterly reports filed by Holdings with the Securities and Exchange Commission are incorporated herein by reference. Also incorporated herein by reference are any such financial statements so filed from the date of this Official Statement until the termination of the offering of the Bonds. Copies of materials incorporated by reference will be provided upon request to Financial Security Assurance Inc., 350 Park Avenue, New York, New York 10022, Attention: Communications Department (telephone: 212-826-0100).

The FSA Bond Insurance Policy does not protect investors against changes in market value of the Bonds which are insured thereby, which market value may be impaired as a result of changes in prevailing interest rates, changes in applicable ratings or other causes. FSA Insurance makes no representation regarding the Bonds insured by the FSA Bond Insurance Policy or the advisability of investing in such Bonds. FSA Insurance makes no representation regarding this Official Statement, nor has it participated in the preparation thereof, except that FSA Insurance has provided to the Commonwealth the information presented under this caption and its form of policy set forth in *Appendix III* for inclusion in this Official Statement.

Financial Guaranty Insurance Company

Bond Insurance Policy. Concurrently with the issuance of the 2002 Refunding Bonds, FGIC Insurance will issue its FGIC Bond Insurance Policy. The FGIC Bond Insurance Policy unconditionally guarantees the payment of that portion of the principal of and interest on the 2002 Insured Bonds which has become due for payment, but shall be unpaid by reason of nonpayment by the Commonwealth. FGIC Insurance will make such payments to State Street Bank and Trust Company, N.A., or its successor as its agent (the "Fiscal Agent"), on the later of the date on which such principal and interest is due or on the business day next following the day on which FGIC Insurance shall have received telephonic or telegraphic notice, subsequently confirmed in writing, or written notice by registered or certified mail, from an owner of 2002 Insured Bonds or the Registrar of the nonpayment of such amount by the Commonwealth. The Fiscal Agent will disburse such amount due on any 2002 Insured Bond to its owner upon receipt by the Fiscal Agent of evidence satisfactory to the Fiscal Agent of the owner's right to receive payment of the principal and interest due for payment and evidence, including any appropriate instruments of assignment, that all of such owner's rights to payment of such principal and interest shall be vested in FGIC Insurance. The term "nonpayment" in respect of a 2002 Insured Bond includes any payment of principal or interest made to an owner of a 2002 Insured Bond which has been recovered from such owner pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction.

The FGIC Bond Insurance Policy is non-cancellable, and the premium will be fully paid at the time of delivery of the 2002 Insured Bonds. The FGIC Bond Insurance Policy covers failure to pay principal of the 2002 Insured Bonds on their respective stated maturity dates or dates on which the same shall have been duly called for mandatory sinking fund redemption, and not on any other date on which the 2002 Insured Bonds may have been otherwise called for redemption, accelerated or advanced in maturity, and also covers the failure to pay any installment of interest on the stated date for its payment.

This Official Statement contains a section regarding the ratings assigned to the 2002 Insured Bonds and reference should be made to such section for a discussion of such ratings and the basis for their assignment to the 2002 Insured Bonds. See *Ratings*. The FGIC Bond Insurance Policy guarantees the scheduled payment of principal of and interest on the 2002 Insured Bonds when due as set forth in the form of the FGIC Bond Insurance Policy included as *Appendix IV* to this Official Statement.

The FGIC Bond Insurance Policy is not covered by the Property/Casualty Insurance Security Fund specified in Article 76 of the New York Insurance Law.

Financial Guaranty Insurance Company. FGIC Insurance is a wholly-owned subsidiary of FGIC Corporation (the "Corporation"), a Delaware holding company. The Corporation is a subsidiary of General Electric Capital Corporation ("GE Capital"). Neither the Corporation nor GE Capital is obligated to pay the debts of or the claims against FGIC Insurance. FGIC Insurance is a monoline financial guaranty insurer domiciled in the State of New York and subject to regulation by the State of New York Insurance Department. As of March 31, 2001, the total capital and surplus of FGIC Insurance was approximately $1.132 billion. FGIC Insurance prepares financial statements on the basis of both statutory accounting principles and generally accepted accounting principles. Copies of such financial statements may be obtained by writing to FGIC Insurance at 115 Broadway, New York, New York 10006, Attention: Communications Department (telephone number: 212-312-3000) or to the New York State Insurance Department at 25 Beaver Street, New York, New York 10004-2319, Attention: Financial Condition Property/Casualty Bureau (telephone number: 212-480-5187).

PUBLIC SECTOR DEBT OF THE COMMONWEALTH

Pro Forma Public Sector Debt

The following table presents a summary of the public sector debt of the Commonwealth as of December 31, 2000 and as adjusted for the issuance of the Bonds and the refunding of the Refunded Bonds. The table should be read in conjunction with the information set forth in *Debt* in *Appendix I.*

Commonwealth of Puerto Rico
Public Sector Debt*
(in thousands)

	December 31, 2000	As Adjusted by the Issuance of the 2001 Bonds**	As Adjusted by the Issuance of the 2002 Refunding Bonds***
Puerto Rico direct debt	$ 5,585,657	$ 6,173,687	$ 5,912,761
Municipal debt	1,446,345	1,446,345	1,446,345
Public corporations debt			
Puerto Rico guaranteed debt	603,343	603,343	603,343
Debt supported by Puerto Rico appropriations or taxes	11,321,577	11,321,577	11,321,577
Other non-guaranteed debt	6,786,513	6,786,513	6,786,513
Total public corporations debt	$ 18,711,433	$ 18,711,433	$ 18,711,433
Total public sector debt	$ 25,743,435	$ 26,331,465	$ 26,070,539

* For a complete recital of all notes to this table, see "Public Sector Debt" under *Debt* in *Appendix I.*

** And the refunding of the 2001 Refunded Bonds.

*** And the July 1, 2001 principal payment on all general obligation bonds and the refunding of the 2002 Refunded Bonds. The figures in this column are stated on the assumption that no additional debt of the type set forth in the table has occurred since December 31, 2000.

Source: Government Development Bank

Debt Service Requirements for Commonwealth General Obligation Bonds and Certain Commonwealth Guaranteed Debt

The following table presents debt service requirements for: (i) general obligation bonds of the Commonwealth outstanding on December 31, 2000, excluding the Refunded Bonds and the January 1, 2001 interest payment on all outstanding general obligation bonds; (ii) the Bonds and (iii) the PRASA Guaranteed Bonds, See "Commonwealth Guaranteed Debt" in *Appendix I.* With respect to other debt of Aqueduct and Sewer Authority, see *Public Corporations* in *Appendix I.* 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. The Commonwealth has on deposit in its Redemption Fund all amounts needed to pay debt service on July 1, 2001 on all outstanding general obligation bonds.

Commonwealth of Puerto Rico
Debt Service Requirements*
(in thousands)

Fiscal Year Ending June 30	Outstanding Bonds Total Debt Service(1)	Outstanding PRASA Bonds Debt Service	2001 Bonds		2002 Bonds		Grand Total(2)
			Principal	Interest	Principal	Interest	
2002	$ 470,530	$ 33,542	$ 0	$ 41,766	$ 0	$ 6,385	$ 552,223
2003	479,678	33,745	0	39,156	11,070	26,421	589,069
2004	442,984	30,125	0	39,156	13,045	25,867	551,178
2005	429,467	30,127	0	39,156	23,640	25,215	547,605
2006	396,464	30,121	0	39,156	32,815	24,033	522,589
2007	356,216	30,126	0	39,156	54,450	22,392	502,341
2008	298,528	30,131	0	39,156	53,105	19,670	440,589
2009	291,935	30,123	0	39,156	44,090	17,014	422,318
2010	292,526	29,984	0	39,156	45,885	14,700	422,251
2011	278,354	29,928	0	39,156	61,975	12,291	421,704
2012	271,329	30,127	0	39,156	65,370	8,882	414,864
2013	253,645	30,128	0	39,156	68,970	5,287	397,185
2014	253,685	30,125	24,910	39,156	27,150	1,493	376,519
2015	253,727	30,126	54,915	37,938	0	0	376,706
2016	253,765	30,121	57,750	34,994	0	0	376,629
2017	253,797	30,122	61,040	31,842	0	0	376,800
2018	273,518	30,126	44,540	28,523	0	0	376,706
2019	252,066	30,125	46,875	26,148	0	0	355,214
2020	252,092	0	50,540	23,586	0	0	326,218
2021	238,127	0	24,495	20,947	0	0	283,569
2022	216,083	0	25,725	19,717	0	0	261,525
2023	192,802	0	27,010	18,431	0	0	238,243
2024	169,297	0	28,380	17,063	0	0	214,740
2025	146,040	0	29,795	15,644	0	0	791,479
2026	112,141	0	40,880	14,080	0	0	167,101
2027	64,656	0	61,360	11,933	0	0	137,949
2028	31,028	0	64,580	8,712	0	0	104,319
2029	0	0	67,890	5,402	0	0	73,292
2030	0	0	37,520	1,923	0	0	39,443
	$7,224,479	$547,952	$748,205	$828,522	$501,565	$209,648	$10,060,370

* Totals may not add due to rounding.

(1) Debt service requirements on all general obligation bonds outstanding, excluding called and refunded debt service on the Refunded Bonds (excluding fiscal year 2001 debt service for which funds have already been set aside).

(2) Debt service requirements on all general obligation bonds outstanding, adjusted to include the PRASA bonds, the issuance of the Bonds and the refunding of the Refunded Bonds.

Source: Government Development Bank and Department of the Treasury

TAX MATTERS

2001 Bonds

The Internal Revenue Code of 1986, as amended (the "Code"), includes requirements regarding the use, expenditure and investment of bond proceeds and the timely payment of certain investment earnings to the Treasury of the United States, if required, which the Commonwealth must continue to meet after the issuance of the 2001 Bonds so that interest on the 2001 Bonds is not included in gross income for federal income tax purposes. The Commonwealth's failure to meet these requirements may cause interest on the 2001 Bonds to be included in gross income for federal income tax purposes, retroactive to their date of issuance. The Commonwealth has covenanted to comply, to the extent permitted by the Constitution of Puerto Rico 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 2001 Bonds. Bond Counsel is not aware of any provision of the Constitution or laws of the Commonwealth, which would prevent the Commonwealth from complying with the requirements of the Code.

In the opinion of Bond Counsel, subject to continuing compliance by the Commonwealth 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 2001 Bonds will not be includable in gross income for federal income tax purposes. Interest on the 2001 Bonds will not be an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations; however, interest on the 2001 Bonds will be includable in the computation of the alternative minimum tax on corporations imposed by the Code. No opinion is rendered by Bond Counsel as to the exclusion from gross income of the interest on the 2001 Bonds for federal income tax purposes on or after the date on which any action is taken under the Bond Resolution or any other instrument relating to the 2001 Bonds upon the approval of counsel, other than Bond Counsel. Bond Counsel is further of the opinion that the 2001 Bonds and the interest thereon are exempt from state, Commonwealth and local income taxation.

Ownership of tax-exempt obligations 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 tax-exempt obligations may also result in collateral income tax consequences under Puerto Rico law to financial institutions doing business in Puerto Rico.

Prospective purchasers of the 2001 Bonds should consult their tax advisors as to 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 2001 Bonds will not have an adverse effect on the tax-exempt status of the 2001 Bonds. Legislative or regulatory actions and proposals may also affect the economic value of tax exemption or the market price of the 2001 Bonds.

Discount Bonds

The excess, if any, of the amount payable at maturity of the 2001 Bonds over the initial public offering price to the public (excluding bond houses, brokers or similar persons acting in the capacity of underwriter or wholesalers), at which price a substantial amount of such maturity is sold, constitutes original issue discount. The amount of original issue discount accrues in accordance with a constant yield method based on the compounding of interest. Original issue discount accruing pursuant to the constant yield method described above will be excluded from gross income to the same extent as interest on the 2001 Bonds for federal income tax purposes. A portion of the original issue discount that accrues in each year to an owner of the 2001 Bonds with original issue discount (the "Discount Bonds") that is a corporation will be included in the calculation of the corporation's federal alternative minimum tax liability. In addition, original issue discount that accrues in each year to an owner of a Discount Bond is included in the calculation of the distribution requirements of certain regulated investment companies and may result in some of the collateral federal income tax consequences discussed herein. Consequently, owners of any Discount Bond should be aware that the accrual of original issue discount in each year may result in an alternative minimum tax liability, additional distribution requirements or other collateral federal income tax consequences, although the owner of such Discount Bond has not received cash attributable to such original issue discount in such year.

A purchaser in the initial offering who acquires a Discount Bond at an issue price equal to the initial offering price thereof, as set forth or derived from information set forth on the inside cover page, will be treated as receiving an amount of interest not includable in gross income for federal income tax purposes equal to the original issue discount accruing during the period he holds such Discount Bond, and will increase his adjusted basis in such Discount Bond by the amount of such accruing discount for purposes of determining taxable gain or loss on the redemption, sale or other disposition of such Discount Bond for federal income tax purposes. The accrual of original issue discount and its effect on redemption, sale or other disposition of Discount Bonds that are not purchased in the initial offering at the initial offering price may be determined according to rules that differ from those described above.

Owners of Discount Bonds should consult their tax advisors with respect to the determination for federal income tax purposes of the amount of original issue discount or interest properly accruable with respect to such Discount Bonds and with respect to state, Commonwealth and local tax consequences of owning and disposing of Discount Bonds.

Premium Bonds

The excess, if any, of the tax basis of a 2001 Bond to a purchaser (other than a purchaser who holds such 2001 Bond as inventory, stock in trade or for sale to customers in the ordinary course of business) who purchases such 2001 Bond as part of the initial offering and at the initial offering price over the amount payable at maturity of such 2001 Bond is "Bond Premium." Bond Premium is amortized over the term of such 2001 Bond for federal income tax purposes (or in the case of a bond with Bond Premium callable prior to its stated maturity, the amortization period and yield may be required to be determined on a basis of an earlier call date that results in the lowest yield on such bond). No deduction is allowed for such amortization of Bond Premium; however, Bond Premium is treated as an offset to qualified stated interest received on such 2001 Bond. Owners of such 2001 Bonds are required to decrease their adjusted basis in such 2001 Bonds by the amount of amortizable Bond Premium attributable to each taxable year such 2001 Bonds are held. Owners of such 2001 Bonds should consult their tax advisors with respect to the precise determination, for federal income tax purposes, of the treatment of Bond Premium upon redemption, sale or other disposition of such 2001 Bonds and with respect to the state, Commonwealth and local tax consequence of owning and disposing of such 2001 Bonds.

2002 Refunding Bonds

Assuming no change in existing law, it is expected that an opinion substantially similar to the opinion described above with respect to the 2001 Bonds, and subject to the same limitations as described above with respect to the 2001 Bonds, will be issued in connection with the issuance of the 2002

Refunding Bonds. See "Delayed Delivery of the 2002 Refunding Bonds" under *Plan of Financing* and "Form of Opinions of Bond Counsel" in *Appendix II*.

UNDERWRITING

The Underwriters have jointly and severally agreed, subject to certain conditions, to purchase the 2001 Bonds from the Commonwealth at an aggregate discount of $4,972,380.30 from the initial offering prices of such Bonds, set forth or derived from information set forth on the inside cover hereof. The Underwriters have jointly and severally agreed, subject to certain conditions, to purchase the 2002 Refunding Bonds from the Commonwealth at an aggregate discount of $3,057,144.50 from the initial public offering prices for such Bonds, set forth or derived from information set forth on the inside cover hereof. The obligations of the Underwriters are subject to certain conditions precedent, and they will be obligated to purchase all of the 2001 Bonds, if any 2001 Bonds are purchased. The obligation of the Underwriters to purchase the 2002 Refunding Bonds is subject to certain conditions precedent, and may be terminated, as described above in "Delayed Delivery of the 2002 Refunding Bonds" under *Plan of Financing*. The Underwriters will be obligated to purchase all 2002 Refunding Bonds if any such Bonds are purchased. The Underwriters may offer to sell the Bonds to certain dealers and others at prices lower than the initial public offering prices. The offering prices may be changed, from time to time, by the Underwriters.

Goldman, Sachs & Co. ("GS"), has entered into a written agreement with FirstBank Puerto Rico ("FirstBank"), a bank organized under the laws of the Commonwealth, pursuant to which FirstBank has agreed to act as a consultant to GS in connection with GS's provision of underwriting and investment banking services to the Commonwealth with respect to the Bonds. Pursuant to this agreement, the existence of which has been disclosed to the Commonwealth and Government Development Bank, FirstBank will be entitled to receive a portion of GS's actual net profits, if any, in connection with the underwriting of the Bonds. Other agreements have been entered into and disclosed to the Commonwealth and Government Development Bank by Merrill Lynch & Co. and Santander Securities Corporation, J.P. Morgan & Co. and Alianza Capital (Puerto Rico), Inc., and Morgan Stanley & Co. Incorporated and Popular Securities Inc.

LEGAL MATTERS

The proposed form of opinions of Sidley Austin Brown & Wood LLP, Bond Counsel, is set forth in *Appendix II* to this Official Statement. Certain legal matters will be passed upon for the Underwriters by Fiddler González & Rodríguez, LLP, San Juan, Puerto Rico.

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.

VERIFICATION OF MATHEMATICAL COMPUTATIONS

Samuel Klein and Company will verify, from the information provided to them, the mathematical accuracy as of the date of the closing of the Bonds of (1) the computations contained in the provided schedules to determine that the anticipated receipts from the securities and cash deposits listed in such schedules, to be held in escrow, will be sufficient to pay, when due, the principal, interest (after July 1, 2001, except for the 2002 Refunded Bonds) and call premium payment requirements, if any, of the Refunded Bonds (see *Plan of Financing*), and (2) the computations of yield on both the securities and the Bonds contained in such schedules used by Bond Counsel in its determination that interest on the Bonds is excludable from gross income for federal income tax purposes. Samuel Klein and Company will express no opinion on the assumptions provided to them, nor as to the exclusion from gross income for federal income tax purposes of the interest on the Bonds.

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO

As required by Act No. 272 of the Legislature of Puerto Rico, approved May 15, 1945, as amended, Government Development Bank has acted as financial advisor to the Commonwealth in connection with the Bonds. As a 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, its instrumentalities and public corporations. Certain of the Underwriters or their affiliates participate in other financial transactions with Government Development Bank.

RATINGS

Moody's Investors Service ("Moody's") and Standard & Poor's are expected to give the Bonds ratings of Baa1 and A, respectively. These ratings do not reflect the FSA Bond Insurance Policy and the FGIC Bond Insurance Policy. Moody's and Standard & Poor's are expected to give the Public Improvement Bonds, the 2001 Refunding Bonds and the 2002 Insured Bonds ratings of Aaa and AAA, respectively, based on the issuance of the Policies. Ratings reflect only the respective views of the rating agencies and an explanation of the significance of each rating may be obtained only from the respective rating agency.

Such rating agencies were provided with materials relating to the Commonwealth 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.

There is no assurance that such ratings will remain in effect for any given period of time or that they will not be revised downward or withdrawn entirely by either or both of such rating agencies, if in the judgment of either or both, circumstances so warrant. Any such downward revision or withdrawal of such ratings, or either of them, may have an adverse effect on the market prices of the Bonds.

CONTINUING DISCLOSURE

In accordance with the requirements of Rule 15c-12, as amended (the "Rule"), promulgated by the Securities and Exchange Commission (the "SEC"), the Commonwealth has covenanted in the Bond Resolution for the benefit of the Beneficial Owners (as defined in such Bond Resolution and generally the tax owners of the Bonds):

1. to file within 305 days after the end of each fiscal year, commencing with the fiscal year ending June 30, 2001, with each NRMSIR and with any Commonwealth state information depository ("SID"), core financial information and operating data for the prior fiscal year, including (i) the Commonwealth's 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) on the Commonwealth and its revenues, expenditures, financial operations and indebtedness, generally found in this Official Statement; and

2. to file, in a timely manner, with each NRMSIR or with the MSRB, and with any Commonwealth SID, notice of any failure of the Commonwealth to comply with paragraph 1 above, and of the occurrence of any of the following events with respect to the Bonds, if material:

a. principal and interest payment delinquencies;
b. non-payment related defaults;
c. non-scheduled draws on debt service reserves reflecting financial difficulties;
d. unscheduled draws on credit enhancements reflecting financial difficulties;
e. substitution of credit or liquidity providers, or their failure to perform;
f. adverse opinions or events affecting the tax-exempt status of the Bonds;
g. modifications to rights of the holders (including Beneficial Owners) of the Bonds;
h. Bond calls;
i. defeasances;
j. release, substitution, or sale of property securing repayment of the Bonds; and
k. rating charges.

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". For a description of the Bonds, see *The Bonds*. In addition, with respect to the following events:

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

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

Event (h). The Commonwealth 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 the terms, dates and amounts of redemption are set in detail in this Official Statement under "*The Bonds – Redemption*", the only open issue is which Bonds will be redeemed in the case of partial redemption and notice of 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.

The Commonwealth expects to provide the information described in paragraph 1(ii) above by filing its first bond official statement that includes such information for the preceding fiscal year or, if no such official statement is issued by the 305-day deadline, by filing the Commonwealth Report.

As of May 1, 2001, there was no Commonwealth SID, and the name and address of each NRMSIR is: Bloomberg Municipal Repositories, P.O. Box 840, Princeton, New Jersey 08542; Standard & Poor's J.J. Kenny Repository, 55 Water Street, 45th Floor, New York, New York 10041; Interactive Data, 100 William Street, New York, New York 10038, Attn: Repository; and DPC Data Inc., One Executive Drive, Fort Lee, New Jersey 07024.

The Commonwealth 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 Commonwealth, such other events are material with respect to the Bonds, but the Commonwealth does not undertake to provide notice of the occurrence of any material event except those events listed above.

The Commonwealth acknowledges that its undertaking pursuant to the Rule described above is intended to be for the benefit of the Beneficial Owners of the Bonds, and shall be enforceable by any such Beneficial Owners; provided, that the right to enforce the provisions of its undertaking shall be limited to a right to obtain specific enforcement of the Commonwealth's obligations hereunder.

