

**Supplement, dated December 21, 2007, to Official Statement  
dated December 7, 2007, relating to:**

**\$895,290,000**

**PUERTO RICO PUBLIC BUILDINGS AUTHORITY**

**\$562,850,000 Government Facilities Revenue Refunding Bonds, Series M**

**\$329,415,000 Government Facilities Revenue Bonds, Series N**

**\$3,025,000 Government Facilities Revenue Bonds, Series O**

**Guaranteed by the Commonwealth of Puerto Rico**

Please note the following changes to the Official Statement dated December 7, 2007, relating to the above bonds (all terms used below having the same meanings given to such terms in the Official Statement dated December 7, 2007):

After the first full paragraph under the heading *Ratings* on **page 51** of said Official Statement, the following paragraph is added: "On December 14, 2007, Moody's affirmed its Aaa rating for MBIA and changed its outlook for MBIA to Negative from Stable. Also on such date, Moody's affirmed its Aaa rating for Ambac Assurance and its rating outlook of Stable. On December 19, 2007, S&P affirmed its AAA rating for each of MBIA and Ambac Assurance and changed its outlook for each of MBIA and Ambac Assurance to Negative from Stable."

This Supplement will be filed with each NRMSIR and with the MSRB.

**PUERTO RICO PUBLIC BUILDINGS AUTHORITY**

By: /s/ Leila Hernández Umpierre

Leila Hernández Umpierre

Executive Director

Dated: December 21, 2007

**NEW ISSUE - BOOK-ENTRY ONLY**

*In the opinion of Squire, Sanders & Dempsey L.L.P, Bond Counsel, under existing law, (i) assuming continuing compliance by the Puerto Rico Public Buildings Authority with certain covenants and the accuracy of certain representations, interest on the Series M Bonds and the Series N Bonds is excluded from gross income for federal income tax purposes and is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations, and (ii) the Series M Bonds and the Series N Bonds and the interest thereon are exempt from state, Commonwealth of Puerto Rico, and local income taxation. Interest on the Series M Bonds and the Series N Bonds may be subject to certain federal taxes imposed only on certain corporations, including the corporate alternative minimum tax on a portion of that interest.*

*In the opinion of Quiñones & Sánchez PSC, Special Tax Counsel, as described herein, interest on the Series O Bonds is not excludable from gross income for federal income tax purposes under Section 103 of the United States Internal Revenue Code. Under existing statutes, the Series O Bonds, and the interest thereon, are exempt from Commonwealth of Puerto Rico taxation. Under most circumstances, interest on the Series O Bonds is exempt from United States income taxation to residents of Puerto Rico. For a more complete discussion of the tax aspects, see the discussion under Tax Matters herein.*

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**PUERTO RICO PUBLIC BUILDINGS AUTHORITY**

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**\$3,025,000 Government Facilities Revenue Bonds, Series O**

**Guaranteed by the Commonwealth of Puerto Rico**

**Dated: Date of Delivery**

**Due: As shown in the inside cover page**

The Puerto Rico Public Buildings Authority Government Facilities Revenue Refunding Bonds, Series M, Guaranteed by the Commonwealth of Puerto Rico (the "Series M Bonds"); the Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds, Series N, Guaranteed by the Commonwealth of Puerto Rico (the "Series N Bonds"); and the Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds, Series O, Guaranteed by the Commonwealth of Puerto Rico (the "Series O Bonds") and, together with the Series M Bonds and the Series N Bonds, collectively referred to as the "Bonds") will be issued in fully registered form and when issued, will be initially registered only in the name of Cede & Co., as nominee of The Depository Trust Company ("DTC"), New York, New York, which will act as securities depository for the Bonds. The Puerto Rico Public Buildings Authority (the "Authority") will issue the Series M Bonds in three separate subseries, with the first such subseries bearing interest at fixed annual rates to their stated maturities or earlier redemption (subseries M-1 as listed in the inside cover page of this Official Statement; the "Series M-1 Bonds"), the second such subseries bearing interest at fixed annual rates up to and including June 30, 2017, and thereafter being subject to mandatory tender for purchase (subseries M-2 as listed in the inside cover page of this Official Statement; the "Series M-2 Bonds"), and the third such subseries having interest rates that will be periodically reset by a remarketing agent (subseries M-3 as listed in the inside cover page of this Official Statement; the "Series M-3 Bonds"), all as more specifically described herein. The Bonds, other than the Series M-3 Bonds, will be initially available to purchasers in denominations of \$5,000 and any multiple thereof only under the book-entry system maintained by DTC through brokers and dealers who are, or act through, DTC Participants (as such term is defined herein). The Series M-3 Bonds will be initially available to purchasers in denominations of \$100,000 or any integral multiple of \$5,000 in excess thereof only under the book-entry system maintained by DTC through brokers and dealers who are, or act through, DTC Participants. **Purchasers will not receive delivery of the Bonds. So long as any purchaser is the beneficial owner of a Bond, such purchaser must maintain an account with a broker or dealer who is, or acts through, a DTC Participant to receive payment of principal of and interest on such Bond.** See "Book-Entry Only System" under *Description of the Bonds* herein. Interest on the Bonds will accrue from their date of issuance at the annual rates set forth or described in the inside cover page of this Official Statement. Interest on the Bonds, other than the Series M-3 Bonds, will be payable each January 1 and July 1 until repayment (or, with respect to the Series M-2 Bonds, until conversion to another Interest Rate Period at the end of the Initial Term Rate Period (as such terms are defined herein)), commencing on July 1, 2008. Interest on the Series M-3 Bonds will be payable the first Business Day of each calendar month, commencing on January 1, 2008. Certain Bonds will be subject to redemption prior to maturity and mandatory tender for purchase as described herein.

All outstanding Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds and Puerto Rico Public Buildings Authority Government Facilities Revenue Refunding Bonds, as well as the Bonds and any additional Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds and Revenue Refunding Bonds hereafter issued under the 1995 Bond Resolution (all of the foregoing, collectively, "Government Facilities Bonds"), will be secured equally and ratably by a pledge of the rentals of government facilities financed or refinanced by such bonds and leased by the Authority to departments, agencies, instrumentalities and municipalities of the Commonwealth of Puerto Rico (the "Leased Facilities"). The Leased Facilities will not be mortgaged or otherwise encumbered to secure any Government Facilities Bonds. The good faith and credit of the Commonwealth of Puerto Rico (the "Commonwealth" or "Puerto Rico") are pledged to the payment or advance of such rentals.

**The Bonds are further secured by the guaranty of the Commonwealth, under which the Commonwealth pledges to draw from any funds available in the Treasury of Puerto Rico such sums as may be necessary to cover any deficiency in the amount required for the payment of principal of and interest on the Bonds. The good faith and credit of the Commonwealth, as in the case of the Commonwealth's general obligation bonds, are pledged for such payments.**

The scheduled payment of principal of and interest on the Series M-2 Bonds maturing on July 1, 2035 will be guaranteed by Ambac Assurance Corporation, as further described herein. The scheduled payment of principal of and interest on the Series M-3 Bonds will be guaranteed by MBIA Insurance Corporation, as further described herein. See *Bond Insurance* herein.

In connection with the issuance of the Series M-3 Bonds, JPMorgan Chase Bank, National Association has agreed to purchase Series M-3 Bonds that are tendered and not remarketed, except under certain circumstances described herein, under a Standby Bond Purchase Agreement, with the Authority, which agreement will expire, subject to earlier termination under certain circumstances or extension, prior to the final maturity of said Series M-3 Bonds. **As more fully described herein, the rights of the owners of Series M-3 Bonds to tender their Series M-3 Bonds may be immediately terminated or suspended without notice to any person or without mandatory tender of the Series M-3 Bonds.**

*The Bonds are offered for delivery, subject to prior sale, when, as, and if issued by the Authority and accepted by the Underwriters subject to the approval of legality by Squire, Sanders & Dempsey L.L.P, Miami, Florida, Bond Counsel, and certain other conditions. Certain legal matters will be passed upon by Quiñones & Sánchez PSC, San Juan, Puerto Rico, Underwriters' Counsel and Special Tax Counsel. It is expected that the Bonds will be available for delivery to DTC in New York, New York on or about December 20, 2007.*

**Lehman Brothers**

**Bear, Stearns & Co., Inc.  
Banc of America Securities LLC  
DEPFA First Albany Securities, LLC  
Loop Capital  
Oriental Financial Services  
Santander Securities  
UBS Investment Bank**

**BBVAPR MSD  
Goldman, Sachs & Co.  
Merrill Lynch & Co.  
Popular Securities  
Scotia Capital**

**RBC Capital Markets  
Citi  
JPMorgan  
Morgan Stanley  
Samuel A. Ramírez & Co., Inc.  
TCM Capital  
Wachovia Capital Markets, LLC**

## MATURITY SCHEDULE

**\$562,850,000**

### **Government Facilities Revenue Refunding Bonds, Series M**

#### **Subseries M-1**

<u>Maturity</u> <u>July 1</u>	<u>Amount</u>	<u>Interest Rate</u>	<u>Yield</u>	<u>CUSIP</u>
2009	\$ 7,480,000	5.25%	3.68%	745235ZC8
2010	10,950,000	5.50	3.80	745235ZD6
2011	11,550,000	5.50	3.89	745235ZE4
2012	12,180,000	5.50	4.00	745235ZF1
2013	16,235,000	5.50	4.10	745235ZG9
2014	17,130,000	5.75	4.18	745235ZH7
2015	18,115,000	5.75	4.25	745235ZJ3
2016	19,155,000	5.75	4.33	745235ZK0
2017	20,260,000	5.75	4.41	745235ZL8
2018	940,000	5.00	4.51	745235ZM6
2019	3,060,000	5.50	4.59	745235ZN4
2020	12,545,000	6.00	4.68	745235ZP9
2021	19,230,000	6.25	4.75	745235ZQ7
2022	27,085,000	6.25	4.81	745235ZR5
2023	21,385,000	6.25	4.87	745235ZS3