No 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 Beneficial Owner shall have filed with the Commonwealth written notice of any request to cure such breach, and the Commonwealth 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, Puerto Rico for the equal benefit of all 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. Moreover, Proceedings filed by Beneficial Owners against the Commonwealth may be subject to the sovereign immunity provisions of Section 2 of Act No. 104, approved June 29, 1955, as amended (32 L.P.R.A. §3077 and §3077a), which governs the scope of legal actions against the Commonwealth, substantially limits the amount of monetary damages that may be awarded against the Commonwealth and provides certain notice provisions which, if not complied with, may further limit any recovery.

The Covenants may only be amended if:

(1) 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 Commonwealth, or type of business conducted; 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 interest of Beneficial Owners, as determined by persons unaffiliated with the Commonwealth; or

(2) all or any part of the Rule, as interpreted by the staff of the SEC at the date of the adoption of such Rule, ceases to be in effect for any reason, and the Commonwealth elects that the Covenants shall be deemed amended accordingly.

The Commonwealth has further 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.

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

MISCELLANEOUS

The foregoing summaries of or references to the Act, the Bonds, the Bond Resolution, the Policies and the summaries of or references to the various acts contained in the Commonwealth Report, are made subject to all the detailed provisions thereof to which reference is hereby made for further information and do not purport to be complete statements of any or all of such provisions.

Appended to and constituting a part of this Official Statement is the Commonwealth Report *(Appendix I)*, the proposed form of opinions of Bond Counsel *(Appendix II)*, a specimen insurance policy of FSA Insurance *(Appendix III)* and a specimen insurance policy of FGIC Insurance *(Appendix IV)*.

The information set forth in this Official Statement and incorporated herein by reference, except for information pertaining to DTC, FSA Insurance, FGIC Insurance and the information appearing in *Underwriting*, was supplied by certain officials of the Commonwealth or certain of its agencies or instrumentalities, in their respective official capacities, or was obtained from publications of the Commonwealth or certain of its agencies or instrumentalities, and is included or incorporated by reference in this Official Statement on the authority of such officials or the authority of such publications as public official documents. The information pertaining to DTC was supplied by DTC. The information set forth under *Underwriting* was supplied by the Underwriters, and the information under *Bond Insurance* and *Appendices III* and *IV* was provided by FSA Insurance in respect of FSA Insurance and the FSA Bond Insurance Policy and by FGIC Insurance in respect of FGIC Insurance and FGIC Bond Insurance Policy.

The Official Statement will be filed with each NRMSIR and with the MSRB.

COMMONWEALTH OF PUERTO RICO

By: /s/ Juan A. Flores
Secretary of the Treasury

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APPENDIX I

COMMONWEALTH OF PUERTO RICO

Financial Information and Operating Data Report
April 30, 2001

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COMMONWEALTH OF PUERTO RICO

Financial Information and Operating Data Report
April 30, 2001

INTRODUCTION

Geographic Location and Demography

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 3,808,610 in 2000, compared to 3,522,000 in 1990. As of 1999, the population of San Juan, the island's capital and largest city, was approximately 439,004.

Relationship with the United States

Puerto Rico was discovered by Columbus in 1493, and shortly thereafter the island was conquered and settled by the Spaniards. It remained a Spanish possession for four centuries.

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 for Puerto Rico, the Congress of the United States enacted Public Law 600, which is "in the nature of a compact" and which became effective upon its acceptance by the electorate of Puerto Rico. It provides that those sections of existing law, which defined the political, economic and fiscal relationship between Puerto Rico and the United States, should remain in full force. It also authorized the people of Puerto Rico to draft and adopt their own Constitution. The Constitution was drafted by a popularly elected constitutional convention, overwhelmingly approved in a special referendum by the people of Puerto Rico and approved by the United States Congress and the President of the United States, becoming effective upon proclamation of the Governor of Puerto Rico on July 25, 1952. Puerto Rico's relationship with the United States is referred to herein as commonwealth status.

The United States and the Commonwealth of Puerto Rico (the "Commonwealth") share a common defense, market and currency. The Commonwealth exercises virtually the same control over its internal affairs, as do the fifty 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 who has a voice in the House of Representatives but no vote. Most federal taxes, except those such as Social Security taxes which are imposed by mutual consent, 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. Federal excise taxes on shipments of alcoholic beverages from Puerto Rico and other rum producing countries (which are at $13.25 per gallon from October 1, 1999 until December 31, 2001, and thereafter at $10.50 per gallon) and other taxes on shipments of tobacco products from Puerto Rico to the mainland are returned to the Treasury Department of Puerto Rico. See "Major Sources of General Fund Revenues" under *Puerto Rico Taxes, Other Revenues and Expenditures* for a discussion of current federal legislative proposals relating to federal excise taxes on shipments of alcoholic beverages.

The official languages of Puerto Rico are Spanish and English.

Governmental Structure

The Constitution of the Commonwealth provides for the separation of powers of the executive, legislative, and judicial branches of government. The Governor is elected every four years. The Legislature 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. 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 Puerto Rico 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.

Sila M. Calderón was sworn in as Governor of Puerto Rico on January 2, 2001. She obtained a Bachelor's degree in Political Science from Manhattanville College in New York and attended the Graduate School of Public Administration of the University of Puerto Rico. Since 1973, she has worked in the public sector as Executive Assistant of the Labor Secretary, Special Assistant to the Governor of Puerto Rico, Chief of Staff of the Governor of Puerto Rico, and Secretary of State. In the private sector, she has worked as an Executive in charge of Business Development for Citibank, N.A., President of the Commonwealth Investment Company Inc., and a member of the board of directors of BanPonce, Banco Popular de Puerto Rico and Pueblo International, Inc. In 1996, she was elected as Mayor of the municipality of San Juan.

Juan A. Flores, Secretary of the Treasury, took office on January 2, 2001. He is a certified public accountant and a graduate of the University of Puerto Rico, Mayagüez Campus, where he obtained a Bachelor's degree in Business Administration. Prior to his appointment to the Department of the Treasury, he worked in a manufacturing company and as an auditor for a large accounting firm.

Melba Acosta, Director of the Office of Management and Budget ("OMB"), took office on January 3, 2001. She is a graduate of the University of Puerto Rico, where she obtained a Bachelor's degree in Business Administration, in Accounting, and a Juris Doctor degree. In 1992, she received her Master's degree in Business Administration, Finance and General Management from the Harvard Graduate School of Business. She is a certified public accountant and has six years of experience as a tax consultant and corporate attorney in the private sector. Prior to her appointment as head of the OMB, she served for four years in the public sector.

Juan Agosto Alicea, President of Government Development Bank for Puerto Rico ("Government Development Bank" or "GDB"), took office on January 2, 2001. He obtained a Bachelor's degree in Accounting from the University of Puerto Rico and is licensed as a certified public accountant since 1966. He has worked as an auditor for Arthur Andersen & Co., the Puerto Rico Industrial Development Company, Peat Marwick & Mitchell, and the Federal Department of Housing and Urban Development. From 1985 to 1988 he served as Secretary of the Treasury, and as such was chairman of the board of directors of Government Development Bank for Puerto Rico. From 1995 to 1996 he was Administrator of the Municipality of San Juan. He is a former president of the Puerto Rico College of CPA's and the Board of Directors of United Way of Puerto Rico.

Political Trends

For many years there have been two major views in Puerto Rico with respect to the island's relationship with the United States: one favoring the commonwealth status, represented by the Popular Democratic Party, and the other favoring statehood, represented by the New Progressive Party. The following table shows the percentages of the total vote received by the gubernatorial candidates of the various parties in the last five elections by voter preference with respect to commonwealth status, statehood, and independence. While the electoral choices of Puerto Rico's voters are not based solely on preferences regarding the island'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.

	1984	1988	1992	1996	2000
Popular Democratic Party	48.5%	48.7%	45.9%	44.5%	48.6%
New Progressive Party	45.5	45.8	49.9	51.1	45.7
Puerto Rico Independence Party	3.9	5.4	4.2	3.8	5.2
Others	2.1	0.1	-	0.6	0.5

With the results of the 2000 election, control of the executive and legislative branches is now under the Popular Democratic Party. The composition of the Senate and House by the several political parties is as follows:

	Senate	House
Popular Democratic Party	19	30
New Progressive Party	8	20
Puerto Rico Independence Party	1	1
	28	51

The next general election (gubernatorial, municipal, and legislative) in Puerto Rico will be held in November 2004. Voter participation in Puerto Rico is substantially higher than in the United States, averaging 83% since 1972.

THE ECONOMY

General

The Commonwealth has established policies and programs directed at developing the manufacturing and service sectors of the economy and expanding and modernizing the island's infrastructure. Domestic and foreign investment has been stimulated by selective tax exemption, 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 island's population.

The economy of Puerto Rico is fully integrated with that of the United States mainland. During fiscal 2000, approximately 88% of Puerto Rico's exports went to the United States mainland, which was also the source of approximately 56% of Puerto Rico's imports. In fiscal 2000, Puerto Rico experienced an $11.4 billion positive merchandise trade balance.

The dominant sectors of the Puerto Rico economy are manufacturing and services. The manufacturing sector has experienced a basic change over the years as a result of increased emphasis on higher wage, high technology industries, such as pharmaceuticals, electronics, computers, microprocessors, professional and scientific instruments, and certain high technology machinery and equipment. The services sector, including finance, insurance, real estate, wholesale and retail trade, and hotel and related services, also plays a major role in the economy. It ranks second only to manufacturing in contribution to the gross domestic product and leads all sectors in providing employment.

The expansion in the construction sector continued in fiscal year 2000. The growth in this sector is illustrated by a significant growth of 52.1% in the total value of permits. Although, compared to other sectors, it represents a relatively small segment of the economy, it has made significant contributions to the growth of economic activity on the Island. The strength of public investment has been an important component in the significant expansion of construction investment since 1995. In fiscal year 1999, private investment in construction received an extraordinary boost from FEMA and insurance funds in order to compensate for damages caused by Hurricane Georges. Traditionally, housing investment has been the principal segment of private construction activity.

Fiscal 1996 to 2000

Puerto Rico's almost two decades-long economic expansion continued throughout the five-year period from fiscal 1996 through fiscal 2000. Almost every sector of the economy participated, and record levels of employment were achieved. Factors behind this expansion included government-sponsored economic development programs, periodic declines in the exchange value of the United States dollar, increases in the level of federal transfers, the relatively low cost of borrowing and, until recently, low oil prices.

Gross product in fiscal 1996 was $30.4 billion and gross product in fiscal 2000 was $41.4 billion ($34.8 billion in 1996 prices). This represents an increase in gross product of 36.3% from fiscal 1996 to 2000 (14.7% in 1996 prices).

Since fiscal 1985, personal income, both aggregate and per capita, has increased consistently each fiscal year. In fiscal 2000, aggregate personal income was $38.2 billion ($34.6 billion in 1996 prices) and personal income per capita was $9,870 ($8,925 in 1996 prices). The difference in the statistics of 1996 prices for gross product and personal income is attributable to the different price deflators used for each.

Personal income includes transfer payments to individuals in Puerto Rico under various social programs. Total federal payments to Puerto Rico, which payments include transfers to local government entities and expenditures of federal agencies in Puerto Rico, in addition to federal transfer payments to individuals, are lower on a per capita basis in Puerto Rico than in any state. Transfer payments to individuals in fiscal 2000 were $7.6 billion, of which $5.7 billion, or 75.1%, represented entitlements to individuals who had previously performed services or made contributions under programs such as Social Security, Veterans' Benefits, Medicare and U.S. Civil Service retirement pensions.

According to the Labor Department's Household Employment Survey, average employment increased from 1,092,200 in fiscal 1996 to 1,159,470 in fiscal 2000. Average unemployment decreased from 13.8% in fiscal 1996 to 11.0% in fiscal 2000.

The following table shows the gross product for the five fiscal years ended June 30, 2000.

Commonwealth of Puerto Rico

Gross Product

	Fiscal Year Ended June 30				
	1996	**1997**	**1998**	**1999**	**2000(p)**
Gross product - $ millions	$ 30,357	$ 32,343	$ 35,161	$ 38,297	$ 41,366
Real gross product - $ millions (1996 prices)	30,357	31,390	32,401	33,750	34,812
Annual percentage increase in real gross product (1996 prices)	3.3%	3.4%	3.2%	4.2%	3.1%
U.S. annual percentage increase in real gross product (1996 prices)	2.8%	4.0%	4.4%	3.9%	5.2%

(p) Preliminary.

Sources: Planning Board and Data Resources Inc.

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. In contrast with the BEA, which computes the economic accounts on a quarterly basis, the Planning Board computes the economic accounts on an annual basis. Like the BEA, the Planning Board revises the macroeconomic numbers on a regular basis. The Planning Board has always classified the latest annual numbers as preliminary until they are revised and made final in conjunction with the release of new data each year. At present, all macroeconomic accounts for fiscal 2000 are preliminary until the revised figures are released.

Fiscal 2001

According to the Labor Department's Household Employment Survey, during the first nine months of fiscal 2001, total employment increased 1.0% over the same period in fiscal 2000. Total monthly employment averaged 1,160,200 during the first nine months of fiscal 2001, compared to 1,149,700 in the same period of fiscal 2000.

The Planning Board's gross product forecast for fiscal 2001, made in March 2001, projected an increase of 2.2% over fiscal 2000, and an increase of 2.0% for fiscal 2002. The performance of the economy during fiscal 2001 will be affected principally by the performance of the United States economy and by the level of oil prices and the level of interest rates. The change in the Federal Reserve monetary policy to lower interest rates embodies a positive impact for the Commonwealth's economy, primarily its construction industry. Since Puerto Rico is heavily dependent on oil imports for its energy needs, if oil prices remain at their current high level for a long period of time, that could have an adverse effect on the level of economic activity in Puerto Rico.

Economic Development Program

The Commonwealth's economic development program is based on the fundamental, interrelated changes in technology, demographics and institutions, which are transforming the global economy. These changes provide the challenges and opportunities that encompass the economic development strategy.

The Commonwealth's goal is to target basic, export industries that can make the maximum net contribution to the Commonwealth's growth and competitiveness in the globalizing economy. Although the global share of the manufacturing sector of the GDP is in decline, this is largely due to the higher rate of productivity growth in this sector. Manufacturing remains by far the largest source of growth in international trade in goods and services and is also the source of demand for the growing business service sector. Service sector growth is also a primary source of demand for certain manufactured capital goods.

Puerto Rico is experiencing the effects of a demographic transition in which the working age population growth is declining and is expected to continue to decline resulting in a reduction of the net number of new entrants into the working age population. Although the Commonwealth still has large job creation needs due to high unemployment and the low percentage of the working age population that is part of the labor force, the government believes that the declining growth rate for the working age population will allow the Commonwealth to invest more resources improving the quality of education and infrastructure.

The Commonwealth intends to exploit this demographic transition to move up-market into more productive employment. The island can leverage its position as a surplus labor region in the U.S. market, while positioning itself as a bi-lingual, bi-cultural interface for the Americas.

The economic program is based on: 1) Jump-starting the manufacturing sector, 2) Regionalizing (decentralizing) economic development planning and implementation and 3) "Operación Manos Tecnológicas" to enable industries to acquire and develop more advanced technologies.

Initiatives to achieve the economic program objectives have begun in the following five areas: 1) Puerto Rico legislation, 2) institutional development, 3) new promotional strategies, 4) refocused strategic projects and 5) federal legislative proposals.

Puerto Rico Legislation. Legislative initiatives include laws introduced or under development to extend the benefits of the 1998 Tax Incentives Act to all eligible businesses operating under previous tax incentives laws. These benefits include 200% deductions for research and development expenses, worker training and the ability to deduct as a current expense investments in machinery and equipment. Other legislative proposals include legislation to reduce the capital gains tax from 20% to 10% for eligible government investments, a revision of real estate investment trust ("REIT") legislation and additional tax incentives to promote initial public offerings ("IPOs") of local companies.

Institutional Development. The Puerto Rico Industrial Development Company ("PRIDCO") has been reorganized into five major departmental areas and three offices, which report directly to the Executive Director. All promotional offices (Continental, Foreign, Puerto Rico, and Industrial Services) are consolidated in a single area, and the Office of Science and Technology has been integrated into this same area. A Strategic Planning function has been added to the Economic Analysis Area.

The Export Promotion Company ("PROMOEXPORT") has been integrated into the Commercial Development Administration in order to insure that overall programs for small business development are complementary to export assistance for those firms.

The Tourism Company is also undergoing reorganization, as are the Commonwealth offices that gather Puerto Rico's economic statistics.

An extensive program for the revitalization of urban centers is being implemented to help meet economic goals of job creation, efficiency and equity for low-income families. Bringing jobs to urban areas that already have infrastructure for utilities saves on public sector investment requirements, and reduces transportation time and costs for workers and businesses. Revitalized urban centers enhance the quality of life for residents and for all consumers of urban culture and commerce. This program will include the creation of micro-enterprise incubators, and a targeting of wage incentives under the "Valempleo" program to focus on urban revitalization projects.

New Promotional Strategies. Promotional strategies for economic development will build on Puerto Rico's competitive strengths provided by the Commonwealth's fiscal autonomy, which allows it to grant tax and financial incentives. The primary focus will be on competitive manufacturing clusters in pharmaceutical manufacturing, medical instruments and electronics and information technologies products. One objective is to expand the base of suppliers of intermediate products and professional services available to these clusters. Another goal is to use technology development resources to expand the capabilities of competitive cluster manufacturers in new product development and start-up enterprises. The Commonwealth is positioned to be a center of manufacturing and services at the crossroads of the Americas.

Refocused Strategic Projects. Strategic projects include a transshipment port complex targeted for the South coast to be known as the "Port of the Americas" and the Golden Triangle tourism/convention center/world trade complex in San Juan.

Federal Legislative Proposals. The Commonwealth has developed a proposal calling for an amendment to the U.S. Internal Revenue Code of 1986 to provide a new and permanent tax regime applicable to U.S.-based businesses that have operations in the Commonwealth or other U.S. possessions. This new regime will be based on the tax rules generally applied by Congress to U.S. corporations with international operations, but with certain modifications intended to promote employment both in the Commonwealth and the United States.

Employment and Unemployment

The number of persons employed in Puerto Rico during fiscal 2000 averaged 1,159,470. Unemployment, although at relatively low historical levels, remains above the average for the United States. Average unemployment decreased from 16.6% in fiscal 1993 to 11% in fiscal 2000, the lowest since 1970, and has continued to decline into fiscal 2001. In the first nine months of fiscal year 2001 (July through March 2001) total employment increased 1.0% over the same period in fiscal 2000. The moderate increase in employment in the last few years, along with a drop in the participation rate, resulted in a decline in the unemployment rate to the lowest levels in more that two decades.

The following table presents annual statistics of employment and unemployment for fiscal 1996 through fiscal 2000, and monthly statistics for July 2000 through March 2001.

Commonwealth of Puerto Rico

Employment and Unemployment (1)

Fiscal Years Ended June 30	Labor Force(1)	Employed(1)	Unemployed(1)	Unemployment Rate(2)
		(Annual Average)		
1996	1,268	1,092	175	13.8%
1997	1,298	1,128	170	13.1
1998	1,317	1,137	179	13.6
1999	1,310	1,147	163	12.5
2000	1,303	1,159	143	11.0
Fiscal 2001		(Seasonally Adjusted)		
July	1,317	1,187	130	9.9%
August	1,315	1,173	142	10.8
September	1,300	1,176	123	9.5
October	1,284	1,155	129	10.0
November	1,281	1,162	119	9.3
December	1,287	1,152	135	10.5
January	1,284	1,156	129	10.0
February	1,292	1,145	147	11.4
March	1,271	1,136	135	10.6

(1) Thousands of persons 16 years of age and over. Totals may not add due to rounding.
(2) Unemployed as percentage of labor force.

Source: Department of Labor and Human Resources - Household Survey

Economic Performance by Sector

Puerto Rico has a diversified economy. During the period between fiscal 1996 and 2000, the manufacturing and services sectors generated the largest portion of gross domestic product. Three sectors of the economy provide the most employment: manufacturing, services and government.

The following table presents annual statistics of gross domestic product by sector and gross product for the five fiscal years ended June 30, 2000.

Commonwealth of Puerto Rico

Gross Domestic Product by Sector and Gross Product
(in millions at current prices)

	Fiscal Year Ended June 30				
	1996	**1997**	**1998**	**1999**	**2000(p)**
Manufacturing	$18,467	$19,302	$22,976	$26,637	$27,442
Services(1)	17,470	18,955	20,723	22,333	24,036
Government(2)	4,841	5,220	5,251	5,526	5,478
Transportation, communication and public utilities	3,563	3,751	3,979	3,951	4,057
Agriculture, forestry and fisheries	376	466	437	336	450
Construction(3)	1,077	1,257	1,483	1,645	1,863
Statistical discrepancy	(452)	(765)	(714)	(388)	(176)
Total gross domestic product(4)	45,341	48,187	54,133	60,040	63,150
Less: net payment abroad	(14,984)	(15,844)	(18,973)	(21,742)	(21,783)
Total gross product(4)	$30,357	$32,343	$35,161	$38,298	$41,366

(p) Preliminary.
(1) Includes wholesale and retail trade, finance, insurance and real estate, and other services.
(2) Includes the Commonwealth, its municipalities and the federal government; excludes public corporations.
(3) Includes mining.
(4) Totals may not add due to rounding.

Source: Planning Board

The following table presents annual statistics of average employment by sector for the five fiscal years ended June 30, 2000.

Commonwealth of Puerto Rico

Average Employment by Sector
(thousands of persons age 16 and over)

	Fiscal Year Ended June 30				
	1996	**1997**	**1998**	**1999**	**2000**
Manufacturing	167	162	161	159	159
Services(1)	527	551	573	578	587
Government(2)	246	261	244	246	249
Transportation, communication and public utilities	61	59	59	59	55
Construction(3)	59	64	69	78	86
Agriculture, forestry and fisheries	32	31	31	27	24
Total(4)	1,092	1,128	1,137	1,147	1,159

(1) Includes wholesale and retail trade; finance, insurance and real estate; hotels and related services; and other services.
(2) Includes the Commonwealth of Puerto Rico, its municipalities and the federal government; excludes public corporations.
(3) Includes mining.
(4) Totals may not add due to rounding.