\$66,250,000, 6.25% Term Bonds, due July 1, 2031, Yield 5.12%, CUSIP 745235ZT1

#### **Subseries M-2**

\$69,300,000, 5.75% Term Bonds<sup>1</sup>, due July 1, 2034, Yield 4.62%\*, CUSIP 745235B67

\$60,000,000, 5.50% Term Bonds<sup>2</sup>, due July 1, 2035, Yield 4.20%\*, CUSIP 745235B75

#### **Subseries M-3**

\$150,000,000 Term Bonds<sup>3</sup>, due July 1, 2028, Price 100.00%, CUSIP 745235B83

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\* Priced to July 1, 2017 mandatory tender date.

1 Will bear interest at the rate of 5.75% to and including June 30, 2017, at which time will be subject to mandatory tender for purchase. Subsequent to the Initial Term Rate Period, will be Variable Rate Bonds and will bear interest at the rates and shall have such other terms and provisions as set forth in the Series Resolution and as described in *Description of the Bonds* herein.

2 Will bear interest at the rate of 5.50% to and including June 30, 2017, at which time will be subject to mandatory tender for purchase. Subsequent to the Initial Term Rate Period, will be Variable Rate Bonds and will bear interest at the rates and shall have such other terms and provisions as set forth in the Series Resolution and as described in *Description of the Bonds* herein. Insured by Ambac Assurance Corporation.

3 Will bear interest at the rate determined by the Underwriters on or about December 19, 2007, with such rate being the lowest rate that in the sole judgment of the Underwriters would be necessary to market the Series M-3 Bonds at par on December 20, 2007 for the period ending December 26, 2007; thereafter the Series M-3 Bonds shall be in a Weekly Interest Rate Period (as defined herein) until converted to another Interest Rate Period as provided in the Series Resolution. See *Description of the Bonds* herein. JPMorgan Chase Bank, National Association, Initial Liquidity Facility Provider; Lehman Brothers Inc., Remarketing Agent. Insured by MBIA Insurance Corporation.

**\$329,415,000**  
**Government Facilities Revenue Bonds, Series N**

<u>Maturity</u> <u>July 1</u>	<u>Amount</u>	<u>Interest Rate</u>	<u>Yield</u>	<u>CUSIP</u>
2013	\$ 3,670,000	5.00%	4.10%	745235ZU8
2014	7,040,000	5.00	4.18	745235ZV6
2015	7,390,000	5.00	4.25	745235ZW4
2016	7,760,000	5.25	4.33	745235ZX2
2017	8,165,000	5.25	4.41	745235ZY0
2018	8,595,000	5.50	4.50*	745235ZZ7
2019	9,070,000	5.50	4.56*	745235A27
2020	9,570,000	5.50	4.61*	745235A35
2021	10,095,000	5.50	4.68*	745235A43
2022	10,650,000	5.50	4.74*	745235A50
2023	11,235,000	5.50	4.80*	745235A68
2024	11,855,000	5.50	4.85*	745235A76
2025	12,505,000	5.50	4.88*	745235A84
2026	13,195,000	5.50	4.92*	745235A92
2027	13,920,000	5.50	4.95*	745235B26

\$81,145,000, 5.00% Term Bond, due July 1, 2032, Yield 5.08%, CUSIP 745235B34  
 \$103,555,000, 5.00% Term Bond, due July 1, 2037, Yield 5.11%, CUSIP 745235B42

**\$3,025,000**  
**Government Facilities Revenue Bonds, Series O**

<u>Maturity</u> <u>July 1</u>	<u>Amount</u>	<u>Interest Rate</u>	<u>Price</u>	<u>CUSIP</u>
2013	\$3,025,000	5.25%	100%	745235B59

\* Priced to July 1, 2017 call date.

No dealer, broker, sales representative, or other person has been authorized by the Authority 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 Authority or the Underwriters. 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 or incorporated herein by reference has been obtained from the Authority, Ambac Assurance, MBIA, or with respect to the information under the caption "Initial Liquidity Facility Provider," the Initial Liquidity Facility Provider, and other official sources that are believed to be reliable, but is not guaranteed as to accuracy or completeness and is not to be construed as a representation by any Underwriter. 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 Authority or the Commonwealth since the date hereof. This Official Statement is submitted in connection with the sale of the Bonds referred to herein and may not be reproduced or used, in whole or in part, for any other purpose. The Underwriters have provided the following sentence for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with, and as 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 PRICE OF THE BONDS OFFERED HEREBY AND OF OUTSTANDING BONDS OF THE AUTHORITY AT LEVELS ABOVE THOSE WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

CERTAIN STATEMENTS CONTAINED IN THIS OFFICIAL STATEMENT REFLECT NOT HISTORICAL FACTS BUT FORECASTS AND "FORWARD-LOOKING STATEMENTS." THESE STATEMENTS ARE BASED UPON A NUMBER OF ASSUMPTIONS AND ESTIMATES THAT ARE SUBJECT TO SIGNIFICANT UNCERTAINTIES, MANY OF WHICH ARE BEYOND THE CONTROL OF THE AUTHORITY. IN THIS RESPECT, THE WORDS "ESTIMATES," "PROJECTS," "ANTICIPATES," "EXPECTS," "INTENDS," "BELIEVES" AND SIMILAR EXPRESSIONS ARE INTENDED TO IDENTIFY FORWARD-LOOKING STATEMENTS. ALL PROJECTIONS, FORECASTS, ASSUMPTIONS, EXPRESSIONS OF OPINIONS, ESTIMATES, AND OTHER FORWARD-LOOKING STATEMENTS ARE EXPRESSLY QUALIFIED IN THEIR ENTIRETY BY THIS CAUTIONARY STATEMENT: ACTUAL RESULTS MAY DIFFER MATERIALLY FROM THOSE EXPRESSED OR IMPLIED BY FORWARD-LOOKING STATEMENTS.

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**\$895,290,000**  
**Puerto Rico Public Buildings Authority**  
**\$562,850,000 Government Facilities Revenue Refunding Bonds, Series M**  
**\$329,415,000 Government Facilities Revenue Bonds, Series N**  
**\$3,025,000 Government Facilities Revenue Bonds, Series O**  
**Guaranteed by the Commonwealth of Puerto Rico**

**INTRODUCTION**

The purpose of this Official Statement of the Puerto Rico Public Buildings Authority (the "Authority") is to furnish information with respect to the \$562,850,000 Puerto Rico Public Buildings Authority Government Facilities Revenue Refunding Bonds, Series M, Guaranteed by the Commonwealth of Puerto Rico (the "Series M Bonds"); \$329,415,000 Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds, Series N, Guaranteed by the Commonwealth of Puerto Rico (the "Series N Bonds"); and \$3,025,000 Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds, Series O, Guaranteed by the Commonwealth of Puerto Rico (the "Series O Bonds" and, together with the Series M Bonds and the Series N Bonds, collectively referred to as the "Bonds") to be issued by the Authority and to be guaranteed by the Commonwealth of Puerto Rico (the "Commonwealth" or "Puerto Rico").

The Bonds will be issued pursuant to Act No. 56 of the Legislature of Puerto Rico (the "Legislature"), approved on June 19, 1958, as amended (the "Enabling Act"), and under the provisions of Resolution No. 468, adopted by the Authority on June 22, 1995 (the "1995 Bond Resolution"), as supplemented by Resolution No. 1280 adopted by the Authority on December 6, 2007 (the "Series Resolution" and, together with the 1995 Bond Resolution, sometimes hereinafter referred to as the "Bond Resolution"). Immediately after the issuance of the Bonds, and after taking into account the refunding and defeasance of the Refunded Bonds (as such term is defined herein), the Authority will have outstanding \$2,946,603,182 of its Government Facilities Bonds (calculated by excluding all accretion on any existing capital appreciation bonds and convertible capital appreciation bonds) issued under the 1995 Bond Resolution.

The Authority is issuing the Series M Bonds in three separate subseries, as described below and under *Description of the Bonds* herein.

*Series M-1.* \$283,550,000 principal amount of the Series M Bonds shall be issued as a subseries designated "Series M-1" (the "Series M-1 Bonds"). The Series M-1 Bonds shall bear interest at fixed rates of interest as set forth in the inside cover page of this Official Statement to their stated maturities or earlier redemption and shall have such details as set forth in the Series Resolution and as described in *Description of the Bonds* below.

*Series M-2.* \$129,300,000 principal amount of the Series M Bonds shall be issued as a subseries designated "Series M-2" (the "Series M-2 Bonds") initially bearing interest at the fixed rates of interest set forth in the inside cover page of this Official Statement to and including June 30, 2017. The Series M-2 Bonds are subject to mandatory tender for purchase on July 1, 2017. The interest rates on the Series M-2 Bonds shall be increased to 10% if such Bonds are not successfully remarketed on July 1, 2017, as provided in the Series Resolution and more specifically described under *Description of the Bonds* herein. After the Initial Term Rate Period (as defined herein), the Series M-2 Bonds shall bear interest at variable rates of interest and shall have such other terms and provisions as set forth in the Series Resolution and as described in *Description of the Bonds* below. "Initial Term Rate Period" means the period beginning on the date of delivery of the Series M-2 Bonds through and including June 30, 2017, or, if the Series M-2 Bonds are not remarketed on July 1, 2017, continuing until (but not including) such later date as the Series M-2 Bonds are successfully remarketed as described below. The Series M-2 Bonds, after the Initial Term Rate Period, will be Variable Rate Bonds (as defined herein). The Series M-2 Bonds maturing July 1, 2035 will be insured by a financial guaranty insurance policy (the "Ambac Insurance Policy") issued by Ambac Assurance Corporation ("Ambac Assurance").