Source: Department of Labor and Human Resources - Household Survey

Manufacturing

Manufacturing is the largest sector of the Puerto Rico economy, in terms of gross domestic product. The Planning Board estimates that in fiscal 2000 manufacturing generated $27.4 billion, or 43.5% of gross domestic product. The manufacturing sector employed 140,555 workers as of March 2000 (as reported in the Department of Labor and Human Resources - Benchmark on Employment Hours and Earnings). Most of the island's manufacturing output is shipped to the United States mainland, which is also the principal source of semifinished manufactured articles on which further manufacturing operations are performed in Puerto Rico. The United States minimum wage laws are applicable in Puerto Rico. As of March 2001, the average hourly manufacturing wage rate in Puerto Rico was 65.5% of the average mainland United States rate.

Manufacturing in Puerto Rico is now more diversified than during the earlier phases of the industrial development program. In the last two 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 the heavy investment in the pharmaceuticals, scientific instruments, computers, microprocessors, medical products, and electrical products industries in Puerto Rico over the last decade.

The following table sets forth gross domestic product by manufacturing sector for the five fiscal years ended June 30, 2000.

Commonwealth of Puerto Rico

Gross Domestic Product by Manufacturing Sector
(in millions at current prices)

	Fiscal Year Ended June 30				
	1996	**1997**	**1998**	**1999**	**2000(p)**
Pharmaceuticals	$9,570	$10,354	$13,192	$15,569	$15,810
Machinery and metal products	4,021	4,055	4,583	5,677	6,273
Food products	2,167	2,086	2,052	1,908	1,783
Apparel	645	622	610	616	671
Other(1)	2,063	2,185	2,538	2,866	2,906
Total gross domestic product of manufacturing sector(2)	$18,467	$19,302	$22,976	$26,637	$27,442

(p) Preliminary.
(1) Includes petroleum products; petrochemicals and other chemical products; tobacco products; stone, clay and glass products; textiles and others.
(2) Totals may not add due to rounding.

Source: Planning Board

The following table sets forth manufacturing employment by industry group as of March 31 for the last five years.

Commonwealth of Puerto Rico

Manufacturing Employment by Industry Group
(persons age 16 years and over)

	As of March 31				
Industry Group	**1996**	**1997**	**1998**	**1999**	**2000**
Apparel and related products	23,918	21,750	19,039	18,349	16,770
Food and related products	20,343	19,949	17,816	16,852	15,182
Electrical machinery, equipment and supplies	23,464	24,671	22,728	20,254	19,394
Chemicals and related products (includes pharmaceuticals)	28,047	27,235	27,524	26,899	28,714
Professional and scientific instruments	15,131	14,914	15,105	14,542	14,818
Machinery, except electrical and transportation equipment	3,824	3,755	3,068	3,790	3,593
Petroleum refining and related industries; rubber and miscellaneous plastic products	5,268	5,768	5,994	5,970	6,197
Leather and leather products	6,636	6,566	5,834	4,749	3,982
Paper and related products; printing, publishing and related industries	7,184	7,441	8,698	9,418	9,536
Metal products	5,157	5,683	6,159	6,390	6,719
Stone, clay and glass products	4,825	4,972	5,217	5,509	5,929
Lumber and wood products; furniture and fixtures	3,183	3,352	3,538	3,446	3,343
Textile mill products	3,841	3,627	3,282	2,827	2,010
Tobacco products	989	1,206	1,285	1,297	1,254
Miscellaneous manufacturing industries	2,134	2,384	3,558	3,125	3,114
Total	153,944	153,273	148,845	143,417	140,555

Sources: Department of Labor and Human Resources, Census of Manufacturing, except for March 1999 and 2000, which information was derived from the "benchmark" on Employment, Hours and Earnings

While total employment in the manufacturing sector decreased by 12,718 from March 1997 to March 2000, other indicators of the manufacturing sector suggest that manufacturing production increased. Average weekly hours worked increased 6.0% from fiscal 1997 to fiscal 2000. The reduction in manufacturing employment occurred during a period of significant expansion in real manufacturing output, as reflected in the growth of exports. This trend suggests a significant increase in manufacturing productivity. Most of the decreases in employment have been concentrated in labor intensive industries, particularly apparel, textile and tuna manufacturing. When compared to the reduction of employment in the U.S. manufacturing sector, the sharper reduction in Puerto Rico is probably due to the island's larger share of employment in declining industries.

Leading United States and Foreign Companies with Manufacturing Operations in Puerto Rico

Employment 2,500 and over	Product
American Home Products	Pharmaceuticals
Baxter International	Pharmaceuticals
General Electric Co.	Electronic Instruments
Johnson and Johnson	Pharmaceuticals
Sara Lee Corp.	Apparel
Employment 1,500 to 2,499	
Abbott Laboratories, Inc.	Pharmaceuticals
Bristol-Myers Squibb	Pharmaceuticals
Eaton Corp.	Electronic Instruments
H. J. Heinz Co.	Food
Hewlett-Packard	Computers
Hubell Incorporated	Electrical Instruments
Intel Corporation	Electronics
Merck & Co.	Chemicals
Monsanto	Pharmaceuticals
Schering-Plough Corp.	Pharmaceuticals
Warner-Lambert Co.	Pharmaceuticals
Employment 1,000 to 1,499	
Atlantron Inc.	Communications
Bumble Bee Seafoods	Food
MacAndrews & Forbes Holdings	Tobacco Products
Ocular Science-American Hydron	Ophthalmic Products
Pfizer	Pharmaceuticals
Sensormatic Electronics	Electronic Components
U.S. Surgical Corp.	Scientific Instruments
Dexter Shoe	Footwear
Medtronics	Surgical and Medical Instruments
Employment 500 to 999	
Allergan	Pharmaceuticals
AMP Incorporated	Electronic Connectors
Aramark	Apparel
Aztra Zeneca Corp.	Pharmaceuticals
B. Braun Medical Systems	Medical Equipment
Becton-Dickinson & Co.	Scientific Instruments
Coleman Co.	Luggage
Conagra	Food
D.J. Manufacturing Corp.	Apparel
Dooney & Bourke	Leather
DuPont (E.I.) de Nemours	Chemicals
Eli Lilly and Co.	Pharmaceuticals
Essilor International	Ophthalmic Products

	Product
Guidant Corp.	Medical Instruments
Hamilton Sundstrand Corp.	Electronic Instruments
Ingersoll-Rand Co.	Electrical Instruments
Isla Verde Investment	Apparel
Nypro	Medical Devices
Pall Corp.	Filters
Pharmacia Up-John Co.	Pharmaceuticals
Procter & Gamble Co.	Pharmaceuticals
R.J.R. Nabisco	Food and Cigarettes
Seaboard Flour Corp.	Food
SmithKline Beecham	Pharmaceuticals
Storage Technology Corp.	Electronic
Stryker Corp.	Surgical and Medical Instruments
Suiza Foods	Food
Thomas & Betts	Electrical Instruments
Timberland Company (The)	Leather
Wesley Jessen Corp.	Ophthalmic Products
Employment 300 to 499	
Amgen Manufacturing Co.	Pharmaceuticals
Avon Products Inc.	Costume Jewelry
Block Drug Co.	Pharmaceuticals
Checkpoint Systems Inc.	Electronic
CocaCola Company (The)	Food
Colgate-Palmolive Co.	Consumers Products
E.A. Industries	Apparel
Eagle Work Clothes	Apparel
Emerson Electric	Electronic and Scientific Instruments
Esco Co.	Filters
Goya Foods	Food
ICN Pharmaceuticals Inc.	Pharmaceuticals
Insilco Corp.	Electronic Transformers
Kendall Healthcare Co.	Medical Instruments
Lawson Mardon Wheaton	Glass and Plastics
Loctite Corp.	Chemicals
Lutron Electronics Co.	Electronic
Millipore Corporation	Medical Devices
Owens Illinois	Glass and Plastics
PepsiCo	Food
Rhone-Poulenc	Pharmaceuticals
Siemens AG	Electrical Instruments
Unilever	Consumers & Medicals
Viasystems	Electronic

Source: PRIDCO, Office of Economic Research (as of February, 2001)

Services

Puerto Rico has experienced significant growth in the services sector (including finance, insurance, real estate, wholesale and retail trade, hotels and related services and other services) in terms of both income and employment over the past decade, showing a favorable trend as compared with certain other industrialized economies. During the period between fiscal 1996 and 2000, the gross domestic product in this sector increased at an annual average rate of 6.6%, while employment increased at an annual average rate of 2.2%. The development of the services sector has shown a strong interaction among the following important sectors: manufacturing, tourism, construction, and agriculture. The services sector in Puerto Rico has a diversified base.

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. A major element in the diversification effort is the further development of the local services sector, which has the capacity to increase its export potential and to generate more income and jobs during the coming years.

The services sector ranks second to manufacturing in its contribution to gross domestic product, and it is the sector with the greatest employment. In fiscal 2000, services generated $23.4 billion of gross domestic product, or 37.0% of the total. Service employment grew from 526,720 in fiscal 1996 to 587,438 in fiscal 2000, a cumulative increase of 11.5%, which increase was greater than the 6.2% cumulative growth in total employment over the same period. Wholesale and retail trade, finance, insurance and real estate have experienced significant growth in the fiscal 1996 to 2000 period, as measured by gross domestic product. Gross domestic product in wholesale and retail trade increased from $6.3 billion in fiscal 1996 to $8.4 billion in fiscal 2000. In finance, insurance and real estate, gross domestic product increased from $6.2 billion in fiscal 1996 to $8.9 billion in fiscal 2000. There are sixteen commercial banks and trust companies currently operating in Puerto Rico of which one is a U.S. major money center bank, two are foreign banks, one is a national bank from Florida, and thirteen are local banks and trust companies. Total assets of these institutions as of December 31, 2000 were $54.8 billion. In addition, five major securities firms operate on the island.

The following tables set forth gross domestic product and employment for the services sector for the five fiscal years ended June 30, 2000.

Commonwealth of Puerto Rico

Gross Domestic Product by Service Sector
(in millions at current prices)

	Fiscal Year Ended June 30				
	1996	**1997**	**1998**	**1999**	**2000(p)**
Wholesale and retail trade	$6,281	$ 6,724	$ 7,287	$ 7,896	$8,437
Finance, insurance and real estate	6,164	6,917	7,672	8,327	8,920
Other services	5,025	5,314	5,763	6,110	6,679
Total(1)	$17,470	$18,955	$20,723	$22,333	$24,036

(p) Preliminary.
(1) Totals may not add due to rounding.

Source: Planning Board

Commonwealth of Puerto Rico

Average Employment by Service Sector
(thousands of persons age 16 and over)

	Fiscal Year Ended June 30				
	1996	**1997**	**1998**	**1999**	**2000**
Wholesale and retail trade	218	228	236	229	239
Finance, insurance and real estate	39	38	40	43	42
Other services	270	285	297	306	307
Total(1)	527	551	573	578	587

(1) Includes hotels and related services.

Source: Department of Labor and Human Resources Household Survey.

Hotels and Related Services - Tourism

Total visitors' expenditures accounted for 3.8% of the island's gross domestic product in fiscal 2000, compared to 3.6% in fiscal 1999. Visitors' expenditures and the number of visitors to the island had grown consistently from 1985 to 1998, reaching $2.2 billion, and more than 4.6 million, respectively, in fiscal 1998. In fiscal 1999, however, the number of visitors to the island decreased to 4.2 million and visitors' expenditures decreased to $2.1 billion, a decrease of 4.2% compared to fiscal 1998, due in part to the effect of Hurricane Georges, which struck the island in September 1998. During fiscal 2000, the number of visitors to the Island increased to 4.6 million and visitors' expenditures increased $2.4 billion, an increase of 8.2% and 11.7%, respectively, compared to fiscal 1999. The number of persons registered in tourist hotels during fiscal 2000 increased 1.4% over the number registered for fiscal 1999. The average occupancy rate in tourist hotels during fiscal 2000 was 74.3% compared to 75.4% in fiscal 1999. The average number of rooms rented in tourist hotels increased 1.7% during fiscal 2000 compared with fiscal 1999. These increases are due in part to the increased marketing by the Commonwealth of Puerto Rico, the trends in the U.S. economy and increased hotel usage by Puerto Rico residents. Since fiscal 1992, a number of major hotels have undergone substantial renovation and more than 2,680 new rooms have been added with the opening of several major hotels. Various international hotel corporations have recently made substantial capital investments to develop additional tourist facilities. At June 30, 2000, the total number of hotel rooms was 11,928 with the completion and renovation of several new hotels.

During the first nine months of fiscal 2001 the number of persons registered in tourist hotels was 994,000, an increase of 7.8% over the number registered for the same period in fiscal 2000. The average occupancy rate in tourist hotels during this period was 68.0% compared to 73.4% in fiscal 2000. The average number of rooms rented in tourist hotels increased 1.1% during the first nine months of fiscal 2001 compared with the same period of fiscal 2000.

San Juan has become the largest homeport for cruise ships in the Caribbean and the second largest homeport for cruise ships in the world.

The following table presents data relating to visitors to Puerto Rico and tourist expenditures for the five fiscal years ended June 30, 2000.

Commonwealth of Puerto Rico

Tourism Data

	Number of Visitors				
Fiscal Year Ended June 30	**Tourist Hotels(1)**	**Cruise Ship**	**Other (2)**	**Total**	**Total Visitors' Expenditures (in millions)**
1996	828,251	1,045,104	2,236,805	4,110,160	$1,898.3
1997	906,706	1,107,913	2,335,068	4,349,687	2,046.3
1998	1,030,500	1,274,700	2,365,600	4,670,800	2,232.9
1999	1,042,000	1,197,200	1,982,100	4,221,300	2,138.5
2000(p)	1,050,100	1,224,600	2,291,300	4,566,000	2,387.9

(p) Preliminary.
(1) Includes visitors in guesthouses.
(2) Including visitors in homes of relatives, friends, and in hotel apartments.

Sources: Puerto Rico Tourism Company and the Planning Board

Government

The government sector of Puerto Rico plays an important role in the economy. In fiscal 2000, government accounted for $5.5 billion of Puerto Rico's gross domestic product, or 8.7% of the total. The government is also a significant employer, providing jobs for 249,213 workers, or 21.5% of total employment in fiscal 2000. Government sector employment does not include employment by public corporations, which employment is included in other sectors. These public corporations include significant employers such as the Electric Power Authority and the Aqueduct and Sewer Authority. The government's (including the central government, the public corporations and the municipalities) share of payroll employment, measured according to the payroll survey, has diminished from 34.9% in fiscal 1981, to 33.6% in fiscal 1990, and to 26.5% in fiscal 2000.

On February 25, 1998, legislation was enacted permitting the unionization of government employees (excluding municipal employees). Under this law, government employees are given collective bargaining rights subject to a number of limitations. Among those limitations are: employees are prohibited from striking; annual salary increases are limited; employees cannot be required to become union members and pay union dues; and collective bargaining negotiations cannot occur in an election year. Negotiations of non-economic conditions with government employees pursuant to this bill commenced in fiscal 2000, and negotiations of economic conditions commenced in fiscal 2001.

Transportation

Thirty-four (34) 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 on the island including Arecibo, Culebra, Fajardo, Guayama, Guayanilla, Mayagüez, Ponce, Vieques, and Yabucoa.

The Luis Muñoz Marín International Airport is currently served by twenty-six (26) United States and international airlines. At present, there is daily direct service between San Juan and New York, Chicago, Dallas, Los Angeles, Miami, Atlanta, Boston, and numerous other destinations within the United States. There is also regularly scheduled service between Puerto Rico and other Caribbean islands and major Latin American and European cities. American Airlines uses San Juan as a hub for its intra-Caribbean airline service. Several smaller airports serve intra-island traffic.

The island's major cities are connected by a modern highway system, which, as of December 31, 2000, totaled approximately 4,610 miles.

Construction

The construction industry has experienced substantial real growth since fiscal 1987. During the period from fiscal 1996 through fiscal 1999, construction investment increased 62%. In fiscal 2000, investment in construction rose to a record level of $7.0 billion, an increase of 7.3%, over the $6.6 billion in fiscal 1999. The strong growth in the construction industry resulted from increased public and private investment in the past few years. During fiscal year 2000, the total value of construction permits increased 52.1% and cement sales decreased 3.5% in comparison with fiscal 1999. In fiscal 2000, the average employment in the construction sector was 84,886, an increase of 9.2% over fiscal 1999. The Planning Board's construction investment forecast for fiscal 2001, made in March 2001, projected a nominal increase of 7.4% attributable primarily to the construction of large infrastructure projects, commercial projects and other investments.

During the first eight months of fiscal year 2001, the total value of construction permits increased 54.1% and total cement sales decreased 4.5% in comparison with the same period in fiscal 2000. The average employment in the construction sector during the first eight months of fiscal 2001 was 85,700, a decrease of 2.0% over the same period in fiscal 2000.

Agriculture

The Department of Agriculture and related agencies have directed their efforts at increasing and improving local agricultural production, increasing efficiency and quality of produce, and stimulating import substitution where economically feasible. During fiscal 2000, gross income from agriculture was $810.1 million, an increase of 13.5% in comparison with fiscal 1999. Agriculture gross income consists of the total value of production in the principal agricultural sectors, which include traditional crops, cattle products, farinaceous, vegetables, fruits, and other products. Recently, cattle products, non-traditional crops, and livestock products have contributed a higher percentage of the sector's income.

The Commonwealth of Puerto Rico 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, approved on December 1, 1995, increased the tax benefits available to bona fide farmers. The Act provides a 90% income tax exemption for income derived from agricultural operations, an investment tax credit equal to 50% of the investment 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 to be issued by financial institutions to provide financing to agricultural businesses. Subsequent legislation imposed an aggregate annual limitation of $15 million on the investment tax credits available under Act No. 225.

Since fiscal 1995, the Commonwealth has sold to private entities various agricultural operations previously conducted by governmental entities. These include certain assets of the pineapple processing operation and a mango growing facility. The Commonwealth has transferred to local private sugarcane growers the sugar processing facilities formerly operated by the Sugar Corporation.

Policy changes will be implemented to promote employment and income generated by the agricultural sector. The policy initiatives being considered are restructuring of the Department of Agriculture, an increase in government purchases of local agricultural products, and a new system of agricultural credits and subsidies for new projects.

Higher Education

During the four decades from 1950 to 1990, 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 services sector has increased significantly. This has resulted in an increased demand for workers having a higher level of education, in general, and, in particular, 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 proportion of college attendance by such population. Since the 1980s, college attendance has remained relatively stable as a percentage of the college-age population, generally following the trend in the United States.

The University of Puerto Rico, the only public university in Puerto Rico, includes eleven campuses located throughout the island. Total enrollment of the University was 69,749 students during academic year 1999-2000. The Commonwealth of Puerto Rico is legally bound to appropriate annually to the University an amount equal to 9.60% of the average annual revenue from internal sources for each of the two fiscal years immediately preceding the current fiscal year.

The following table presents comparative trend data for Puerto Rico and the United States with respect to college age population and percentage of such population attending institutions of higher learning.

Commonwealth of Puerto Rico

Trend in College Enrollment

	Commonwealth of Puerto Rico			Mainland United States		
Academic Year	Population 18-24 Years of Age[1]	Higher Education Enrollment[2]	Percent[3]	Population 18-24 Years of Age[1]	Higher Education Enrollment[2]	Percent[3]
1970	341,448	57,340	16.8%	23,714,000	8,580,887	36.2%
1980	397,839	130,105	32.7	30,022,000	12,096,895	40.3
1990	417,636	156,147	37.4	26,961,000	13,819,000	51.3
1997	478,028	173,608	36.3	24,979,000	14,345,000	57.4
1998	480,775	175,633	36.5	25,476,000	14,608,000	57.3
1999	483,028	175,449	36.3	26,011,000	14,881,000	57.2
2000(e)	470,660	174,550	37.1	26,748,000	15,072,000	56.3

(e) Estimated.
(1) 1970, 1980 and 1990 based on enumerated population as of April 1; other years based on estimated population as of July 1.
(2) For some small college level institutions, the data for 1998 and 1999 was estimated.
(3) Number of persons of all ages enrolled in institutions of higher education as percent of population 18–24 years of age.

Sources: United States Bureau of the Census (Mainland United States Population), United States National Center for Education Statistics, Planning Board (Puerto Rico Population) and Council on Higher Education of Puerto Rico

In addition to the University of Puerto Rico, there are thirty-seven (37) private institutions of higher education located in Puerto Rico. Such institutions have current enrollment in excess of 100,000 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.

Tax Incentives

One of the factors that promotes the development of the manufacturing sector in Puerto Rico has been the various local and federal tax incentives available, particularly those under Puerto Rico's Industrial Incentives Program and Sections 30A and 936 of the United States Internal Revenue Code of 1986, as amended (the "Code"). New tax and other incentives have 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 industrial incentives laws designed to stimulate industrial investment in the island. 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 industrial incentives laws is Act No. 135 of December 2, 1997 (the "1998 Tax Incentives Law"), a new industrial incentives law aimed at attracting and retaining foreign investment in Puerto Rico.

The benefits provided by the 1998 Tax Incentives Law are available to new companies as well as companies currently conducting tax exempt operations in Puerto Rico which choose to renegotiate their existing tax exemption grant. The activities eligible for tax exemption include manufacturing, certain designated services performed for markets outside Puerto Rico, the production of energy from local renewable sources for consumption in Puerto Rico and laboratories for scientific and industrial research. For companies qualifying thereunder, the 1998 Tax Incentives Law imposes income tax rates ranging from 2% to 7% for periods ranging from ten (10) to twenty-five (25) years. In addition, it grants 90% exemption from property taxes, 100% exemption from municipal license taxes during the first eighteen months of operation and between 80% and 60% thereafter, and 100% exemption from municipal excise taxes. The 1998 Tax Incentives Law also provides various special deductions designed to stimulate employment and productivity, research and development and capital investment in Puerto Rico.