In connection with the Series M-2 Bonds, Lehman Brothers Inc. ("Lehman Brothers") will serve as remarketing agent (the "Series M-2 Remarketing Agent") under a remarketing agreement with the Authority (the "Series M-2 Remarketing Agreement"). As of the date of this Official Statement, the Authority has not provided

and does not intend to provide any liquidity facility for the payment of the purchase price payable upon the mandatory tender of the Series M-2 Bonds at the end of the Initial Term Rate Period, nor is there any requirement that such liquidity facility be obtained. The Tender Purchase Price (as such term is defined herein) for the Series M-2 Bonds is expected to be obtained solely from the remarketing of such Series M-2 Bonds. U.S. Bank Trust National Association will serve as tender agent for the Series M-2 Bonds (the "Tender Agent").

*Series M-3.* \$150,000,000 principal amount of the Series M Bonds shall be issued as a subseries designated "Series M-3" (the "Series M-3 Bonds"). The initial Interest Rate Period for the Series M-3 Bonds shall be a Weekly Interest Rate Period (as defined herein). The Series M-3 Bonds are Variable Rate Bonds. See *Description of the Bonds* herein. U.S. Bank Trust National Association will serve as Tender Agent for the Series M-3 Bonds. In connection with the Series M-3 Bonds, the Authority and JPMorgan Chase Bank, National Association ("JPMorgan" or the "Initial Liquidity Facility Provider") will enter into a standby bond purchase agreement on December 20, 2007 (the "Standby Purchase Agreement") providing for the purchase of Series M-3 Bonds that are tendered and not remarketed, which agreement will expire, subject to earlier termination under certain circumstances or extension, prior to the final maturity of said Series M-3 Bonds. The regularly scheduled payments of principal of and interest on the Series M-3 Bonds will be insured by a financial guaranty insurance policy (the "MBIA Insurance Policy") issued by MBIA Insurance Corporation ("MBIA").

Lehman Brothers will serve as remarketing agent for the Series M-3 Bonds (the "Series M-3 Remarketing Agent") under a remarketing agreement dated December 20, 2007 with the Authority (the "Series M-3 Remarketing Agreement"). In order to effectively fix the interest cost to the Authority of said Series M-3 Bonds, the Authority has entered into an interest rate swap (the "Interest Rate Swap") with The Royal Bank of Canada (the "Swap Provider") under a master interest rate exchange agreement dated September 8, 2006 and related documentation. The Interest Rate Swap is evidenced by a confirmation entered into by the Authority and the Swap Provider on December 5, 2007. The Royal Bank of Canada is the parent company of RBC Dain Rauscher Inc. doing business under the name RBC Capital Markets. The Royal Bank of Canada will pay BBVAPR Division de Valores Municipales ("BBVA PR MSD") a commission related to the Interest Rate Swap that has not increased the fixed rate payable by the Authority.

The Series N Bonds shall bear interest at fixed rates of interest, as set forth in the inside cover page of this Official Statement, and shall have such details as set forth in the Series Resolution and as described in *Description of the Bonds* herein.

The Series O Bonds shall bear interest at the fixed rate of interest set forth in the inside cover page of this Official Statement and shall have such details as set forth in the Series Resolution and as described in *Description of the Bonds* herein.

Reference is made to the 1995 Bond Resolution, as supplemented by the Series Resolution, for the complete terms of the Bonds. Terms used in this Official Statement and not defined herein have the respective meanings ascribed to them in the 1995 Bond Resolution, as supplemented by the Series Resolution, copies of which may be obtained by contacting Director-New York Office, Government Development Bank for Puerto Rico, 666 Fifth Avenue, 15th Floor, New York, New York 10103-1599, telephone number (212) 422-6420, or to Director-General Obligations Division, Government Development Bank for Puerto Rico, P.O. Box 42001, San Juan, Puerto Rico 00940, telephone number (787) 722-7060.