Under the 1998 Tax Incentives Law, companies can repatriate or distribute their profits free of dividend taxes. In addition, passive income derived from the investment of eligible funds in Puerto Rico financial institutions, obligations of the Commonwealth of Puerto Rico and other designated investments are fully exempt from income and municipal license taxes. Individual shareholders of an exempted business are allowed a credit against their Puerto Rico income taxes equal to 30% of their proportionate share of the exempted business's income tax liability. Gain from the sale or exchange of shares of an exempted business by its shareholders during the exemption period is subject to a 4% income tax rate.

Tourism Incentives Program

For many years Puerto Rico has also had incentives laws designed to stimulate investment in hotel operations on the island. The most recent of these laws, the Tourism Incentives Act of 1993, provides exemptions from income, property, and municipal license taxes for a period of up to ten (10) years. In addition, it provides certain tax credits for qualifying investments in hotel development projects.

As part of the incentives to promote the tourism industry, the Commonwealth of Puerto Rico established the Tourism Development Fund as a subsidiary of GDB with the authority to make investments in or provide financing to entities that contribute to the development of the tourism industry. The Fund was initially capitalized with $50,000,000 and was authorized to provide financial guarantees for financing hotel development projects. To date the Fund has provided financial guarantees to private entities issuing bonds or borrowing funds to finance the development of thirteen (13) hotel projects that provided approximately 3,000 new hotel rooms.

Incentives under the Code

United States corporations operating in Puerto Rico have been subject to special tax provisions since the Revenue Act of 1921. Prior to the Tax Reform Act of 1976, Section 931 of the Code provided that United States corporations operating in Puerto Rico would be taxed only on income arising from sources within the United States and were entitled to exclude income from sources outside of the United States, if for the three-year period immediately preceding the end of the taxable year (i) 80% or more of the gross income of the corporation was derived from sources within Puerto Rico and (ii) 50% or more of their gross income was derived from the active conduct of a trade or business within Puerto Rico.

The Tax Reform Act of 1976 created Section 936 of the Code, which revised the tax treatment of United States corporations operating in Puerto Rico by taxing such corporations on their worldwide income in a manner similar to that applicable to any other United States corporation but providing such corporations a full credit for the federal tax on their business and qualified investment income in Puerto Rico. The credit provided an effective 100% federal tax exemption for operating and qualifying investment income from Puerto Rico sources. Amendments to Section 936 made in 1993 (the "1993 Amendments") instituted two alternative methods for calculating the tax credit and limited the amount of the credit that a qualifying company could claim. These limitations are based on a percentage of qualifying income (the "percentage of income limitation") and on qualifying expenditures on wages, other wage related benefits, and other qualifying expenditures (the "economic activity limitation," also known as the "wage credit limitation"). As a result of additional amendments made in 1996 (the "1996 Amendments"), as described below, the tax credit is now being phased out over a ten-year period for existing claimants and is no longer available for corporations that establish operations in Puerto Rico after October 13, 1995 (including existing Section 936 Corporations (as defined below), to the extent substantially new operations are established in Puerto Rico). The 1996 Amendments also moved the credit based on the economic activity limitation to Section 30A of the Code and phased it out over ten (10) years. In addition, the 1996 Amendments eliminated the credit previously available for income derived from certain qualified investments in Puerto Rico. The Section 30A Credit and the remaining Section 936 credit are discussed below.

Section 30A. The 1996 Amendments added Section 30A to the Code. Section 30A permits a "qualifying domestic corporation" ("QDC") that meets certain gross income tests (which are similar to the 80% and 75% gross income tests of Section 936 of the Code discussed below) to claim a credit (the "Section 30A Credit") against the federal income tax imposed on taxable income derived from sources outside the United States from the active conduct of a trade or business in Puerto Rico or from the sale of substantially all the assets used in such business ("possession income").

A QDC is a United States corporation which (i) was actively conducting a trade or business in Puerto Rico on October 13, 1995, (ii) had a Section 936 election in effect for its taxable year that included October 13, 1995, (iii) does not have in effect an election to use the percentage limitation of Section 936(a)(4)(B) of the Code, and (iv) does not add a "substantial new line of business."

The Section 30A Credit is limited to the sum of (i) 60% of qualified possession wages as defined in the Code, which includes wages up to 85% of the maximum earnings subject to the OASDI portion of Social Security taxes plus an allowance for fringe benefits of 15% of qualified possession wages, (ii) a specified percentage of depreciation deductions ranging between 15% and 65%, based on the class life of tangible property, and (iii) a portion of Puerto Rico income taxes paid by the QDC, up to a 9% effective tax rate (but only if the QDC does not elect the profit-split method for allocating income from intangible property).

A QDC electing Section 30A of the Code may compute the amount of its active business income eligible for the Section 30A Credit by using the cost sharing formula, the profit-split formula or the cost-plus formula, under the same rules and guidelines prescribed for such formulas as provided under Section 936 (see discussion below). To be eligible for the first two formulas, the QDC must have a significant presence in Puerto Rico.

In the case of taxable years beginning after December 31, 2001, the amount of possession income that would qualify for the Section 30A Credit would be subject to a cap based on the QDC's possession income for an average adjusted base period ending before October 14, 1995 (the "income cap").

Section 30A applies exclusively to taxable years beginning after December 31, 1995, and before January 1, 2006.

Section 936. Under Section 936 of the Code, as amended by the 1996 Amendments, United States corporations that meet certain requirements and elect its application ("Section 936 Corporations") are entitled to credit against their United States corporate income tax the portion of such tax attributable to income derived from the active conduct of a trade or business within Puerto Rico ("active business income") and from the sale or exchange of substantially all assets used in the active conduct of such trade or business. To qualify under Section 936 in any given taxable year, a corporation must derive for the three-year period immediately preceding the end of such taxable year (i) 80% or more of its gross income from sources within Puerto Rico, and (ii) 75% or more of its gross income from the active conduct of a trade or business in Puerto Rico.

Under Section 936, a Section 936 Corporation may elect to compute its active business income, eligible for the Section 936 credit, under one of three formulas: (i) a cost-sharing formula, whereby it is allowed to claim all profits attributable to manufacturing intangibles and other functions carried out in Puerto Rico provided it makes a cost sharing payment in the amount required under Section 936; (ii) a profit-split formula, whereby it is allowed to claim 50% of the combined net income of its affiliated group from the sale of products manufactured in Puerto Rico; or (iii) a cost-plus formula, whereby it is allowed to claim a reasonable profit on the manufacturing costs incurred in Puerto Rico. To be eligible for the first two formulas, the Section 936 Corporation must have a significant business presence in Puerto Rico for purposes of the Section 936 rules.

As a result of the 1993 Amendments and the 1996 Amendments, the Section 936 credit is only available to companies that were operating in Puerto Rico on October 13, 1995, and had elected the percentage of income limitation, and is limited in amount to 40% of the credit allowable prior to the 1993 Amendments, subject to a five-year phase-in period from 1994 to 1998 during which the percentage of the allowable credit is reduced from 60% to 40%.

In the case of taxable years beginning on or after 1998, the possession income subject to the 936 credit will be subject to a cap based on the Section 936 Corporation's possession income for an average adjusted base period ending on October 14, 1995. The 936 credit is eliminated for taxable years beginning in 2006.

Controlled Foreign Corporations

Because of the credit limitations and impending phase out of Sections 30A and 936, a large number of firms previously operating under the provisions of those sections have restructured their operations in Puerto Rico, in whole or in part, to become controlled foreign corporations ("CFCs"). The Puerto Rico Office of Tax Exemption has received notification of over sixty (60) corporations that have converted part or all of their operations under Puerto Rico tax incentives laws to CFCs. These include most of the major pharmaceutical, instrument and electronics companies manufacturing in Puerto Rico.

CFCs operate under transfer pricing rules for intangible income that are different from those corporations operating under Sections 936 and 30A. 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 companies were exempted from Puerto Rico withholding taxes on any cost sharing payments they might have opted to make, but CFCs are subject to a ten percent Puerto Rico withholding tax on royalty payments.

Because of the increase in net property income reported in manufacturing and rapidly rising withholding taxes on royalty payments, it is reasonable to believe that a significant share of the net income previously received by Section 936 corporations operating under the profit split method has been corporately restructured as CFCs.

Proposed New U.S. Tax Regime for Companies Doing Business in Puerto Rico

The Commonwealth is currently developing and implementing a comprehensive economic plan, which requires some actions to be taken in the U.S. Congress. Congress would need to enact legislation being proposed by the Commonwealth that would amend the U.S. Internal Revenue Code of 1986 to provide a new and permanent tax regime applicable to U.S. based businesses that have operations in Puerto Rico or other U.S. possessions.

The plan has three substantive components. First, Sections 30A and 936 would be allowed to expire according to their terms and would not be amended to remove the limitations that are scheduled to take effect at the end of 2001. Second, Section 956 would be amended to exclude from current U.S. tax 90% of the otherwise taxable investments in "U.S. property" made by a Qualified Possessions CFC (defined below) out of its Qualified Possessions Income (defined below). Third, transition rules would be provided for companies now conducting operations in Puerto Rico (i.e., existing Section 936 and 30A credit claimants).

A "Qualified Possessions CFC" would be defined under the Code as a controlled foreign corporation which is incorporated in Puerto Rico or another U.S. possession. "Qualified Possessions Income" would be limited to that portion of the CFCs post-2001 foreign source income that is derived from the active conduct by the CFC of a trade or business in Puerto Rico (or another possession) or from the sale or exchange of substantially all the assets used by the CFC in the active conduct of such a trade or business. The proposed Section 956 exclusion would be applicable only to income that is eligible for deferral under general U.S. tax principles. Thus, for example, passive income received by the CFC could not be converted from income that is currently taxable under Subpart F into income eligible for deferral by the investment of such amounts in U.S. property pursuant to the proposed amendment to Section 956.

The new Section 956 exclusion and the related transition rule would be effective for taxable years of CFCs beginning after December 31, 2001. No assurance can be given at this time as to the likelihood of the passage of this legislation.

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-bond debt regardless of maturity), subject to the exclusions described in the following paragraph. Direct debt of the Commonwealth is supported by Commonwealth taxes. 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.

The following table presents a summary of public sector debt as of December 31, 2000. Excluded from this table is debt not primarily payable from either Commonwealth or municipal taxes, Commonwealth appropriations or rates charged by public corporations for services or products. Also excluded from this table is debt the inclusion of which would reflect double counting, including, but not limited to, $1,021,050,000 of bonds outstanding by the Municipal Finance Agency to finance its purchase of bonds of Puerto Rico municipalities, and $1,335,295,000 of obligations of GDB issued to purchase certain Commonwealth public sector debt and for other purposes, of which $267,000,000 is guaranteed by the Commonwealth.

Commonwealth of Puerto Rico

Public Sector Debt
(in thousands)

	December 31, 2000
Puerto Rico direct debt[1]	$ 5,585,657
Municipal debt	1,446,345
Public corporations debt	
Puerto Rico guaranteed debt[2]	603,343
Debt supported by Puerto Rico appropriations or taxes[3]	11,321,577
Other non-guaranteed debt	6,786,513
Total public corporations debt	$18,711,433
Total public sector debt	$25,743,435

(1) Includes a $21,415,921 loan from GDB to the Department of the Treasury to settle certain property tax claims of the municipalities (the "GDB Tax Claims Loan") and $78,820,000 of certain indebtedness originally issued by the Urban Renewal and Housing Corporation that was transferred to the Commonwealth by virtue of Act No. 134 of the Legislature of Puerto Rico, approved on December 13, 1994 ("Act No. 134 of 1994") (such indebtedness referred to as "Transferred CRUV Debt").

(2) Consists of bonds issued by the Housing Bank and Finance Agency and the Aqueduct and Sewer Authority. Excludes $1,564,098,219 of the Public Buildings Authority bonds and notes, which are primarily payable from Commonwealth appropriations and $267,000,000 of GDB bonds payable from available moneys of GDB.

(3) Represents, among others, bonds and notes issued by the Aqueduct and Sewer Authority, the Highway and Transportation Authority, the Public Buildings Authority, the Public Finance Corporation, the Infrastructure Financing Authority and the Housing Bank and Finance Agency and notes of the Health Facilities and Services Administration which were assumed by the Department of Health.

Source: Government Development Bank

No deductions have been made in the above table for 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 and Certain Commonwealth Guaranteed Debt

The following table presents debt service requirements for Commonwealth general obligation bonds and bonds of the Aqueduct and Sewer Authority for which debt service payments are being made under the Commonwealth guaranty, in each case outstanding on December 31, 2000. See "Commonwealth Guaranteed Debt" below. With respect to other debt of the Aqueduct and Sewer Authority, see *Public Corporations*. 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. The table does not include the debt service on $12,505,000 outstanding principal amount of the Puerto Rico Housing Bank and Finance Agency Special Obligation Refunding Bonds (Series H) guaranteed by the Commonwealth, which mature on October 1, 2001, a portion of which has, prior to fiscal 2000, been paid from Commonwealth appropriations. See "Commonwealth Guaranteed Debt" below. Debt service on such bonds is $13,249,048 for the bond year ending on October 1, 2001.

Commonwealth of Puerto Rico

Debt Service Requirements*
(in thousands)

	Outstanding Bonds				
Fiscal Year Ending June 30	Principal	Interest	Total Debt Service	PRASA Bonds Debt Service	Grand Total
2001	$257,731	$268,698	$526,430	$33,473	$559,903
2002	259,824	257,024	516,848	33,542	550,389
2003	194,314	322,650	516,964	32,745	549,709
2004	166,550	315,060	481,609	30,125	511,735
2005	242,947	235,096	478,043	30,127	508,170
2006	205,793	247,235	453,028	30,121	483,149
2007	181,279	251,492	432,771	30,126	462,897
2008	156,623	214,387	371,010	30,131	401,141
2009	167,365	185,391	352,755	30,123	382,879
2010	179,230	173,596	352,826	29,984	382,810
2011	188,502	163,830	352,332	29,928	382,260
2012	198,965	146,324	345,289	30,127	375,416
2013	191,720	135,896	327,616	30,128	357,744
2014	162,423	144,530	306,952	30,125	337,077
2015	169,835	137,304	307,138	30,126	337,264
2016	176,880	130,186	307,066	30,121	337,187
2017	185,922	121,313	307,235	30,122	337,356
2018	194,120	113,023	307,143	30,126	337,269
2019	198,701	86,949	285,650	30,125	315,774
2020	218,250	68,526	286,776	0	286,776
2021	187,200	56,927	244,127	0	244,127
2022	174,600	47,483	222,083	0	222,083
2023	160,140	38,662	198,802	0	198,802
2024	144,935	30,362	175,297	0	175,297
2025	129,450	22,590	152,040	0	152,040
2026	111,920	15,736	127,656	0	127,656
2027	88,590	9,915	98,505	0	98,505
2028	59,680	5,201	64,881	0	64,881
2029	31,935	1,916	33,851	0	33,851
	$ 4,985,421	$3,947,302	$8,932,723	$ 581,425	$ 9,514,148

*Totals may not add due to rounding.

Source: Government Development Bank and Department of the Treasury

Commonwealth Guaranteed Debt

As of December 31, 2000, $12,505,000 of Commonwealth guaranteed bonds of the Housing Bank and Finance Agency was outstanding. These bonds were originally issued by the Urban Renewal and Housing Corporation and refinanced in fiscal 1992 by the Housing Bank and Finance Agency. Their final maturity is October 1, 2001.

As of December 31, 2000, $1,564,098,219 of Commonwealth guaranteed bonds of the Public Buildings Authority was outstanding. Maximum annual debt service on these bonds is $160,778,436 in fiscal year ending June 30, 2002, with their final maturity being July 1, 2027. No payments under the Commonwealth guaranty have been required to date for bonds of the Public Buildings Authority.

As of December 31, 2000, $267,000,000 of Commonwealth guaranteed obligations of GDB were outstanding. No payments under the Commonwealth guaranty have been required for any obligations of GDB to date.

As of December 31, 2000, the Commonwealth had guaranteed the outstanding Series 1995 revenue bonds of the Aqueduct and Sewer Authority in the aggregate principal amount of $361,590,000. On January 2, 1997, the Commonwealth began to make debt service payments under the Commonwealth guaranty and expects to make all debt service payments required on these revenue bonds.

In addition, in April 2000, the Commonwealth extended its guaranty to all of the outstanding bonds issued by the Authority to the United States Department of Agriculture, Rural Development, and to all of the outstanding loans by the State Revolving Funds for the benefit of the Authority. The extended guaranty will also cover any additional bonds and loans that may be issued until June 30, 2005. As of December 31, 2000, aggregate principal amounts outstanding on these obligations were $126,872,000 and $102,376,000, respectively. No payments under the Commonwealth guaranty have been required to date for these bonds of the Authority.

Trends of Public Sector Debt

Historically, the Commonwealth has maintained a fiscal policy that provides for a prudent relationship between the growth of public sector debt and the growth of the economic base required to service that debt. During fiscal 1996, 1997 and 1998, however, public sector debt increased at a greater rate than the growth of gross product due to an increase in the amount of debt incurred to finance certain key infrastructure projects, which are important to the development of the economy and are expected to produce long-term economic benefits, and debt incurred to refinance outstanding debt to enable Puerto Rico to benefit from the historically low levels of interest rates and realize debt service savings.

As of December 31, 2000, outstanding short-term debt, relative to total debt, was 9.8%.

The following table shows the trends in gross product (in current dollars) and public sector debt for the five fiscal years ended June 30, 2000, and for the first six months of fiscal 2001.

Commonwealth of Puerto Rico

Public Sector Debt and Gross Product
(dollars in millions)

	Public Sector Debt					Gross Product(1)	
June 30	Long Term	Short Term(2)	Short Term as % of Total	Total*	Rate of Increase	Amount	Rate of Increase
1996....................	$16,316	$1,310	7.4%	$17,626	10.2%	$30,357	6.7%
1997....................	17,865	1,642(3)	8.4	19,507	10.7	32,343	6.5
1998....................	20,759	1,563(3)	7.0	22,322	14.4	35,161	8.3
1999....................	20,905	1,772(3)	7.8	22,678	1.6	38,298	8.9
2000....................	21,620	2,202	9.2	23,822	5.0	41,366(p)	8.0
December 31, 2000	23,209	2,535	9.8	25,744	8.1	N/A	N/A

* Totals may not add due to rounding.
(p) Preliminary.
(1) In current dollars.
(2) 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.
(3) 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, 2000, and for the first six months of fiscal 2001.

Commonwealth of Puerto Rico

Public Sector Debt by Major Category
(dollars in millions)

	Commonwealth			Municipalities			Public Corporations(1)			Total*		Grand Total*(4)
June 30	Long Term	Short Term(2)	Total*(4)	Long Term	Short Term(2)	Total*	Long Term	Short Term(2)	Total*	Long Term	Short Term(2)	
1996......	4,203	0	4,203	706	58	765	11,405	1,251	12,657	16,316	1,310	17,626
1997......	4,512	0(3)	4,512	843	51	894	12,509	1,590	14,100	17,865	1,642(3)	19,507
1998......	4,819	0(3)	4,819	973	57	1,030	14,967	1,506	16,473	20,759	1,563(3)	22,322
1999.......	5,097	0(3)	5,097	1,215	60	1,275	14,593	1,713	16,306	20,905	1,772(3)	22,678
2000.......	5,349	0	5,349	1,396	68	1,464	14,875	2,133	17,008	21,620	2,202	23,822
December 31, 2000	5,086	500	5,586	1,388	58	1,446	16,735	1,976	18,711	23,209	2,535	25,744

* Totals may not add due to rounding.
(1) Includes Commonwealth guaranteed debt.
(2) 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.
(3) Does not include the tax and revenue anticipation notes which 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.
(4) Includes the GDB Tax Claims Loan and the Transferred CRUV Debt.

Source: Government Development Bank

PUBLIC CORPORATIONS

In Puerto Rico, many governmental or quasi-governmental functions are performed by public corporations. These are governmental entities created by the Legislature with varying degrees of independence from the central government. Public corporations are generally created to perform 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 appointed by the Governor with the advice and consent of the Senate, but some public corporations are subsidiaries of departments of the central government. Capital improvements of most of the larger public corporations are financed by revenue bonds under trust agreements or bond resolutions or notes under loan agreements. The following table presents the outstanding bonds and notes of certain of the public corporations as of December 31, 2000 ("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 the Federal government or is payable from sources other than Commonwealth appropriations or taxes or revenues of public corporations, or is payable from revenues derived from 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
December 31, 2000
(in thousands)

	Bonds			Notes			Total Bond and Notes		
	With Guaranty	Without Guaranty	Total	With Guaranty	Without Guaranty	Total	With Guaranty	Without Guaranty	Total
Agricultural Services Administration	$ 0	$ 0	$ 0	$ 0	10,032	10,032	$ 0	10,032	10,032
Aqueduct and Sewer Authority	403,832	84,630[1]	488,462	0	870,058[1]	870,058	403,832	954,688	1,358,520
Credit and Credit and Development Corp.	0	0	0	0	0	0	0	0	0
Electric Power Authority(2)	0	4,312,163	4,312,163	0	125,000	125,000	0	4,437,163	4,437,163
Health Facilities and Services Administration(3)	0	0	0	0	654,041	654,041	0	654,041	654,041[3]
Highway and Transportation Authority	0	3,897,434	3,897,434	0	300,000	300,000	0	4,197,434	4,197,434
Housing Bank	24,320	519,201	543,521	0	92,195	92,195	24,320	611,396	635,716
Industrial Development Company(2)	0	179,552	179,552	0	8,077	8,077	0	187,629	187,629
Infrastructure Financing Authority	0	2,069,295[7]	2,069,295	0	50,895	10,182	0	2,120,190	2,079,477
Public Finance Corporation(2)	0	1,581,258[4]	1,581,258	0	16,285	16,285	0	1,597,543	1,597,543
Ports Authority	0	102,670	102,670	0	237,730	237,730	0	340,400	340,400
Public Buildings Authority(2)	1,621,000	0	1,621,000	0	138,173	138,173	1,621,000	138,173	1,759,173
Sugar Corporation	0	0	0	0	74,213[4]	74,213	0	74,213	74,213
University of Puerto Rico	0	488,488	488,488	0	675	675	0	489,163	489,163
Others	0	397,005[6]	397,005[6]	0	493,924	493,924	0	890,929	890,929
Total	$2,049,152[5]	13,631,696	15,680,848	$ 0	3,071,298	3,030,585	$2,049,152[5]	16,702,994	18,711,433

(1) Principal of and interest on this debt is reimbursed from Commonwealth appropriations.
(2) Does not include accretion of interest from the respective issuance dates on capital appreciation bonds, as follows (each as of December 31, 2000): Electric Power Authority $137,400,033; Industrial Development Company $6,578,159; Public Buildings Authority $58,643,783; and Public Finance Corporation $21,446,911.
(3) This is debt incurred by the Health Facilities and Services Administration prior to its dissolution on June 30, 1999, which debt was assumed by the Department of Health.
(4) Payable primarily from Commonwealth appropriations.
(5) Authorization for Commonwealth guarantee of debt as of December 31, 2000 was $4,371,000,000.
(6) On November 15, 2000, the Children's Trust issued its Tobacco Settlement Asset-Backed Bonds, Series 2000, in the total principal amount of $397,005,000. Said bonds will be repaid from payments made by certain tobacco companies under a master settlement agreement. See "Other Public Corporations" below.
(7) $1,092.6 million of this amount is payable from interest earnings on $1.2 billion deposited in the Puerto Rico Infrastructure Development Fund from a portion of the proceeds of the sale by the Commonwealth of its controlling interest in the Puerto Rico Telephone Company in 1999.