This Official Statement includes the cover page, the inside cover page, the appendices hereto and the following documents:

- (1) the Commonwealth of Puerto Rico Financial Information and Operating Data Report dated July 1, 2007, which contains financial and other information of the Commonwealth (the "Commonwealth Report") and which is appended as Appendix I to the Official Statement of the Commonwealth dated September 19, 2007 relating to the issuance by the Commonwealth of its \$408,800,000 Public Improvement Bonds of 2007, Series A. The Commonwealth Report, which includes important operating and financial information about the Commonwealth, including information about its economy, historical revenues and expenditures of its General Fund, the estimated year-end results for fiscal year 2007, the budgets for fiscal years 2007 and 2008, and the debt of the Commonwealth's public sector, has been filed by the Commonwealth with

each nationally recognized municipal securities information repository ("NRMSIR"), is incorporated herein by reference and should be read in its entirety and in conjunction with the information contained under the caption *Recent Developments of the Commonwealth* herein; and

- (2) the Comprehensive Annual Financial Report of the Commonwealth for the fiscal year ended June 30, 2006, as amended, prepared by the Department of the Treasury of the Commonwealth (the "Comprehensive Annual Financial Report"), which includes the basic financial statements of the Commonwealth as of and for the fiscal year ended June 30, 2006, together with the independent auditor's report thereon, dated August 1, 2007, of KPMG LLP, certified public accountants. KPMG LLP did not audit the financial statements of the Authority's capital project fund or the Children's Trust special revenue fund (major funds), and certain activities, funds, and component units separately identified in its report. Those financial statements were audited by other auditors whose reports have been furnished to KPMG LLP, and its opinion as to the basic financial statements, insofar as it relates to the amounts included in the basic financial statements pertaining to such activities, funds, and component units, is based solely on the reports of the other auditors. The report of KPMG LLP contains an emphasis paragraph for the adoption of Governmental Accounting Standards Board (GASB) Statement No. 42, *Accounting and Financial Reporting for Impairment of Capital Assets and for Insurance Recoveries*, as of June 30, 2006. The Comprehensive Annual Financial Report has been filed by the Commonwealth with each NRMSIR and is incorporated herein by reference.

Any appendix of an Official Statement of the Commonwealth or of any instrumentality of the Commonwealth containing any revision to the Commonwealth Report, or to the Comprehensive Annual Financial Report that is filed with each NRMSIR, or any new or revised Commonwealth Report or Comprehensive Annual Financial Report, or other document containing information that modifies or supersedes the information contained in the Commonwealth Report or in the Comprehensive Annual Financial Report that is filed with each NRMSIR, in each case after the date hereof and prior to the termination of the offering of the Bonds, shall be deemed to be incorporated by reference into this Official Statement and to be part of this Official Statement from the date of filing of such document. Any statement contained herein or in the Comprehensive Annual Financial Report or in the Commonwealth Report shall be deemed to be modified or superseded for purposes of this Official Statement to the extent that a statement contained in any such subsequently filed document modifies or supersedes such statement.

The Commonwealth will provide without charge to any person to whom this Official Statement is delivered, on the written or oral request of such person, a copy of any or all of the foregoing documents incorporated herein by reference. Requests for such documents should be directed to Director-New York Office, Government Development Bank for Puerto Rico, 666 Fifth Avenue, 15th Floor, New York, New York 10103-1599, telephone number (212) 422-6420, or to Director-General Obligations Division, Government Development Bank for Puerto Rico, P.O. Box 42001, San Juan, Puerto Rico 00940, telephone number (787) 722-7060.

A copy of the Commonwealth Report and the Comprehensive Annual Financial Report may also be obtained by contacting a NRMSIR. The address of each NRMSIR is set forth in *Continuing Disclosure* herein. The Commonwealth expects that its Comprehensive Annual Financial Report for the fiscal year ended June 30, 2007, including its audited general-purpose financial statements for such fiscal year, will be available to investors during the first quarter of calendar year 2008. Promptly after its release, said report will be filed with and available from each NRMSIR.

## **RECENT DEVELOPMENTS OF THE COMMONWEALTH**

This section summarizes and updates certain information about the Commonwealth's current fiscal situation appearing in the Commonwealth Report. This section should be read in conjunction with the information included in the Commonwealth Report, which shall be deemed modified to the extent the information provided therein is different from that appearing below.

Under Act No. 117 of the Legislature, approved on July 4, 2006, as amended (the "Sales Tax Act"), a general sales and use tax of 5.5% is imposed by the central government (the "Central Government Sales Tax") and of 1.5% is imposed by each municipality (the "Municipal Sales Tax" and, together with the Central Government Sales Tax, the "Sales Tax"). In general, the Municipal Sales Tax has the same tax base, exemptions (except for



unprocessed foods) and limitations as those contained in the Central Government Sales Tax. The Sales Tax Act also provides certain income tax reductions to address the regressive effect of the Sales Tax on taxpayers in lower income tax brackets.

Pursuant to Act No. 91 of the Legislature, approved on May 13, 2006, as amended (the "Sales Tax Financing Corporation Act"), Puerto Rico Sales Tax Financing Corporation (the "Sales Tax Financing Corporation") was created for the purpose of refinancing certain debt obligations of the Commonwealth outstanding as of June 30, 2006, which obligations are payable solely from Commonwealth budgetary appropriations and are generally referred to as "extra constitutional debt."

Under the Sales Tax Financing Corporation Act, 1% of the 5.5% Central Government Sales Tax (subject to an annually inflated minimum amount if greater) is deposited by the Secretary of the Treasury of the Commonwealth (the "Secretary of the Treasury") upon receipt into the dedicated sales tax fund (the "Sales Tax Fund"), which is held and owned by the Sales Tax Financing Corporation separate and apart from the Commonwealth's General Fund. Amounts on deposit in the Sales Tax Fund are applied to the payment of debt issued by the Sales Tax Financing Corporation to refinance the extra constitutional debt outstanding. On July 31, 2007, the Sales Tax Financing Corporation issued \$2,667,603,572.60 of Sales Tax Revenue Bonds, Series 2007 A and \$1,333,101,779.90 of Sales Tax Revenue Bonds, Series 2007 B, the proceeds of which were used as the first installment in the refinancing of the Commonwealth's extra constitutional debt.

Since July 1, 2007, the Commonwealth has also issued the following bonds and notes. On October 4, 2007, the Commonwealth issued \$408,800,000 of Public Improvement Bonds, Series 2007 A and \$91,200,000 of Public Improvement Bonds, Series 2007 B, each under the provisions of Act No. 74 of the Legislature, approved on July 23, 2007, as amended. On October 16, 2007, the Commonwealth issued \$926,570,000 of Public Improvement Refunding Bonds, Series 2007 A and \$60,545,000 of Public Improvement Refunding Bonds, Series 2007 B, each under the provisions of Act No. 52 of the Legislature, approved on October 10, 1985, and Joint Resolution No. 57 of the Legislature, approved on July 12, 1993. On November 1, 2007, the Commonwealth issued \$1,010,000,000 of Tax and Revenue Anticipation Notes, Series 2008, under the provisions of Act No. 1 of the Legislature, approved on June 26, 1987, as amended.

## PLAN OF FINANCING

### Series M Bonds

The Series M Bonds will be issued for the purpose of (i) refunding certain bonds issued under the 1995 Bond Resolution (the "Refunded Bonds"); (ii) refunding the interest component (and not principal) of certain other bonds currently outstanding under the 1995 Bond Resolution; and (iii) paying the costs of issuance of the Series M Bonds. From the proceeds of the Series M Bonds, the following bonds will be refunded:

<u>Series Designation</u>	<u>Principal Amount to be Refunded</u>	<u>Interest Rate</u>	<u>Maturity Date July 1</u>	<u>Redemption Date</u>	<u>Redemption Price</u>
Series A	\$ 5,730,000	6.250%	2008	N/A	N/A
Series B	13,995,000	4.800	2008	01/22/2008	101.5%
Series B	14,670,000	5.000	2009	01/22/2008	101.5
Series B	15,405,000	5.100	2010	01/22/2008	101.5
Series B	16,190,000	5.000	2011	01/22/2008	101.5
Series B	16,995,000	5.000	2012	01/22/2008	101.5
Series B	17,845,000	5.000	2013	01/22/2008	101.5
Series B	18,740,000	5.000	2014	01/22/2008	101.5
Series B	19,675,000	5.000	2015	01/22/2008	101.5
Series B	20,660,000	5.000	2016	01/22/2008	101.5
Series B	21,695,000	5.125	2017	01/22/2008	101.5
Series C	9,710,000 <sup>1</sup>	5.250	2008	N/A	N/A
Series D	6,615,000 <sup>2</sup>	5.125	2022	07/01/2012	100.0
Series D	11,725,000 <sup>3</sup>	5.125	2024	07/01/2012	100.0
Series D	18,322,460 <sup>4</sup>	5.450	2030	07/01/2017	100.0

<u>Series Designation</u>	<u>Principal Amount to be Refunded</u>	<u>Interest Rate</u>	<u>Maturity Date July 1</u>	<u>Redemption Date</u>	<u>Redemption Price</u>
Series D	\$ 17,114,668 <sup>5</sup>	5.450%	2031	07/01/2017	100.0%
Series G	1,260,000	4.000	2008	N/A	N/A
Series I	2,075,000	5.500	2019	07/01/2014	100.0
Series I	11,505,000	5.500	2020	07/01/2014	100.0
Series I	18,070,000	5.500	2021	07/01/2014	100.0
Series I	19,100,000	5.500	2022	07/01/2014	100.0
Series I	25,640,000	5.500	2023	07/01/2014	100.0
Series I	27,040,000	5.500	2024	07/01/2014	100.0
Series I	28,535,000	5.500	2025	07/01/2014	100.0
Series I	77,175,000 <sup>6</sup>	5.250	2029	07/01/2014	100.0
Series I	4,000,000 <sup>7</sup>	5.250	2033	07/01/2014	100.0
Series I	91,405,000	5.375	2034	07/01/2014	100.0

<sup>1</sup> Represents a portion of the \$13,250,000 aggregate principal amount maturing on July 1, 2008.