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 make loans to private enterprises to aid in the economic development of Puerto Rico.

As of December 31, 2000, $1,304,370,000 of bonds and notes of GDB were outstanding. As of said date, GDB also had $3,400,572,000 in loans to local public corporations and municipalities. 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 $550,000,000, may be guaranteed by the Commonwealth, of which $267,000,000 were outstanding as of December 31, 2000.

GDB has the following principal subsidiaries:

Housing Finance Corporation was created in November 1977 to provide needed rental housing units and stimulate the construction industry under federally subsidized programs. The Corporation has issued tax-exempt revenue bonds and notes to finance the construction of housing units approved for federal rental subsidies, which bonds and notes are limited obligations of the Corporation payable solely from revenues collected in respect of such housing units. The Federal Housing Administration has insured mortgages on certain of the housing units. As of December 31, 2000, $943,001,605 of bonds of Housing Finance Corporation was outstanding.

Tourism Development Fund was created in November 1993 to promote the hotel and tourism industry of Puerto Rico, primarily by making available guarantees to secure the payment of private financing used for new hotel development projects. The Tourism Development Fund is also authorized to make capital investments and provide direct financing to tourism related projects. As of December 31, 2000, the Tourism Development Fund had issued thirteen (13) guarantees totaling $611,124,306.

Development Fund was created in 1977 to provide an alternate source of financing to private enterprises in Puerto Rico that have difficulties in obtaining financing from traditional sources. The Development Fund may also guarantee obligations of these enterprises and invest in their equity securities.

Capital Fund was created in November 1993 for trading in debt obligations and publicly traded shares of domestic and foreign corporations.

PRTA Holdings was created in 1999 to hold, administer and dispose of, for the benefit of the Employees Retirement System of the Commonwealth of Puerto Rico and its instrumentalities, shares of stock in PRTC's holding company representing the Government's remaining 43% interest in PRTC. PRTA Holdings is a subsidiary of the Puerto Rico Telephone Authority.

Public Finance Corporation was created in December 1984 to provide agencies and instrumentalities of Puerto Rico with alternate means of meeting their financing requirements. In June 1995, the Corporation issued $296,393,974 of bonds to purchase from GDB certain debt of the Maritime Shipping Authority. In April 1996, the Corporation issued $192,108,735 of bonds to purchase from GDB a portion of a debt of the Secretary of the Treasury relating to advances made by the Secretary to the municipalities to settle certain property tax claims. In June 1998, the Corporation issued $383,225,000 of bonds to purchase from GDB the debt which had been incurred by the Office for the Improvement of Public Schools in connection with its public schools repair and improvement program. In January 1999, the Corporation issued $618,085,149 of bonds to purchase from GDB a portion of the outstanding indebtedness of Health Facilities and Services Administration ("AFASS"). All of these bonds of the Corporation are payable from Commonwealth appropriations.

In February 1999, the Corporation issued $228,318,000 of bonds to refund a GDB line of credit utilized by the Corporation to purchase certain property tax debts from the Municipal Revenues Collection Center and the Department of the Treasury. Said bonds are limited obligations payable solely from collections of the property tax debts purchased by the Corporation.

As of December 31, 2000, the Corporation had $1,581,257,741 aggregate principal amount of such bonds outstanding.

A description of certain other affiliates of GDB is provided in "Other Public Corporations."

Other Public Corporations

Aqueduct and Sewer Authority owns and operates a system of public water supply and sanitary sewer facilities. Capital expenditures are financed by revenues of the system, debt issuances, and federal and Puerto Rico grants. Debt service on revenue bonds is payable from net revenues of the system after payment of current expenses.

Facilities and operations of the Authority's system are subject to regulation under numerous federal and Puerto Rico environmental laws, including the federal Clean Water Act and the Safe Drinking Water Act administered by the United States Environmental Protection Agency ("EPA"). The Authority has embarked on an extensive capital improvement program for the five-year period ending June 30, 2005, that is estimated to cost approximately $1.7 billion. A portion of the capital improvement program is designed to enable the Authority to comply with federal and Commonwealth laws and regulations.

The Authority needs to make a substantial investment in infrastructure and a major overhaul of its operations to maintain the viability of the existing system and to finance its expansion for new users. Funds for this investment are expected to be provided through a combination of bond issues, legislative appropriations and federal grants. Due to the Authority's financial difficulties (discussed below) and its inability to access the bond market, Act No. 45 was enacted in July 1994 to provide a Commonwealth guaranty of the principal and interest payments to the bondholders of all outstanding debt previously issued by the Authority which, at that time, amounted to $388 million, and to also guarantee all future bonds or any other similar obligations incurred by the Authority to refinance such debt. In December 1995, the Authority issued $400,340,000 of its Refunding Bonds, Series 1995 (the "Series 1995 Bonds"), to refund all of the Authority's outstanding revenue and revenue refunding bonds. The Series 1995 Bonds are guaranteed by the Commonwealth pursuant to Act No. 45. On January 2, 1997, the Commonwealth began making all debt service payments under said guaranty in respect of the Series 1995 Bonds. In addition, Act No. 45 was amended on April 24, 2000, to extend the payment guaranty of the Commonwealth to all of the outstanding bonds issued by the Authority to the United States Department of Agriculture, Rural Development, and to all of the outstanding loans granted by the Clean Water and Drinking Water State Revolving Funds for the benefit of PRASA. The extended guaranty will cover any additional issuance of these obligations until June 30, 2005.

The Authority has reported net losses of $55.2 million, $94.9 million, $130 million and $100.7 million during fiscal years 1997, 1998, 1999 and 2000, respectively. These losses reflect the continuing financial and operating difficulties that the Authority has experienced in recent years. These losses were aggravated in recent years by extraordinary items, including the required adoption of new government accounting requirements relating to required expense reserves, the posting of previous years' non-registered entries and adjustments, employees' salary increases and early retirement bonuses, non-budgeted or underestimated expenses relating to the PSG Agreement (described below), increased maintenance costs and additional non-budgeted reserves. Legislation was approved in July 1994 providing for annual Commonwealth appropriations to the Authority to pay a portion of the principal of and interest on the Authority's indebtedness, cover capital improvements and defray a portion of the Authority's operating and maintenance expenses, as follows: $20 million for fiscal 1995, $25 million for fiscal 1996, $30 million for fiscal 1997, and $35 million for fiscal 1998. Additional legislation was approved in August 1997 providing for annual Commonwealth appropriations of $35 million annually through fiscal 2008.

On May 26, 1995, the Authority and Professional Services Group, Inc. ("PSG") entered into a five-year agreement (the "Agreement") for the operation, management, repair and maintenance of the Authority's public water supply and sanitary sewer systems, and for its customer service systems (the "Authority Systems"). PSG, which is headquartered in Houston, Texas, is a subsidiary of Air Water Technologies Corporation ("AWT"), which in turn is a subsidiary of Compagnie Générale des Eaux-SAHIDE ("CGE"), a member of the Vivendi Group, a French based international conglomerate of environmental, utility, energy, construction and communication companies. CGE guaranteed PSG's performance obligations under the Agreement. PSG commenced management of the Authority Systems in September 1995. Under the Agreement, all employees remained employees of the Authority, and the Authority retained management responsibilities for the capital planning, construction and environmental compliance departments. The management of certain departments, such as finance and management information systems, was shared by the Authority and PSG.

In September 1998, the Authority, PSG, AWT and CGE entered into an amendment to the Agreement (the "Amended Agreement"), that assigned all of PSG's obligations under the Agreement to CGE and AWT, with CGE being primarily responsible. The Amended Agreement extended the term of the Agreement by one year until August 31, 2001, transferred the management responsibility for the shared departments to CGE, and modified certain terms and conditions of the Agreement. The Amended Agreement includes performance incentives and penalties in the event that CGE fails to operate the Authority Systems within specified parameters, and establishes a contract administrator to oversee and monitor CGE's performance under the Amended Agreement. The annual fees payable to CGE may be adjusted to provide for certain unforeseen events and circumstances, such as additional operations expenses due to hurricanes, and for adding facilities to the Authority Systems. The Amended Agreement gave the Authority the right to terminate the Amended Agreement, without cause or penalty, at the end of the fifth contract year.

On March 1, 1999, the Authority entered into a further amendment to the Amended Agreement, which transferred to CGE responsibility of the departments that had remained under the Authority's control. In connection with such amendment, the fees and costs payable to CGE were adjusted to reflect the additional responsibilities assumed by CGE and the hoped for increased efficiencies of a private management company.

The Authority has entered into an agreement with Thames-Dick Superaqueduct Partners, Inc. for the planning, design, construction, operation and maintenance of the North Coast Superaqueduct Project (the "Project") to supply additional potable water to certain municipalities, mainly in the San Juan Metropolitan Area. The total estimated cost of the Project is approximately $390 million. GDB is providing interim financing for this Project, which is being paid over time from Commonwealth appropriations, and is considering permanent financing alternatives. One of the alternatives being considered is a bond issue payable from Commonwealth appropriations. The Project started operations during January 2000.

Economic Development Bank was created in July 1985 to engage primarily in granting small direct loans, providing loan guarantees to private enterprises, and making equity investments in such enterprises. Its initial capital was provided by a transfer of loans in the principal amount of $15,000,000 previously administered by a now inactive subsidiary of GDB. As of December 31, 2000, Economic Development Bank had an outstanding debt of $13,839,000 with GDB.

Electric Power Authority owns and operates the island's electric system. The Capital Improvement Program for the five-year period ending June 30, 2005, is estimated to cost approximately $2.0 billion and is financed primarily by borrowed funds, supplemented by internally generated funds. The Authority's bonded debt consists of Power Revenue Bonds, secured by a lien on net revenues of the electric system. As of December 31, 2000, the Authority had $4,312,163,000 in bonds outstanding (not including accretion of interest from the respective issuance dates on capital appreciation bonds). As a means of reducing its dependency on oil, the Authority has entered into power purchase contracts relating to the construction of certain cogeneration plants that will use fuels other than oil. These two cogeneration projects consist of EcoElectrica's 507 megawatts liquefied natural gas plant at Guayanilla and a 454 megawatts clean coal facility at Guayama to be built and operated by an affiliate of Applied Energy Systems ("AES"). EcoElectrica's plant started commercial operations in March 2000. Construction of AES' plant began in November 1999, and the plant is expected to be in service during calendar year 2002. It is expected that these two cogeneration plants will initially provide approximately one-third of the Authority's energy needs.

Health Facilities and Services Administration was created by Act No. 26 of November 13, 1975, as amended, for the principal purpose of developing and operating public hospitals and other health facilities and providing health services. In connection with the revamping of the island's public health system and as part of a health reform program that has the effect of changing the public health system from one in which the government provides health services to low income persons to one in which medical services are provided by the private sector and the government provides comprehensive health insurance cover to such persons, AFASS was dissolved on June 30, 1999, and its administrative responsibilities, agreements and claims were transferred to the Department of Health.

The operations of AFASS have been funded substantially by Commonwealth appropriations and lines of credit provided by GDB. Aggregate outstanding indebtedness to GDB as of December 31, 2000, relating to such lines of credit was $654,041,000. Such indebtedness is expected to be paid principally from Commonwealth appropriations.

The Commonwealth has entered into contracts with health insurance providers as part of its public health care reform. Some of these are subject to renewal at the end of fiscal year 2001, others during fiscal year 2002. The Commonwealth is in the process of negotiating contracts with insurance providers in order to reduce costs associated with its health care program and to implement uniform contractual terms among insurance companies and the Commonwealth at the beginning of fiscal 2002.

Highway 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 Authority, and federal and Puerto Rico grants. Debt service on the Authority's revenue bonds constitutes a first lien on its gross revenues, which consist currently of all the proceeds of the gasoline tax, one-half of the proceeds of the tax on gas oil or 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 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. As of December 31, 2000, the Highway and Transportation Authority had $3,897,434,000 in bonds outstanding.

The Authority has under construction the first phase of a new mass transit system, known as Tren Urbano, to serve areas of metropolitan San Juan. The first phase of Tren Urbano is being constructed under several design/build contracts, including a design/build/operate contract covering the design and construction of the system and the operation of Tren Urbano for five years with an additional five-year option at the Authority's election. The cost of the first phase is estimated to be $1.675 billion, which cost will be financed by Federal Transit Administration grants, other federal funding sources and the Authority's own resources. On August 4, 2000, the Authority entered into a loan agreement with the United States Department of Transportation Federal Transit Administration evidencing a long-term loan to the Authority in the amount of $300,000,000. This loan was used by the Authority to pay a portion of the costs related to the first phase of this project. An extension of the first phase of Tren Urbano to serve the area of Minillas Government Center is currently in the planning stage.

The 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 Authority payable by the private company principally from toll revenues. The concession is for a term of thirty-five (35) years, subject to earlier termination or extension. The bridge opened for traffic in February 1994. In certain circumstances as described in the concession agreement, including where toll revenues are insufficient to generate certain rates of return to the private operator, the private company may require the Authority, among other things, to assume the private company's obligations with respect to the special facility revenue bonds. Some of those circumstances, including low toll revenues, exist at this time, but the Authority does not currently anticipate that the private company will exercise its remedy against the Authority.

Housing Bank and Finance Agency is engaged in insuring mortgages and servicing mortgages originated by Urban Renewal and Housing Corporation and issues bonds and notes to provide interim and permanent financing for low-income housing projects and single-family home ownership programs. The Agency obtains funds from legislative appropriations, sales of mortgages, mortgage repayments and other sources.

As of December 31, 2000, the Agency had outstanding $543,521,000 of bonds (of which $12,505,000, originally issued by the Urban Renewal and Housing Corporation, are guaranteed by the Commonwealth) issued to pay obligations of the Commonwealth under law, otherwise payable from Commonwealth appropriations, to fund certain payments of the Commonwealth under its mortgage subsidy program for low and moderate income families, to guarantee certain insurance obligations of the Agency under certain programs, and to refund bonds originally issued by Urban Renewal and Housing Corporation to carry out activities related to the provision of low-cost housing for moderate income families, federally aided public housing for low income families, and urban renewal, housing and related activities. These bonds are payable principally from appropriations in substantially the amount that the Commonwealth would otherwise have been bound to appropriate for such purposes.

Industrial Development Company participates in the Commonwealth-sponsored economic development program by providing physical facilities, general assistance, and special incentive grants to manufacturers. The Company was merged with the Economic Development Administration in January 1998. Rentals derived from the leasing of specified facilities of the Company are pledged to the payment of the Company's revenue bonds. As of December 31, 2000, the Company had $179,552,000 in bonds outstanding (not including accretion of interest from the respective issuance dates on capital appreciation bonds).

Industrial, Tourist, Educational, Medical and Environmental Control Facilities Financing Authority ("AFICA") was created in June 1977. The Authority has issued revenue bonds to finance industrial, tourist, pollution control, medical, and educational 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 the Authority 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 December 31, 2000, $3,425,000,000 of the Authority's bonds were outstanding.

Infrastructure Financing Authority was created in June 1988 by virtue of Act No. 44 of June 21, 1988, as amended ("Act No. 44"), to provide financial, administrative, consulting, technical, advisory, and other types of assistance to other public corporations and governmental instrumentalities of Puerto Rico authorized to develop infrastructure facilities and to establish alternate means for financing infrastructure facilities. The Authority 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 public corporations and instrumentalities of the Commonwealth. Act No. 44 also established the Puerto Rico Infrastructure Fund, funded in the amount of $30 million during fiscal 1989 and $40 million for the following twenty-nine (29) fiscal years with the first proceeds of federal excise taxes imposed on rum and other articles produced in Puerto Rico and sold in the United States which are transferred to Puerto Rico pursuant to the United States Internal Revenue Code of 1986, as amended. On July 7, 1997, Act No. 44 was amended to increase to $60 million for fiscal year 1998 and $70 million for each subsequent year until fiscal year 2028 the amount of federal excise taxes transferred to the Authority. The increased level of appropriations was used by the Authority to provide additional financial support to aqueduct and sewer projects. The Authority had $2,069,259,000 in bonds outstanding as of December 31, 2000.

In January 1998, the Authority expanded the assistance given to Aqueduct and Sewer Authority to include assistance covering the design and construction of various strategic regional water and sewer projects intended to provide improved services to targeted regions throughout the island, the implementation of an immediate action plan to address a number of small water and sewer rehabilitation projects, and legal and technical assistance in achieving compliance with certain environmental laws and in establishing a prioritized capital program. The Authority is undertaking such projects at the request of the Aqueduct and Sewer Authority.

In June 1998, Act No. 44 was amended to establish the Infrastructure Development Fund, a permanent trust fund to be utilized by the Authority for the purpose of financing infrastructure projects. The Infrastructure Development Fund was initially funded in March 1999 with $1.2 billion of proceeds received by the Telephone Authority from the sale of a controlling interest in PRTC. This initial amount will remain permanently deposited in a segregated, perpetual account, denominated the "corpus account," and must be invested exclusively in U.S.

government or U.S. government-backed obligations. The income from such investment may only be used to finance infrastructure projects related to the Commonwealth's water and sewer systems. Other moneys in the Infrastructure Development Fund not attributable to the corpus account or the investment income thereon may be used for other infrastructure projects. The Authority is the custodian and administrator of the Infrastructure Development Fund. On October 11, 2000, the Authority issued $1,092,550,000 in bonds payable from and secured by a pledge of the interest received by the Authority from the investments of the Infrastructure Development Fund. The proceeds of this bond issue are being used to finance certain aqueduct and sewer infrastructure development projects.

Maritime Shipping Authority commenced operations in 1974 upon the acquisition of three shipping lines serving Puerto Rico and the United States mainland. On March 3, 1995, the assets and operations of the Maritime Shipping Authority were acquired by an investor group headed by BTIP, a subsidiary of Bankers Trust New York Corporation, under the terms and conditions approved by the Legislature of Puerto Rico and signed by the Governor on September 27, 1994. The remaining debt of the Authority was refinanced, as allowed under Act No. 113 of September 27, 1994, through the issuance of bonds by Public Finance Corporation, a subsidiary of GDB. The aggregate principal amount of such bonds as of December 31, 2000, was $271,878,974 (not including accreted values of capital appreciation bonds outstanding). The bonds are payable from funds to be appropriated annually by the Legislature of Puerto Rico.

Municipal Finance Agency was created in 1972 as a municipal "bond bank" for Puerto Rico. The Agency 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 the Agency's bonds is payable from debt service payments on municipal bonds held by the Agency 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 Legislature, which appropriation is authorized but not legally required to be made. To date no such payments have been required.

Ports Authority owns and operates the major airport and seaport facilities in Puerto Rico. The 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 seaport equipment and property. The Authority had total net losses of approximately $70 million during fiscal years 1993 and 1994 and, as a result, was not in compliance with its rate covenant with bondholders. After reducing its operating losses through a comprehensive rate revision process, including the implementation of annual (instead of triennial) rate revision analyses, the Authority is currently in compliance with its rate covenant. The Authority is implementing a plan to restructure its operations which, among other things, encompasses revisions to its capital improvement program, measures to increase collections from certain users of its facilities, and proposals to improve the efficiency of its operations. Act No. 1 of January 1, 2000 authorized the transfer of the Authority's unprofitable maritime ferry operations to a newly created government agency. The Authority reported net losses during the fiscal years ended June 30, 1997, 1998 and 1999 of $11.3 million, $28.8 million and $6.5 million, respectively. The Authority reported a net income of $15.3 million for fiscal year 2000. As of December 31, 2000, the Authority had $102,670,000 in bonds outstanding.

Public Buildings Authority is authorized to construct, purchase or lease office, school, health, and social welfare facilities for lease to departments, public corporations, and instrumentalities of the Commonwealth. Bonds that have been issued by the Authority 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 further secured by the Commonwealth's guaranty. The Authority is authorized by Act No. 17 of 1968, as amended, to have outstanding at any one time up to $2,100,000,000 of bonds guaranteed by the Commonwealth. As of December 31, 2000, $1,564,098,219 of such bonds of the Authority was outstanding (not including accretion of interest from the respective issuance dates on capital appreciation bonds). The Authority has four lines of credit for its capital improvement program totaling approximately $631,000,000, of which $138,173,763 was outstanding as of December 31, 2000.

The Authority is undertaking a program to construct additional correctional facilities to be completed by July 2002 at an estimated cost of $187,000,000. The Authority has previously issued $126,972,552 in bonds to finance the construction of three correctional facilities, which are being operated by private companies.

At present, several officers of the Commonwealth are defendants in a lawsuit filed in United States District Court in which they are charged with violating the constitutional rights of correctional system inmates as a result of severe overcrowding in the island's correctional system. Fines to assure compliance with minimum space standards have been assessed in the past against the defendants, such fines being paid by the Commonwealth. Most of these fines have been earmarked for improving the conditions of inmates but not for construction of additional correctional facilities to alleviate prison overcrowding. The Commonwealth of Puerto Rico can give no assurance that additional fines will not be levied in connection with this lawsuit.

Sugar Corporation was created in 1973 to consolidate ownership and management of the Commonwealth of Puerto Rico's interests in Puerto Rico's sugar industry. Until February 27, 1998, Sugar Corporation owned or leased and operated virtually all the sugar production facilities on the island. Sugar Corporation bought all cane grown by private growers, processed the cane, and sold crude and refined sugar and molasses. For many years, its operations produced substantial operating deficits. At December 31, 2000, the assets and liabilities of the Sugar Corporation were transferred to Central Roig and Central Coloso. For fiscal 2000 appropriations of approximately $10,000,000 were made to cover its operating deficit. As of December 31, 2000, the total debt of the corporation was $74,213,000. Of this amount $62,856,000 is payable from Commonwealth appropriations.

On September 5, 1996, the Governor of Puerto Rico signed into law Act No. 189, as amended, which authorized the transfer, for a nominal sum, of certain assets and liabilities of the Corporation to entities created by the sugar cane growers. Pursuant thereto, the Commonwealth has transferred the operations of the Corporation to certain entities formed by sugar cane growers. The Corporation retained substantially all its liabilities.

Telephone Authority was created in July 1974 when the Commonwealth purchased PRTC from International Telephone and Telegraph Corporation. PRTC operates the principal telephone system in Puerto Rico.

On March 2, 1999, the Telephone Authority sold a controlling interest in PRTC to a consortium led by GTE International Telecommunications Incorporated, which has recently been acquired by Verizon. The net proceeds of the sale received at closing were applied to defease outstanding bonds of the Authority in the principal amount of $756 million, to make a $1.2 billion deposit to the Infrastructure Development Fund held by the Infrastructure Financing Authority and to pay certain benefits to PRTC employees. The Government retained a 43% stock participation in PRTC. The proceeds from the future sale of such participation will be applied to reduce the unfunded pension benefits obligations of the Employees Retirement System of the Commonwealth of Puerto Rico and its instrumentalities.

University of Puerto Rico, with 69,773 students during academic year 2000-2001, 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 of which $488,488,000 was outstanding as of December 31, 2000.

On December 21, 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 will be built and operated by Desarrollos Universitarios, Inc., a Puerto Rico not-for-profit corporation, and will be leased to the University for a term equal to the term of the bonds with lease payments being of sufficient amounts to pay debt service on said bonds as they become due.

The Children's Trust Fund (the "Trust") is a not-for-profit corporate entity created by the Commonwealth under Act No. 173 of July 30, 1999. The Trust is a public instrumentally of, but separate and apart from, the Commonwealth.

Pursuant to the Act, the Commonwealth has transferred to the Trust all of its rights, title and interest under the Master Settlement Agreement ("MSA"), including the Commonwealth's right to receive initial, annual and strategic contribution payments to be made by the participating cigarette manufacturers under the MSA.

The Trust issued $397,005,000 aggregate principal amount of Tobacco Settlement Asset-Backed Bonds, Series 2000 on November 15, 2000. The Series 2000 and any other additional series of Senior Bonds will be secured by a statutory pledge of certain tangible and intangible assets of the Trust, including its right to receive fifty percent (50%) of Puerto Rico's portion of the initial payments, annual payments, and strategic contribution payments under the MSA.

Public corporations, in addition to those mentioned above, have outstanding debt in the aggregate amount of $411,886,000 as of December 31, 2000. Debt service on $202,576,000 of such outstanding debt is being paid from legislative appropriations. However, the Commonwealth is not 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 the Electric Power Authority and the Aqueduct and Sewer Authority, which is 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

Public employees of the Commonwealth and its instrumentalities are covered by five retirement systems: the Employees Retirement System of the Commonwealth and its instrumentalities (the "Employees Retirement System"), the Annuity and Pension System for the Teachers of Puerto Rico (the "Teachers Retirement System"), the Commonwealth of Puerto Rico 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 University Retirement System and the Electric Power Authority Retirement System apply to employees of the University of Puerto Rico and Electric Power Authority, respectively. The Commonwealth is not required to contribute directly to those two systems, although a large portion of University revenues is derived from legislative appropriations.

The Teachers Retirement System covers primarily public school teachers, the Judiciary Retirement System covers judges, and the Employees Retirement System covers all other employees of the Commonwealth, its municipalities and instrumentalities. As of June 30, 2000, the total number of active members of the three systems was as follows: Employees Retirement System, 158,000; Teachers Retirement System, 48,122, and Judiciary Retirement System, 343. The three systems are financed by contributions made by employers (the Commonwealth, public corporations, or municipalities), employees, and investment income. The government is responsible for approximately 66% of total employer contributions to the Employees Retirement System, and the other 34% is the responsibility of public corporations and municipalities. The 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 systems and required contributions to the systems by employees are determined by statute. Required contributions to the systems by employers are determined by statute with respect to the Teachers Retirement System and, with respect to the Employees and Judiciary Retirement Systems, by the Administrators of the Systems.

According to the most recent actuarial valuation of the Employees Retirement System and Judiciary Retirement System submitted by a firm of independent consulting actuaries, as of June 30, 2000, the total pension benefit obligation for the Employees Retirement System and Judiciary Retirement System was $9,459,300,000 and $135,800,000, respectively. The unfunded pension benefit obligation of the Employees Retirement System and Judiciary Retirement System for the same period was $7,417,500,000 and $53,000,000, respectively, representing a funding ratio of 22% and 61%, respectively. The actuarial valuation was completed in accordance with the "Projected Unit Credit" method. An investment return of 8.5% per year, a salary increase of 5% per year, and a post-retirement benefit increase of 3% every third year were assumed. This benefit increase was provided by the Legislature of Puerto Rico by Act No. 10 of May 10, 1992. The first 3% increase was granted to retirees who had been receiving their annuities for three or more years as of that date. The second 3% increase was granted to retirees who had been receiving their annuities for three or more years as of January 1, 1995. This increase is being financed by additional contributions from the employers. The third 3% increase was granted to retirees who had been receiving their annuities for three or more years as of January 1, 1998. This third increase is being partially funded with additional contributions from some of the employers. Subsequent increases will depend upon the explicit approval of the System's Board of Trustees and the Legislature, based on a favorable recommendation from the System's independent consulting actuary and given a minimum of twenty-four (24) months of benefit payment reserves.

On February 1, 1990, the Legislature of Puerto Rico enacted Act No. 1 amending the organic act of the Employees Retirement System to reduce the future pension liabilities of the Employees Retirement System. Among other provisions, the legislation increased the level of contribution to the System and limited the retirement benefits for new employees by increasing the length of time for the vesting of certain benefits and reducing the level of benefits in the case of early retirement. The legislation also reduced the level of occupational disability benefits and death benefits received by new employees.

Act No. 305 of September 24, 1999 further amended the organic act of the Employees Retirement System to change it, prospectively, from a defined benefit system to a defined contribution system. This amendment provides for the establishment of an individual account for each employee hired by the Government after December 31, 1999 and for those current employees who elect to transfer from the existing defined benefit system. The individual account of each current employee is credited initially with an amount equal to his aggregate contributions to the Employees Retirement System, plus interest. Current employees who do not elect to transfer to the new defined contribution system will continue accruing benefits under the current defined benefit system. The individual account of each participant of the new defined contribution system is credited monthly with the participant's contribution and is credited semiannually with a rate of return based on either of two notional investment returns. Such accounts are not credited with any contribution by the Commonwealth. Instead, government contributions will now be used completely to reduce the unfunded accumulated pension liability of the Employees Retirement System.

Based on actuarial studies conducted by the actuary of the Employees Retirement System, it is expected that the implementation of the defined contribution system will allow the government to reduce the current actuarial deficit of the Employees Retirement System.

The law approving the sale of a controlling interest in PRTC to a consortium led by GTE International Telecommunications Incorporated provides that any future proceeds received by the government from the sale of its remaining 43% stock ownership in PRTC will be transferred to the Employees Retirement System to reduce its accumulated unfunded pension benefit obligation.

According to the most recent actuarial valuation of the Teachers Retirement System submitted by a firm of independent consulting actuaries, as of June 30, 1999, the accrued actuarial liability of the system was $2,904,195,938, the value of assets amounted to $2,509,490,000, representing a funding ratio of 79.67%, and the resulting unfunded accrued liability was $590,465,938, a decrease of $194,037,629 from the prior valuation made as of June 30, 1998. As of June 30, 1999, the remaining amortization period for the unfunded liability is twenty-one (21) years. The actuarial valuation assumed an investment return of 8% per year and salary increases of 5% per year. Act No. 43 of January 27, 2000 increased the amount of the employee contribution from 7% to 9%, effective immediately. This will result in an increase of employee contributions of $1.5 million per month.

The following table presents, in summary form, the income and expenses of the retirement systems for the fiscal years ended June 30, 1999 and June 30, 2000, and estimates for the fiscal year ending June 30, 2001. The investment income figures presented in the table include unrealized gains and losses. Income for fiscal 2001 is estimated as of December 31, 2000 and does not reflect the decline in the equities market that has occurred in recent months. It is expected that the net income for Fiscal 2001 will be lower than the estimate shown as of December 31, 2000.

Commonwealth of Puerto Rico

Retirement Systems
Income and Expenses
(in thousands)

	Employees Retirement System	Judiciary Retirement System	Teachers Retirement System
Fiscal Year Ended June 30, 1999	**Actual**	**Actual**	**Actual**
Income:			
Employers' contributions	$274,658	$ 5,744	$ 91,155
Employee contributions	217,179	2,115	67,807
Investment income	244,025	7,489	242,198
Total	735,862	15,348	401,160
Expenses:			
Benefit payments	515,993	7,099	206,397
Administrative and other expenses	33,956	1,074	16,469
Total	549,949	8,173	222,866
Net Income	$185,913	$ 7,175	$ 178,294
Fiscal Year Ending June 30, 2000	**Actual**	**Actual**	**Actual**
Income:			
Employers' contributions	$309,097	$ 5,222	$ 86,246
Employee contributions	218,342	2,094	68,864
Investment income	296,842	11,075	286,507
Total	824,281	18,391	441,617
Expenses:			
Benefit payments	605,465	7,705	219,886
Administrative and other expenses	28,651	1,372	31,755
Total	634,116	9,077	251,641
Net Income	$190,165	$ 9,312	$ 189,976
Fiscal Year Ended June 30, 2001(1)	**Projected**	**Projected**	**Projected**
Income:			
Employers' contributions	$ 310,000	$ 5,500	$ 90,000
Employee contributions	220,000	2,200	75,000
Investment income	200,000	8,500	275,000
Total	730,000	16,200	440,000
Expenses:			
Benefit payments	626,000	8,800	242,000
Administrative and other expenses	34,000	1,800	32,000
Total	660,000	10,600	274,000
Net Income	$ 70,000	$ 5,600	$ 166,000

(1) Projected figures as of December 31, 2000

Sources: Employees Retirement System, Judiciary Retirement System and Teachers Retirement System

The Employee Retirement System may borrow on an interim basis, if necessary, from GDB to help cover expenses for Fiscal 2001.

COMMONWEALTH FINANCIAL STATEMENTS

Since fiscal 1990, the complete financial statements of the Commonwealth have been audited. For fiscal 2000, the financial statements of the Commonwealth have been audited by Deloitte & Touche, LLP, independent auditors. Preparation of the audited financial statements of the Commonwealth involves the collection and combination of audited financial statements from fifty (50) separate reporting entities.

The Comprehensive Annual Financial Report of the Commonwealth for fiscal 2000 prepared by the Department of the Treasury, which includes the general purpose financial statements of the Commonwealth for fiscal 2000, has been filed by the Commonwealth with each nationally recognized municipal securities information repository.

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 was incorporated into the General Fund commencing in fiscal 1993.

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 taxes and excise 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 Commonwealth revenues and expenditures of the General Fund on a cash basis for fiscal 1997 through fiscal 2001. The information relating to fiscal 2001 is based on the current budget approved by the Legislature, except for revenues that were revised as of February 2001, and was provided by the Secretary of the Treasury. The information for fiscal 1997 through fiscal 2000 is based on actual fiscal year-end results.

To improve the presentation of the following table, the Department of the Treasury has eliminated the use of line items identified as "Operating Transfers In" and "Operating Transfers Out" in the financial statements of the Commonwealth and has assigned the amounts previously listed under these two categories to the following revenue and expenditure line items according to the purpose and amount of each transfer: "Other Income," "Other Expenditures," "Capital Outlays and Other Debt Service" and "Transfers to Agencies." 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 Legislature has by resolution agreed to appropriate funds. "Transfers to Agencies" represents moneys appropriated for the operation of the Health Facilities and Services Administration and for repayment of certain advances to the General Fund from certain public pension 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 latter 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)

	1997	1998	1999	2000	Estimated 2001(1)
Beginning cash balance	$ 147,066	$ 127,477	$ 340,771	$ 474,759	$ 287,055
Revenues from internal sources:					
Income Taxes:					
Individuals	1,825,337	2,026,612	2,310,376	2,513,061	2,677,000
Corporations	1,440,691	1,527,415	1,544,762	1,752,862	1,697,000
Partnerships	2,120	4,404	2,087	2,339	3,000
Withheld from non-residents	88,603	192,463	369,384	557,276	602,000
Tollgate taxes	210,245	170,953	114,533	111,130	36,000
Interest	7,582	11,406	10,666	11,679	12,000
Dividends	35,438	39,616	38,996	39,664	41,000
Total income taxes	3,610,016	3,972,869	4,390,804	4,988,011	5,068,000
Commonwealth excise taxes					
Alcoholic beverages	229,043	238,118	243,464	236,374	236,000
Cigarettes	120,287	111,094	119,105	115,157	119,000
Motor vehicles	365,820	350,004	411,573	389,995	404,000
Other excise taxes	704,203	613,500	699,685	668,820	623,000
Total Commonwealth excise taxes	1,419,353	1,312,716	1,473,827	1,410,346	1,382,000
Property taxes	8,286	5,673	2,214	1,131	-
Inheritance and gift taxes	4,028	1,380	1,811	3,109	7,000
Licenses	53,535	66,167	70,848	73,801	78,000
Other:					
Lottery	52,829	57,986	59,206	63,779	56,000
Electronic Lottery	47,994	54,681	53,013	70,209	69,000
Miscellaneous non-tax revenues	139,838	158,568	176,669	169,246	203,000
Total other	240,661	271,235	288,888	303,234	328,000
Total revenues from internal sources	5,335,879	5,630,040	6,228,392	6,779,632	6,863,000
Revenues from non-Commonwealth sources:					
Federal excise taxes	203,755	200,260	217,296	245,750	293,000
Customs	61,114	72,206	61,355	50,231	39,000
Total revenues from non- Commonwealth sources	264,869	272,466	278,651	295,981	332,000
Sub-total revenues	5,600,748	5,902,506	6,507,043	7,075,613	7,195,000
Proceeds from Special Funds	23,217	50,253	-	-	-
Total Revenues	5,623,965	5,952,759	6,507,043	7,075,613	7,195,000
Other Income (refunds)(2)	80,388	482,120	45,570	(67,675)	(143,066)
Transfers to Redemption Fund (3)	(375,000)	(368,544)	(320,240)	(410,046)	(297,946)
Short-term note proceeds(4)	-	-	-	175,000	771,481
Repayment of short-term proceeds(5)	-	-	-	(177,709)	(687,000)
Note proceeds (6)	551,186	601,892	600,000	603,863	-
Repayment of notes (7)	(563,628)	(617,775)	(611,410)	(609,446)	-
Adjusted revenues	5,316,911	6,050,452	6,220,963	6,589,600	6,838,469
Expenditures:					
Grants and subsidies	1,676,929	2,118,266	2,392,018	2,864,215	2,516,765
Personal services	2,164,007	2,197,903	2,470,456	2,737,159	3,315,273
Other services	666,004	698,446	723,563	745,194	856,013
Materials and supplies	84,789	84,451	99,404	109,081	144,063
Equipment purchases	37,507	31,626	52,993	56,404	73,070
Capital outlays and other debt service	47,269	253,962	166,841	101,178	6,068
Transfers to agencies	355,213	131,174	181,700	164,073	193,130
Other expenditures	304,782	321,330	-	-	-
Total expenditures	5,336,500	5,837,158	6,086,975	6,777,304	7,104,382
Adjusted revenues less expenditures	(19,589)	213,294	133,988	(187,704)	(265,913)
Ending cash balance	$ 127,477	$ 340,771	$ 474,759	$ 287,055	$ 21,142

(1) Budget, as adopted, except for the estimates of revenues, which were revised in February 2001.
(2) Consists of reimbursement of certain advances to agencies to cover expenses 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 to the Redemption Fund from non-General Fund revenues.
(4) Consists of proceeds of short-term borrowing from the Government Development Bank issued in each such fiscal year.
(5) Consists of repayment of short-term borrowing from the Government Development Bank issued in each such fiscal year.
(6) Consists of proceeds from Commonwealth tax and revenue anticipation notes issued in each such fiscal year.
(7) Consists of amounts deposited for the repayment of Commonwealth tax and revenue anticipation notes issued in each such fiscal year.

Source: Department of the Treasury

Estimated Fiscal 2001 Compared to Fiscal 2000

General Fund estimated total revenues for fiscal 2001 (excluding proceeds from special funds) are forecast at $7,195 million, revised. The major projected changes with respect to fiscal 2000 are: an increase in individuals' income taxes of $164 million; an increase in income tax withheld from non-residents of $45 million; and an increase in federal excise taxes of $47 million. Individual income taxes are expected to rise due to growing employment, particularly in higher wage industries such as pharmaceuticals. Withholding taxes are expected to increase as a result of continuing conversions of corporations from 936 status to controlled foreign corporation tax status and the payment of withholding taxes on royalties paid to U.S. affiliates. Federal excise tax revenues are expected to increase due to growing exports of rum products. For fiscal 2000 the rum excise tax increased from $10.50 to $13.25 per gallon, but for the second half of fiscal 2002, the rum excise tax is expected to return to $10.50 per gallon. See "Major Sources of General Fund Revenues" below.

Total projected expenditures for fiscal 2001 are estimated at $7,104 million, an increase of $327 million or 4.8% over fiscal 2000. The ending cash balance for the General Fund for fiscal 2001 is estimated to be $21.1 million, a decrease of $265.9 million from fiscal 2000. Expenditures grew primarily in the areas of education, health and public safety. This growth is attributable in part to the rising cost of services and expanding programs.

In lieu of issuing tax and revenue anticipation notes in fiscal 2001 to meet seasonal differences in the timing of revenues and expenses, the Commonwealth obtained a loan from the GDB in the amount of $771.4 million. It is expected that at fiscal year end $687 million will have been repaid.

Fiscal 2000 Compared to Fiscal 1999

General Fund total revenues for fiscal 2000 were $7,076 million, an increase of $569 million or 8.7% over fiscal 1999. The major changes were: an increase in individuals' income taxes of $203 million and an increase in corporate income taxes of $208 million.

Total expenditures for fiscal 2000 were $6,777 million, an increase of $690 million or 11.3% over fiscal 1999. The ending cash balance for the General Fund for fiscal 2000 was $287 million, a decrease of $188 million from fiscal 1999.

Fiscal 1999 Compared to Fiscal 1998

General Fund total revenues for fiscal 1999 were $6,507 million, an increase of $604 million (10.2%) over fiscal 1998. Major changes were: an increase in income taxes of $418 million and an increase in excise taxes of $161 million.

Total expenditures for fiscal 1999 were $6,087 million, an increase of $250 million (4.3%) from fiscal 1998. The ending cash balance for the General Fund for fiscal 1999 was $475 million, an increase of $134 million from fiscal 1998.

Fiscal 1998 Compared to Fiscal 1997

General Fund total revenues for fiscal 1998 were $5,903 million, an increase of $302 million (5.4%) over fiscal 1997. Major changes were: an increase in income taxes of $363 million; and a decrease in excise taxes of $107 million (due to the transfer of the first $120 million of excise taxes on certain petroleum products to the Puerto Rico Highways and Transportation Authority and $17 million to Metropolitan Bus Authority).

Total expenditures for fiscal 1998 were $5,837 million, an increase of $501 million (9.4%), when compared to fiscal 1997. The ending cash balance for the General Fund for fiscal 1998 was $341 million, an increase of $213 million from fiscal 1997.

Major Sources of General Fund Revenues

Income Taxes

The Commonwealth's income tax law, the Internal Revenue Code of 1994, as amended (the "PR Code"), imposes 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. A withholding tax is imposed on certain payments made to non-residents of Puerto Rico.

Individuals. Resident individuals are subject to tax on their taxable income from all sources. The PR Code has five tax brackets for individuals with tax rates of 8%, 12%, 18%, 31% and 33%. As a result of legislation enacted in 1999 and 2000, the first four brackets have been reduced to 7.5%, 11%, 16.5% and 29.5% for the taxable year commencing on January 1, 2000, to 7%, 10%, 15% and 28% for taxable years commencing on January 1, 2001, and 6%, 9%, 14% and 27% for the taxable years commencing on and after January 1, 2002. Dividend income from Puerto Rico corporations and certain qualifying foreign corporations is taxed at a rate of 10%. A recent amendment to the PR Code provides an income tax exemption for Real Estate Investment Trusts ("REIT's") and imposes a 17% tax on taxable dividends distributed by such entities.

Gains realized from the sale or exchange of a capital asset, if held for more than six (6) months, are taxed at a rate of 10% (reduced from 20%). Gains realized from the sale of stock of certain Puerto Rico corporations in an initial public offering made prior to December 31, 2000 and December 31, 2003 are subject to a special capital gains rate of 7% and 9%, respectively.

On April 11, 2001, the Commonwealth approved Act No. 24 ("Act 24") which reduces the capital gains rate from 20% to 10 % in the case of individuals resident in Puerto Rico and United States citizens with respect to certain financial assets deemed located in Puerto Rico (i.e., bonds and other obligations issued by the Commonwealth, its municipalities and instrumentalities, stock in corporations organized under the laws of the Commonwealth or stock in foreign corporations that derives at least 80% of their income from Puerto Rico sources). For most taxpayers the reduced rate will be effective for transactions made on or after January 1, 2002. However, a bill has been introduced to change the effective date of the provisions of Act No. 24 to transactions taking place after March 31, 2001.

Interest income in excess of $2,000 on deposits with Puerto Rico financial institutions is taxed at a rate of 17%; 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 and estates qualifies for a special 17% tax rate.

Corporations and Partnerships. Puerto Rico corporations and partnerships are subject to tax on income from whatever source; foreign corporations and partnerships 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 or partnership qualifies for partial exemption from corporate income and other taxes under the industrial incentives program (see "Tax Incentives" under *The Economy* above), it is subject to tax at graduated rates.

The PR Code provides for six income tax brackets for corporations and partnerships, with the highest rate (39%) applicable to taxable income in excess of $275,000. Gains realized from the sale or exchange of a capital asset, if held for more than six months, are taxed at a maximum rate of 25%. Act No. 24 also reduced the capital gain rate from 25% to 12.5% for corporations upon the sale or exchange on the same assets referred to above. The reduced rate applies to transactions taking place in taxable years that commenced after March 31, 2001.

Gains realized from the sale of stock of certain Puerto Rico corporations in an initial public offering made prior to December 31, 2000 and December 31, 2003 are subject to a special capital gains rate of 7% and 9%, respectively. Interest on certain qualifying debt obligations is taxed at a 17% tax rate. The special tax rate applicable to dividend distributions of REIT's also applies to dividends received by corporations.

Certain corporations and partnerships covered by the tax incentives acts continue to be subject to a maximum tax rate of 45% on their taxable income. Corporations and partnerships covered by the Puerto Rico Tourism Incentives Act of 1993, as amended, are subject to a maximum tax rate of 42% on their taxable income. The PR Code also provides for an alternative minimum tax of 22%. Corporations and partnerships operating under a new grant of tax exemption issued under the 1998 Tax Incentives Act are subject to a maximum income tax rate of 7%.

The PR Code imposes a branch profits tax on resident foreign corporations less than 80% of 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 to non-resident non-affiliated corporate recipients is not subject to any income or withholding tax. Interest paid to certain related non-resident recipients continues to be 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 (including Section 936 Corporations) operating under new grants of tax exemption issued under the 1998 Tax Incentives Act are not subject to Puerto Rico income tax. The basic tax on dividends paid to foreign corporate shareholders of Section 936 Corporations operating under grants of tax exemption issued under prior incentives laws is 10% but is subject to reduction with respect to dividends paid from profits invested in certain eligible instruments for specified periods of time.

Payments in excess of $1,000 made by the Commonwealth of Puerto Rico and persons engaged in a trade or business in consideration of the receipt of services are subject to a 7% withholding tax.

Excise Taxes

The PR Code imposes a tax on articles and commodities that are imported into or manufactured in Puerto Rico for consumption in Puerto Rico and a tax on certain transactions, such as hotel occupancy, public shows, and horse racing. The excise tax on certain articles and commodities, such as cigarettes and petroleum products, is based upon the quantity of goods imported. The excise tax on motor vehicles is based on its suggested retail price. The PR Code imposes a tax at an effective rate of 6.6% of the F.O.B. factory price for imported goods and 3.6% of the sales price of goods manufactured in Puerto Rico, except sugar, cement, cigarettes, motor vehicles and certain petroleum products, which are taxed at different rates. Goods to be used by the government, except for motor vehicles and construction equipment, are not exempt. Exemptions apply to certain articles, such as food and medicines, and to articles designated for certain users.

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 include customs duties collected in Puerto Rico and excise taxes on shipments of alcoholic beverages from the island 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.

On April 26, 2001, legislation was introduced in the United States House of Representatives to repeal the return to the Treasury Department of Puerto Rico of the federal excise taxes on shipments of alcoholic beverages from Puerto Rico and other rum producing countries. It is expected that hearings on the proposed repeal will be held by the United States Congress shortly. The Commonwealth will vigorously oppose the enactment of any such repeal. No assurance can be given at this time as to the likelihood of the passage of such repeal.

Property Taxes

Personal property, which accounts for approximately 55% of total collections of taxable property, is self-assessed. Real property taxes are assessed at 1958 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 $15,000 of assessed valuation in owner-occupied residences is available.

On August 30, 1991, legislation was adopted in Puerto Rico providing a municipal reform program, which also involved the creation of the Municipal Revenues Collection Center ("CRIM") to collect property taxes. The program transferred the previous functions of the Department of the Treasury with respect to real and personal property tax assessment, notification, determination, and collection to the CRIM, as of July 1, 1993. The special 1.03% tax on the assessed value of all property (other than exempted property) imposed by the Commonwealth for purposes of paying the Commonwealth's general obligation debt continues to be deposited in the Commonwealth's Redemption Fund.

Commonwealth of Puerto Rico

Assessed Valuations and Real and Personal Property Taxes (Commonwealth and Municipalities Combined) (in thousands)

Fiscal Year Ended June 30	Assessed Valuations(1)	Taxes Levied	Collections of Current Year	Collections of Previous Years	Total
1996	$13,052,524	$416,881	$400,207	$70,571	$470,778
1997	$17,499,974	$533,362	$437,178	$82,435	$519,613
1998	$19,272,428	$619,343	$510,999	$90,311	$601,310
1999	$20,042,738	$642,555	$523,886	$47,309	$571,198
2000	$20,514,014	$704,568	$594,151	$64,812	$658,963

(1) Valuation set as of July 1 of each fiscal year.

Source: Municipal Revenues Collection Center

During 1997, legislation was enacted authorizing the CRIM to sell past-due property taxes on residential, commercial and industrial properties to persons who, after payment of the purchase price to the CRIM, would then be responsible for collecting such taxes from the delinquent property taxpayers. Pursuant to this legislation, in February 1999 the Government securitized eligible property tax debts of the CRIM. The proceeds of the securitization were paid to the CRIM for the benefit of the Commonwealth and the municipalities of the Commonwealth.

As of May 2001, all payments of debt service have been made. CRIM has received notice that it is not in compliance with certain requirements concerning the continuing eligibility of certain past-due accounts in the securitized pool and requesting CRIM to substitute other eligible past-due tax accounts for the pool. Remedial steps are being taken to address this situation.

Collections of Income and Excise Taxes

The Department of the Treasury has continued its program for improving tax collections, which began in fiscal 1986. The program has consisted, in part, of taking the initiative in sponsoring and implementing tax reform, particularly in the areas of excise taxes and income taxes, in order to decrease the incidences of nonpayment of taxes and to expand the taxpayer base. The program has also included (a) improving the methods by which delinquent taxpayers are identified, primarily through the use of computer analyses, (b) computerizing the processing of tax returns, and (c) identifying and eliminating taxpayer abuses of the existing tax laws.

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 of Puerto Rico 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 the payment of 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 moneys and payments for the amortization of the principal of and interest on non-general obligations payable from Commonwealth appropriations.

Transfers to Agencies

Includes 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 the Health Facilities and Services Administration 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 to be reimbursed to the General Fund by law.

Federal Grants

Puerto Rico receives grants under numerous federal programs. The following table presents revenues from federal grants by broad program areas, which are accounted in the central accounting system of the Department of the Treasury.

Commonwealth of Puerto Rico

Federal Grants
(in thousands)

	Fiscal Year Ending June 30				
	1998	**1999**	**2000(p)**	**2001(e)**	**2002(e)**
Education	$ 504,296	$ 571,758	$ 675,876	$ 734,494	$ 741,563
Social Services	1,592,402	1,548,876	1,579,453	1,685,563	1,694,593
Health	399,790	362,905	298,980	304,068	310,690
Labor and Human Resources (1)	161,272	308,699	263,263	335,158	337,073
Public Works and Transportation(2)	0	0	0	0	0
Crime	25,726	27,552	24,836	17,700	11,623
Housing(3)	224,787	232,359	232,359	232,359	236,931
Drug and Justice	10,909	9,841	14,424	14,712	11,062
Agriculture and Natural Resources	6,771	6,898	7,307	9,949	6,820
Contributions to Municipalities	64,911	58,865	58,865	56,809	59,191
Other	6,337	5,914	4,915	6,116	6,965
Total	$2,997,201	$3,133,667	$3,160,278	$3,396,928	$3,416,511

(p) Preliminary.
(e) Estimated.
(1) Amounts include grants to the Right to Work Administration and to the Occupational Development and Human Resources Council.
(2) Amounts of federal grants to the Highway and Transportation Authority are not included in the Public Works and Transportation area.
(3) Amounts include grants to the Public Housing Administration.

BUDGET OF THE COMMONWEALTH OF PUERTO RICO

Office of Management and Budget

The fundamental objective of the Office of Management and Budget ("OMB") is to improve and strengthen the relationship between policy formulation and budgetary and fiscal management. The law creating OMB also strengthened budgetary controls and created an Operational Audit Division with the primary function of evaluating government operations and programs.

Budgetary Process

The fiscal year of the Commonwealth begins each July 1. The Governor is constitutionally required to submit to the Legislature an annual balanced budget of capital improvements and operating expenses of the central government for the ensuing fiscal year. The annual budget is prepared by OMB, working with the Planning Board, the Department of the Treasury, 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 and zero-base 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 her judgment are necessary, convenient, and in conformity with the four-year investment plan prepared by the Planning Board.

The Legislature 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 Legislature, 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 Legislature with her objections. The Legislature, by a two-thirds majority in each house, may override the Governor's veto. If a budget is not adopted prior to the end of the fiscal year, the annual budget for the preceding fiscal year as originally approved by the Legislature and the Governor is automatically renewed for the ensuing fiscal year until a new budget is approved by the Legislature and the Governor. This permits the Commonwealth to continue to make 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 Department of the Treasury, except for estimates of federal grants, which are prepared by OMB and 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 severally by the Governor, through the Director of OMB, and the Secretary of the Treasury. Quarterly reviews and expenditure cut-off procedures are designed to prevent expenditures in excess of appropriations.

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 Legislature a detailed report of any adjustment necessary to balance the budget, or make recommendations to the Legislature 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 Act"), to cover the appropriations approved in any fiscal year in which the revenues available for such fiscal year are insufficient, to honor the public debt, and to provide for unforeseen circumstances in the provision of public services. The Budgetary Fund Act was amended in 1994 to require that an annual legislative appropriation equal to one-third of one percent (.33%) of the total budgeted appropriations for each fiscal year be deposited in the Budgetary Fund. In 1997, the Budgetary Fund Act was further amended to increase the annual legislative appropriation required to be deposited in the Budgetary Fund to 1% of the total revenues of the preceding fiscal year, beginning in fiscal year 2000. 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.

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 for contributions to public corporations, municipalities, and private organizations. Such appropriations are made by a single annual law known as the Joint Resolution of the General Budget.

(ii) General Fund appropriations for special operating expenses and for capital expenditures. Such appropriations are authorized by separate laws for one or more years for special programs or activities, which may be permanent or transitory.

(iii) Disbursements of Special Funds for operating purposes and for capital improvements. For the most part, such disbursements 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. Such expenditures may occur in one or more years.

In Puerto Rico, the central government has many functions, which in the fifty (50) states are the responsibility of local government, such as providing public education and police and fire protection. The central government also makes large annual grants to the University of Puerto Rico, PRASA and to the municipalities. In the summaries of the budgets of the central government presented below, grants to the University of Puerto Rico are included in current expenses for education and debt service on general obligation bonds is included in current expenses for debt service. Debt service on Sugar Corporation notes paid by the Commonwealth is included in current expenses for economic development, and debt service on Urban Renewal and Housing Corporation bonds and notes and on Housing Bank and Finance Agency mortgage subsidy bonds paid by the Commonwealth is included in current expenses for housing.

Approximately 25.2% of the General Fund is committed for payment of fixed charges such as municipal subsidies, grants to the University of Puerto Rico, contributions to the Aqueduct and Sewer Authority, and rental payments to the Public Buildings Authority, among others, including debt service on direct debt of the Commonwealth.

Fiscal 2001 Budget

The following table presents a summary of the Commonwealth budget for the fiscal year ending June 30, 2001.

Commonwealth of Puerto Rico

Summary of Central Government Annual Budget
Fiscal Year Ended June 30, 2001
(in thousands)

	General Fund	Bond Fund	Special Funds	Total
Revenues from internal sources:				
Property taxes	$ -	$ -	$ 101,371	$ 101,371
Personal income taxes	2,729,000	-	-	2,729,000
Income tax withheld from non-residents	525,000	-	-	525,000
Corporation income taxes	1,767,000	-	-	1,767,000
Partnership income taxes	3,000	-	-	3,000
Tollgate taxes	94,000	-	-	94,000
17% withholding tax on interest	13,000	-	-	13,000
10% withholding tax on dividends	40,000	-	-	40,000
Inheritance and gift taxes	2,000	-	-	2,000
Excise taxes:				
Alcoholic beverages	258,000	-	-	258,000
Motor vehicles and accessories	441,000	-	-	441,000
Cigarettes	119,000	-	-	119,000
Special excise tax on certain petroleum products	70,000	-	-	70,000
General 5% excise tax	599,000	-	-	599,000
Slot machines and machines for entertainment	-	-	-	-
Other	97,000	-	117,020	214,020
Licenses	78,000	-	-	78,000
Miscellaneous non-tax revenues:				
Contributions from lottery fund	58,000	-	-	58,000
Electronic lottery	63,000	-	-	63,000
Registration and document certification fees	147,000	-	-	147,000
Other	53,000	-	191,850	244,850
Total revenues from internal sources	7,156,000	-	410,241	7,566,241
Revenues from non-Commonwealth sources:				
Federal excise taxes on off-shore shipments	291,000	-	-	291,000
Federal grants	-	-	3,396,928[1]	3,396,928
Customs	58,000	-	-	58,000
Total revenues from non-Commonwealth sources	349,000	-	3,396,928	3,745,928
Total revenues	7,505,000	-	3,807,169	11,312,169
Other:				
Balance from previous year	106,220	-	348,027	454,247
Bonds authorized	-	425,000	-	425,000
Total other sources	106,220	425,000	348,027	879,247
Total resources	7,611,220	425,000	4,155,196	12,191,416

	General Fund	Bond Fund	Special Funds	Total
Appropriations:				
Current expenses:				
General government	841,537	-	56,959	898,496
Education	2,337,485	-	796,260	3,133,745
Health	1,263,702	-	328,567	1,592,269
Welfare	382,807	-	2,049,875	2,432,682
Economic development	171,151	-	68,599	239,750
Public safety and protection	1,264,612	-	61,324	1,325,936
Transportation and communications	72,446	-	11,324	83,770
Housing	20,892	-	117,395	138,287
Contributions to municipalities	300,380	-	2,047	302,427
Special pension contributions	46,410	-	-	46,410
Debt service	446,920	-	92,455	539,375
Other debt service	436,585	-	19,000	455,585
Total appropriations-current expenses	7,584,927	-	3,603,805	11,188,732
Capital improvements	25,915	425,000	160,896	611,811
Total appropriations	7,610,842	425,000	3,764,701	11,800,543
Year-end balance	378	-	390,495	390,873
Total appropriations and year-end balance	$7,611,220	$425,000	$4,155,196	$12,191,416

(1) Does not include grants received by agencies whose accounting systems are not centralized in the Department of the Treasury.

Sources: Department of the Treasury and Office of Management and Budget as reported on March 29, 2001

In the fiscal 2001 budget proposal, revenues and other resources of all budgetary funds total $11,312,169,000 excluding balances from the previous fiscal year and general obligation bonds authorized. The estimated net increase in General Fund revenues in fiscal 2001 is accounted for by increases in personal income taxes (up $215,934,000), corporation income taxes (up $14,138,000), Federal excise taxes on off-shore shipments (up $45,250,000), general excise tax of 5% (up $73,438,000), excise tax on motor vehicles and accessories (up $51,005,000), special excise tax on certain petroleum products (up $45,214,000), registration and documentation fees (up $21,144,000), excise tax on alcoholic beverages (up $21,626,000), and decreases in tollgate taxes (down $17,130,000) and income tax withheld from non-residents (down $32,276,000).

Current expenses and capital improvements of all budgetary funds total $11,800,543,000, an increase of $760,761,000 from fiscal 2000. The major changes in General Fund expenditures by program are: increases in education (up $240,844,000), general government (up $129,339,000), public safety and protection (up $95,263,000), health (up $55,602,000), debt service (up $36,874,000), other debts (up $30,460,000), contributions to municipalities (up $6,567,000), special pension contributions (up $6,908,000), housing (up $1,306,000), and decreases in transportation and communications (down $5,294,000), welfare (down $6,257,000), and economic development (down $43,481,000).

General Fund Revenues were budgeted at $7,611 million, including an $106 million balance from the previous year. Revenues are currently estimated at $7,301 million (including such beginning balance). General Fund Expenditures were budgeted at $7,611 million. Expenditures are currently estimated at $7,742 million. The difference in current estimated Revenues and Expenditures of approximately $441 million will be covered by: (i) measures taken by OMB to reduce expenditures and apply available surpluses which together are estimated at $167 million, (ii) the financing of certain deposits to the Redemption Fund in the amount of approximately $164 million, and (iii) the balance will be funded with loans from GDB.

The general obligation bond authorization for the fiscal 2001 budget was $425,000,000.

Proposed Fiscal 2002 Budget

The following table presents a summary of the proposed Commonwealth budget for the fiscal year ending June 30, 2002:

Commonwealth of Puerto Rico

Summary of Central Government Annual Budget
Fiscal Year Ending June 30, 2002
(in thousands)

	General Fund	Bond Fund	Special Funds	Total
Revenues from internal sources:				
Property taxes	$ -	$ -	$ 104,412	$ 104,412
Personal income taxes	2,749,000	-	-	2,749,000
Income tax withheld from non-residents	670,000	-	-	670,000
Corporation income taxes	1,660,000	-	-	1,660,000
Partnership income taxes	3,000	-	-	3,000
Tollgate taxes	36,000	-	-	36,000
17% withholding tax on interest	15,000	-	-	15,000
10% withholding tax on dividends	41,000	-	-	41,000
Inheritance and gift taxes	3,000	-	-	3,000
Excise taxes:				
Alcoholic beverages	245,000	-	-	245,000
Motor vehicles and accessories	417,000	-	-	417,000
Cigarettes	119,000	-	-	119,000
Special excise tax on certain petroleum products	50,000	-	-	50,000
General 5% excise tax	591,000	-	-	591,000
Slot machines and machines for entertainment	-	-	-	-
Other	77,000	-	126,320	203,320
Licenses	79,000	-	-	79,000
Miscellaneous non-tax revenues:				
Contributions from lottery fund	56,000	-	-	56,000
Electronic lottery	61,000	-	-	61,000
Registration and document certification fees	143,000	-	-	143,000
Other	70,000	-	212,566	282,566
Total revenues from internal sources	7,085,000	-	443,298	7,528,298
Revenues from non-Commonwealth sources:				
Federal excise taxes on off-shore shipments	280,000	-	-	280,000
Federal grants	-	-	3,416,511[1]	3,416,511
Customs	40,000	-	-	40,000
Total revenues from non-Commonwealth sources	320,000	-	3,416,511	3,736,511
Total revenues	7,405,000	-	3,859,809	11,264,809
Other:				
Other Income	258,554	-	-	258,554
Balance from previous year	378	-	390,495	390,873
Bonds authorized	-	465,000	-	465,000
Total other sources	258,932	465,000	390,495	1,114,427
Total resources	7,663,932	465,000	4,250,304	12,379,236

	General Fund	Bond Fund	Special Funds	Total
Appropriations:				
Current expenses:				
General government	938,477	-	55,986	994,463
Education	2,366,594	-	819,428	3,186,022
Health	1,030,174	-	335,710	1,365,884
Welfare	377,315	-	2,092,769	2,470,084
Economic development	187,581	-	64,949	252,530
Public safety and protection	1,313,246	-	53,915	1,367,161
Transportation and communications	72,346	-	14,948	87,294
Housing	20,716	-	122,046	142,762
Contributions to municipalities	345,884	-	2,095	347,979
Special pension contributions	50,181	-	-	50,181
Debt service	476,636	-	104,412	581,048
Other debt service	484,404	-	19,000	503,404
Total appropriations-current expenses	7,663,554	-	3,685,258	11,348,812
Capital improvements	-	465,000	165,019	630,019
Total appropriations	7,663,554	465,000	3,850,277	11,978,831
Year-end balance	378	-	400,027	400,405
Total appropriations and year-end balance	$7,663,932	$465,000	$4,250,304	$12,379,236

(1) Does not include grants received by agencies whose accounting systems are not centralized in the Department of Treasury.

Sources: Department of the Treasury and Office of Management and Budget as reported on March 29, 2001

In the fiscal 2002 budget proposal, revenues and other resources of all budgetary funds total $11,523,363,000, excluding balances from the previous fiscal year and general obligation bonds authorized. The estimated net increase in General Fund revenues in fiscal 2002 is accounted for principally by increases in retained non-resident income tax (up $145,000,000), personal income taxes (up $20,000,000), interest subject to 17% (up $2,000,000), licenses (up $1,000,000), and decreases in electronic lottery revenues (down $2,000,000), contributions from lottery fund (down $2,000,000), general excise of 5% (down $8,000,000), federal excise taxes on off-shore shipments (down $11,000,000), excise tax on alcoholic beverages (down $13,000,000), customs (down $18,000,000), special excise tax on certain petroleum products (down $20,000,000), motor vehicles and accessories (down $24,000,000), tollgate taxes (down $58,000,000), and corporation income taxes (down $107,000,000).

Current expenses and capital improvements of all budgetary funds total $11,978,831,000, an increase of $178,288,000 from fiscal 2001. The major changes in General Fund expenditures by program in fiscal 2001 are: general government (up $96,940,000), public safety and protection (up $48,634,000), other debts (up $47,819,000), contributions to municipalities (up $45,504,000), debt service (up $29,716,000), education (up $29,109,000), economic development (up $16,430,000), special pension contributions (up $3,771,000) and decreases in transportation and communications (down $100,000), housing (down $176,000), welfare (down $5,492,000) and health (down $233,528,000).

The general obligation bond authorization proposed for the fiscal 2002 budget is $465,000,000.

Differences between Budget and General Purpose Financial Statements

Revenues and expenditures, as reported by the Department of the Treasury in its General Purpose 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 the financial statements prepared by the Department of the Treasury 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 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 amount of bonds sold in any year does not necessarily equal the amount of bonds authorized in the budget for that year. Expenditures for capital improvements are financed by advances from the General Fund to the Capital Projects Fund, which are later reimbursed from proceeds of bond or note sales.

LITIGATION

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 the Legislature of Puerto Rico, approved on June 25, 1955, as amended ("Act No. 104"), persons are authorized to sue the Commonwealth only for causes of actions specified in said Act. The Commonwealth may be liable under Act No. 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 the Legislature of Puerto Rico, approved on November 26, 1975, as amended ("Act No. 9"), 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 Act No. 9.

With respect to pending and threatened litigation, as of June 30, 2000, the Commonwealth included in its financial statements reported liabilities of approximately $350 million for awarded and anticipated unfavorable judgments. This amount represented 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. This amount includes approximately $200 million of accrued liabilities related to the fines described below. The Commonwealth believes that the ultimate liability in excess of amounts provided in the financial statements, if any, would not be significant.

The Commonwealth is a defendant in approximately three hundred related lawsuits in which the plaintiffs allege a torts claim and violation of their civil rights in connection with the preparation by the government of dossiers on certain individuals. The lawsuits are still in the discovery stage. A petition to certify these claims as a class action has been denied, and such denial has become final. The aggregate amount of damages claimed by the plaintiffs exceeds $50 billion. The Commonwealth has accepted liability for the claims without renouncing the limitations, immunities and defenses available to it under Act No. 104. The Commonwealth believes that the amount of damages claimed is exaggerated and that the outcome of this litigation will not materially affect the revenues and expenditures of the Commonwealth. The Commonwealth's financial statements for the fiscal year, which ended June 30, 2000, did not include any provision for liability with respect to these lawsuits.

Several officers of the Commonwealth are defendants in a class action lawsuit filed in 1979 in the United States District Court for the District of Puerto Rico by various inmates who alleged that their constitutional rights were being violated because of overcrowding and lack of adequate healthcare in the island's correctional system. In 1980, the United States District Court issued a preliminary injunction and required the defendants to provide additional capacity for the cells of the correctional facilities and to improve the healthcare services available to inmates. Fines in the amount of $280 million have been assessed against the defendants in order to assure compliance with the space and healthcare requirements imposed by the United States District Court. Of the fines imposed, $150 million have already been paid by the Commonwealth.

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June __, 2001

Hon. Juan A. Flores
Secretary of the Treasury of Puerto Rico
San Juan, Puerto Rico

Dear Sir:

We have examined Act. No. 118 of the Legislature of Puerto Rico, approved July 13, 2000 (the "Act"), and certified copies of the legal proceedings, including a resolution adopted by the Secretary of the Treasury of the Commonwealth of Puerto Rico and approved by the Governor of the Commonwealth of Puerto Rico (the "Resolution"), and other proofs submitted relative to the issuance and sale of the following described bonds (the "Bonds"):

$410,970,000
COMMONWEALTH OF PUERTO RICO

PUBLIC IMPROVEMENT BONDS OF 2001

Dated: Date of Delivery.

Maturing on July 1 of the years and in such principal amounts, subject to redemption and bearing interest at the rates, all as set forth in the Resolution. The Bonds are issuable as registered Bonds without coupons in the manner and in accordance with the terms and conditions of the Resolution.

We have also examined one of the Bonds as executed and authenticated.

From such examination we are of the opinion that:

1. The Act is valid.

2. Said proceedings have been validly and legally taken.

3. The Act and said proceedings and proofs show lawful authority for the issuance and sale of the Bonds, and the Bonds constitute valid and binding general obligations of the Commonwealth of Puerto Rico for the prompt payment of the principal of and the interest on which the good faith, credit and taxing power of the Commonwealth of Puerto Rico are pledged.

4. Under the provisions of the Acts of Congress now in force and under existing regulations, rulings and court decisions, (i) subject to continuing compliance with the covenant referred to below and requirements of the Internal Revenue Code of 1986, as amended (the "Code"), and the Resolution regarding the use, expenditure and investment of Bond proceeds and the timely payment of certain investment earnings to the Treasury of the United States, if required, interest on the Bonds is not includable in gross income for federal income tax purposes; and (ii) the Bonds and the interest thereon are exempt from state, Commonwealth of Puerto Rico and local income taxation. No opinion is rendered, however, as to the exclusion from gross income of the interest on the Bonds for federal income tax purposes on or after the date on which any action is taken under the Resolution or any instrument relating to the Bonds upon the approval of counsel other than our firm.

Interest on the Bonds is not a specific item of tax preference for the purpose of computing the alternative minimum tax on individuals and corporations imposed by the Code. Such interest, however, is includable in the computation of the alternative minimum tax on corporations imposed by the Code. The Code contains other provisions that could result in tax consequences, upon which we express no opinion, as a result of (a) ownership of Bonds or (b) the inclusion in certain computations (including, without limitation, those related to the corporate alternate minimum tax) of interest that is excluded from gross income.

The Commonwealth of Puerto Rico has covenanted to comply, to the extent permitted by the Constitution and laws of the Commonwealth of Puerto Rico, with the requirements of the Code so that interest on the Bonds will remain exempt from federal income taxes to which it is not subject on the date of issuance of the Bonds. We are not aware of any provisions of the Constitution or laws of the Commonwealth of Puerto Rico which would prevent the Commonwealth of Puerto Rico from complying with the requirements of the Code.

Respectfully submitted,

[To be signed "Sidley Austin Brown & Wood LLP"]

SIDLEY AUSTIN BROWN & WOOD LLP

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June__, 2001

Hon. Juan A. Flores
Secretary of the Treasury of Puerto Rico
San Juan, Puerto Rico

Dear Sir:

We have examined Act. No. 33 of the Legislature of Puerto Rico, approved December 7, 1942 (the "Act"), and certified copies of the legal proceedings, including a resolution adopted by the Secretary of the Treasury of the Commonwealth of Puerto Rico and approved by the Governor of the Commonwealth of Puerto Rico (the "Resolution"), and other proofs submitted relative to the issuance and sale of the following described bonds (the "Bonds"):

$337,235,000
COMMONWEALTH OF PUERTO RICO

PUBLIC IMPROVEMENT REFUNDING BONDS, SERIES 2001

Dated: Date of Delivery.

Maturing on July 1 of the years and in such principal amounts, subject to redemption and bearing interest at the rates, all as set forth in the Resolution. The Bonds are issuable as registered Bonds without coupons in the manner and in accordance with the terms and conditions of the Resolution and are not subject to redemption prior to maturity.

We have also examined one of the Bonds as executed and authenticated.

From such examination we are of the opinion that:

1. The Act is valid.

2. Said proceedings have been validly and legally taken.

3. The Act and said proceedings and proofs show lawful authority for the issuance and sale of the Bonds, and the Bonds constitute valid and binding general obligations of the Commonwealth of Puerto Rico for the payment of the principal of and the interest on which the good faith, credit and taxing power of the Commonwealth of Puerto Rico are pledged.

4. Under the provisions of the Acts of Congress now in force and under existing regulations and judicial decisions, (i) subject to continuing compliance with the covenant referred to below and requirements of the Internal Revenue Code of 1986, as amended (the "Code"), and the Resolution regarding the use, expenditure and investment of Bond proceeds and the timely payment of certain investment earnings to the Treasury of the United States, if required, interest on the Bonds is not includable in gross income for federal income tax purposes; and (ii) the Bonds and the interest thereon are exempt from state, Commonwealth of Puerto Rico and local income taxation. No opinion is rendered, however, as to the exclusion from gross income of the interest on the Bonds for federal income tax purposes on or after the date on which any action is taken under the Resolution or any instrument relating to the Bonds upon the approval of counsel other than our firm.

Interest on the Bonds is not a specific item of tax preference for the purpose of computing the alternative minimum tax on individuals and corporations imposed by the Code. Such interest, however, is includable in the computation of the alternative minimum tax on corporations imposed by the Code. The Code contains other provisions that could result in tax consequences, upon which we express no opinion, as a result of (a) ownership of Bonds or (b) the inclusion in certain computations (including, without limitation, those related to the corporate alternate minimum tax) of interest that is excluded from gross income.

The Commonwealth of Puerto Rico has covenanted to comply, to the extent permitted by the Constitution and laws of the Commonwealth of Puerto Rico, with the requirements of the Code so that interest on the Bonds will remain exempt from federal income taxes to which it is not subject on the date of issuance of the Bonds. We are not aware of any provisions of the Constitution or laws of the Commonwealth of Puerto Rico which would prevent the Commonwealth of Puerto Rico from complying with the requirements of the Code.

Respectfully submitted,

[To be signed "Sidley Austin Brown & Wood LLP"]

SIDLEY AUSTIN BROWN & WOOD LLP

CHICAGO
DALLAS
LOS ANGELES
SAN FRANCISCO
SEATTLE
WASHINGTON, D.C.

ONE WORLD TRADE CENTER
NEW YORK, NEW YORK 10048-0557
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FACSIMILE 212 839 5599
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FOUNDED 1866

BEIJING
HONG KONG
LONDON
SHANGHAI
SINGAPORE
TOKYO

April __, 2002

Hon. Juan A. Flores
Secretary of the Treasury of Puerto Rico
San Juan, Puerto Rico

Dear Sir:

We have examined Act. No. 33 of the Legislature of Puerto Rico, approved December 7, 1942 (the "Act"), and certified copies of the legal proceedings, including a resolution adopted by the Secretary of the Treasury of the Commonwealth of Puerto Rico and approved by the Governor of the Commonwealth of Puerto Rico (the "Resolution"), and other proofs submitted relative to the issuance and sale of the following described bonds (the "Bonds"):

$501,565,000
COMMONWEALTH OF PUERTO RICO

PUBLIC IMPROVEMENT REFUNDING BONDS, SERIES 2002

Dated: Date of Delivery.

Maturing on July 1 of the years and in such principal amounts, subject to redemption and bearing interest at the rates, all as set forth in the Resolution. The Bonds are issuable as registered Bonds without coupons in the manner and in accordance with the terms and conditions of the Resolution and are not subject to redemption prior to maturity.

We have also examined one of the Bonds as executed and authenticated.

From such examination we are of the opinion that:

1. The Act is valid.

2. Said proceedings have been validly and legally taken.

3. The Act and said proceedings and proofs show lawful authority for the issuance and sale of the Bonds, and the Bonds constitute valid and binding general obligations of the Commonwealth of Puerto Rico for the payment of the principal of and the interest on which the good faith, credit and taxing power of the Commonwealth of Puerto Rico are pledged.

4. Under the provisions of the Acts of Congress now in force and under existing regulations and judicial decisions, (i) subject to continuing compliance with the covenant referred to below and requirements of the Internal Revenue Code of 1986, as amended (the "Code"), and the Resolution regarding the use, expenditure and investment of Bond proceeds and the timely payment of certain investment earnings to the Treasury of the United States, if required, interest on the Bonds is not includable in gross income for federal income tax purposes; and (ii) the Bonds and the interest thereon are exempt from state, Commonwealth of Puerto Rico and local income taxation. No opinion is rendered, however, as to the exclusion from gross income of the interest on the Bonds for federal income tax purposes on or after the date on which any action is taken under the Resolution or any instrument relating to the Bonds upon the approval of counsel other than our firm.

Interest on the Bonds is not a specific item of tax preference for the purpose of computing the alternative minimum tax on individuals and corporations imposed by the Code. Such interest, however, is includable in the computation of the alternative minimum tax on corporations imposed by the Code. The Code contains other provisions that could result in tax consequences, upon which we express no opinion, as a result of (a) ownership of Bonds or (b) the inclusion in certain computations (including, without limitation, those related to the corporate alternate minimum tax) of interest that is excluded from gross income.

The Commonwealth of Puerto Rico has covenanted to comply, to the extent permitted by the Constitution and laws of the Commonwealth of Puerto Rico, with the requirements of the Code so that interest on the Bonds will remain exempt from federal income taxes to which it is not subject on the date of issuance of the Bonds. We are not aware of any provisions of the Constitution or laws of the Commonwealth of Puerto Rico which would prevent the Commonwealth of Puerto Rico from complying with the requirements of the Code.

Respectfully submitted,

[To be signed "Sidley Austin Brown & Wood LLP"]

FINANCIAL SECURITY ASSURANCE®

MUNICIPAL BOND INSURANCE POLICY

SPECIMEN

ISSUER:

BONDS:

Policy No.: -N

Effective Date:

Premium: $

FINANCIAL SECURITY ASSURANCE INC. ("Financial Security"), for consideration received, hereby UNCONDITIONALLY AND IRREVOCABLY agrees to pay to the trustee (the "Trustee") or paying agent (the "Paying Agent") (as set forth in the documentation providing for the issuance of and securing the Bonds) for the Bonds, for the benefit of the Owners or, at the election of Financial Security, directly to each Owner, subject only to the terms of this Policy (which includes each endorsement hereto), that portion of the principal of and interest on the Bonds that shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer.

On the later of the day on which such principal and interest becomes Due for Payment or the Business Day next following the Business Day on which Financial Security shall have received Notice of Nonpayment, Financial Security will disburse to or for the benefit of each Owner of a Bond the face amount of principal of and interest on the Bond that is then Due for Payment but is then unpaid by reason of Nonpayment by the Issuer, but only upon receipt by Financial Security, in a form reasonably satisfactory to it, of (a) evidence of the Owner's right to receive payment of the principal or interest then Due for Payment and (b) evidence, including any appropriate instruments of assignment, that all of the Owner's rights with respect to payment of such principal or interest that is Due for Payment shall thereupon vest in Financial Security. A Notice of Nonpayment will be deemed received on a given Business Day if it is received prior to 1:00 p.m. (New York time) on such Business Day; otherwise, it will be deemed received on the next Business Day. If any Notice of Nonpayment received by Financial Security is incomplete, it shall be deemed not to have been received by Financial Security for purposes of the preceding sentence and Financial Security shall promptly so advise the Trustee, Paying Agent or Owner, as appropriate, who may submit an amended Notice of Nonpayment. Upon disbursement in respect of a Bond, Financial Security shall become the owner of the Bond, any appurtenant coupon to the Bond or right to receipt of payment of principal of or interest on the Bond and shall be fully subrogated to the rights of the Owner, including the Owner's right to receive payments under the Bond, to the extent of any payment by Financial Security hereunder. Payment by Financial Security to the Trustee or Paying Agent for the benefit of the Owners shall, to the extent thereof, discharge the obligation of Financial Security under this Policy.

Except to the extent expressly modified by an endorsement hereto, the following terms shall have the meanings specified for all purposes of this Policy. "Business Day" means any day other than (a) a Saturday or Sunday or (b) a day on which banking institutions in the State of New York or the Insurer's Fiscal Agent are authorized or required by law or executive order to remain closed. "Due for Payment" means (a) when referring to the principal of a Bond, payable on the stated maturity date thereof or the date on which the same shall have been duly called for mandatory sinking fund redemption and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by mandatory sinking fund redemption), acceleration or other advancement of maturity unless Financial Security shall elect, in its sole discretion, to pay such principal due upon such acceleration together with any accrued interest to the date of acceleration and (b) when referring to interest on a Bond, payable on the stated date for payment of interest. "Nonpayment" means, in respect of a Bond, the failure of the Issuer to have provided sufficient funds to the Trustee or, if there is no Trustee, to the Paying Agent for payment in full of all principal and interest that is Due for Payment on such Bond. "Nonpayment" shall also include, in respect of a Bond, any payment of principal or interest that is Due for Payment made to an Owner by or on behalf of the Issuer which has been recovered from such Owner pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction. "Notice" means telephonic or telecopied notice, subsequently confirmed in a signed writing, or written notice by registered or certified mail, from an Owner, the Trustee or the Paying Agent to Financial Security which notice shall specify (a) the person or entity making the claim, (b) the Policy Number, (c) the claimed amount and (d) the date such claimed amount became Due for Payment. "Owner" means, in respect of a Bond, the person or entity who, at the time of Nonpayment, is entitled under the terms of such Bond to payment thereof, except that "Owner" shall not include the Issuer or any person or entity whose direct or indirect obligation constitutes the underlying security for the Bonds.

Financial Security may appoint a fiscal agent (the "Insurer's Fiscal Agent") for purposes of this Policy by giving written notice to the Trustee and the Paying Agent specifying the name and notice address of the Insurer's Fiscal Agent. From and after the date of receipt of such notice by the Trustee and the Paying Agent, (a) copies of all notices required to be delivered to Financial Security pursuant to this Policy shall be simultaneously delivered to the Insurer's Fiscal Agent and to Financial Security and shall not be deemed received until received by both and (b) all payments required to be made by Financial Security under this Policy may be made directly by Financial Security or by the Insurer's Fiscal Agent on behalf of Financial Security. The Insurer's Fiscal Agent is the agent of Financial Security only and the Insurer's Fiscal Agent shall in no event be liable to any Owner for any act of the Insurer's Fiscal Agent or any failure of Financial Security to deposit or cause to be deposited sufficient funds to make payments due under this Policy.

To the fullest extent permitted by applicable law, Financial Security agrees not to assert, and hereby waives, only for the benefit of each Owner, all rights (whether by counterclaim, setoff or otherwise) and defenses (including, without limitation, the defense of fraud), whether acquired by subrogation, assignment or otherwise, to the extent that such rights and defenses may be available to Financial Security to avoid payment of its obligations under this Policy in accordance with the express provisions of this Policy.

This Policy sets forth in full the undertaking of Financial Security, and shall not be modified, altered or affected by any other agreement or instrument, including any modification or amendment thereto. Except to the extent expressly modified by an endorsement hereto, (a) any premium paid in respect of this Policy is nonrefundable for any reason whatsoever, including payment, or provision being made for payment, of the Bonds prior to maturity and (b) this Policy may not be canceled or revoked. THIS POLICY IS NOT COVERED BY THE PROPERTY/CASUALTY INSURANCE SECURITY FUND SPECIFIED IN ARTICLE 76 OF THE NEW YORK INSURANCE LAW.

In witness whereof, FINANCIAL SECURITY ASSURANCE INC. has caused this Policy to be executed on its behalf by its Authorized Officer.

[Countersignature]

By ______________________________

FINANCIAL SECURITY ASSURANCE INC.

By ______________________________
Authorized Officer

A subsidiary of Financial Security Assurance Holdings Ltd.
350 Park Avenue, New York, N.Y. 10022-6022
(212) 826-0100

Financial Guaranty Insurance Company
115 Broadway
New York, NY 10006
(212) 312-3000
(800) 352-0001

A GE Capital Company

FGIC

APPENDIX IV

Municipal Bond
New Issue Insurance Policy

Issuer:

Policy Number:

Control Number: 0010001

Bonds:

Premium:

Financial Guaranty Insurance Company ("Financial Guaranty"), a New York stock insurance company, in consideration of the payment of the premium and subject to the terms of this Policy, hereby unconditionally and irrevocably agrees to pay to State Street Bank and Trust Company, N.A., or its successor, as its agent (the "Fiscal Agent"), for the benefit of Bondholders, that portion of the principal and interest on the above-described debt obligations (the "Bonds") which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Issuer.

Financial Guaranty will make such payments to the Fiscal Agent on the date such principal or interest becomes Due for Payment or on the Business Day next following the day on which Financial Guaranty shall have received Notice of Nonpayment, whichever is later. The Fiscal Agent will disburse to the Bondholder the face amount of principal and interest which is then Due for Payment but is unpaid by reason of Nonpayment by the Issuer but only upon receipt by the Fiscal Agent, in form reasonably satisfactory to it, of (i) evidence of the Bondholder's right to receive payment of the principal or interest Due for Payment and (ii) evidence, including any appropriate instruments of assignment, that all of the Bondholder's rights to payment of such principal or interest Due for Payment shall thereupon vest in Financial Guaranty. Upon such disbursement, Financial Guaranty shall become the owner of the Bond, appurtenant coupon or right to payment of principal or interest on such Bond and shall be fully subrogated to all of the Bondholder's rights thereunder, including the Bondholder's right to payment thereof.

This Policy is non-cancellable for any reason. The premium on this Policy is not refundable for any reason, including the payment of the Bonds prior to their maturity. This Policy does not insure against loss of any prepayment premium which may at any time be payable with respect to any Bond.

As used herein, the term "Bondholder" means, as to a particular Bond, the person other than the Issuer who, at the time of Nonpayment, is entitled under the terms of such Bond to payment thereof. "Due for Payment" means, when referring to the principal of a Bond, the stated maturity date thereof or the date on which the same shall have been duly called for mandatory sinking fund redemption and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by mandatory sinking fund redemption), acceleration or other advancement of maturity and means, when referring to interest on a Bond, the stated date

Financial Guaranty Insurance
Company
115 Broadway
New York, NY 10006
(212) 312-3000
(800) 352-0001

A GE Capital Company

FGIC.

Municipal Bond
New Issue Insurance Policy

for payment of interest. "Nonpayment" in respect of a Bond means the failure of the Issuer to have provided sufficient funds to the paying agent for payment in full of all principal and interest Due for Payment on such Bond. "Notice" means telephonic or telegraphic notice, subsequently confirmed in writing, or written notice by registered or certified mail, from a Bondholder or a paying agent for the Bonds to Financial Guaranty. "Business Day" means any day other than a Saturday, Sunday or a day on which the Fiscal Agent is authorized by law to remain closed.

In Witness Whereof, Financial Guaranty has caused this Policy to be affixed with its corporate seal and to be signed by its duly authorized officer in facsimile to become effective and binding upon Financial Guaranty by virtue of the countersignature of its duly authorized representative.

Deborah M. Reif

President

Effective Date: **Authorized Representative**

State Street Bank and Trust Company, N.A., acknowledges that it has agreed to perform the duties of Fiscal Agent under this Policy.

Authorized Officer

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