<sup>2</sup> Represents a portion of the \$9,025,000 aggregate principal amount maturing on July 1, 2022.

<sup>3</sup> Represents \$5,715,000 of the \$7,800,000 amortization requirement due July 1, 2023 and \$6,010,000 of the \$8,205,000 amortization requirement due July 1, 2024.

<sup>4</sup> Represents a portion of the \$24,998,151.50 aggregate principal amount convertible capital appreciation bond maturing on July 1, 2030.

<sup>5</sup> Represents a portion of the \$23,350,643.40 aggregate principal amount convertible capital appreciation bond maturing on July 1, 2031.

<sup>6</sup> Represents \$5,000,000 of the \$30,025,000 amortization requirement due July 1, 2026, \$5,000,000 of the \$44,645,000 amortization requirement due July 1, 2029, the amortization requirement due July 1, 2027 in the amount of \$31,605,000 and the amortization requirement due July 1, 2028 in the amount of \$35,570,000.

<sup>7</sup> Represents \$2,000,000 of the \$77,870,000 amortization requirement due July 1, 2032 and \$2,000,000 of the \$86,070,000 amortization due July 1, 2033.

The Authority will deposit \$612,173,470.26, consisting of the net proceeds of the Series M Bonds and other available moneys, into an irrevocable escrow fund with U.S. Bank Trust National Association, the Fiscal Agent under the 1995 Bond Resolution (the "Fiscal Agent") for investment in certain Government Obligations (as defined in the 1995 Bond Resolution), the principal of and interest on which, will be sufficient to (i) pay when due the principal of, redemption premium (if any) and interest on the Refunded Bonds on the redemption date mentioned above, which redemption date will be irrevocably designated by the Authority and (ii) pay the interest component due on July 1, 2008 of certain other bonds outstanding under the 1995 Bond Resolution. Under the 1995 Bond Resolution, upon such deposit, the Refunded Bonds will be deemed to have been paid and no longer outstanding for purposes of the 1995 Bond Resolution.

The adequacy of the amounts so deposited with the Fiscal Agent, with the investment earnings thereon, to accomplish the refunding of the Refunded Bonds and the payment of interest due July 1, 2008 on certain other bonds outstanding under the 1995 Bond Resolution will be verified by Samuel Klein and Company, Certified Public Accountants, the verification agent. See *Verification of Mathematical Computations* herein.

### Series N Bonds

The Series N Bonds will be issued to provide funds to (i) pay a portion of the costs of construction of certain buildings and facilities to be leased by the Authority to various departments and instrumentalities of the Commonwealth; (ii) pay the principal of and a portion of the accrued interest on certain outstanding notes of the Authority held by Government Development for Puerto Rico (the "Government Development Bank"), evidencing amounts loaned by Government Development Bank to the Authority to finance a portion of the cost of its capital improvements program (the "GDB Notes"); (iii) pay capitalized interest on the Series N Bonds; and (iv) pay costs of issuance of Series N Bonds. For a more detailed description of the Authority's construction program, see *The Authority* herein.

### Series O Bonds

The Series O Bonds will be issued to provide funds to (i) pay a portion of the accrued interest on the GDB Notes; (ii) pay capitalized interest on the Series O Bonds; and (iii) pay costs of issuance of Series O Bonds.

**Sources and Uses of Funds**

The proceeds of the Bonds (including any premium and net of original issue discount) are expected to be used as follows:

**Series M Bonds**

Sources of Funds	
Series M Bonds .....	\$ 562,850,000.00
Net original issue premium .....	44,516,304.55
Other Sources of Funds <sup>1</sup> .....	15,445,428.17
Total .....	<u>\$ 622,811,732.72</u>
Uses of Funds	
Deposit into escrow account for Refunded Bonds and refunded interest.....	\$ 612,173,470.26
Underwriting discount, bond insurance premiums, and estimated legal, printing, and other financing expenses.....	10,638,262.46
Total.....	<u>\$ 622,811,732.72</u>

**Series N Bonds**

Sources of Funds	
Series N Bonds .....	\$ 329,415,000.00
Net original issue premium .....	5,363,915.50
Total .....	<u>\$ 334,778,915.50</u>
Uses of Funds	
Deposit into the 1995 Construction Fund .....	\$ 117,692,287.04
Repayment of certain GDB Notes <sup>2</sup> .....	166,672,196.82
Payment of capitalized interest on Series N Bonds.....	47,940,023.93
Underwriting discount and estimated legal, printing, and other financing expenses.....	2,474,407.71
Total.....	<u>\$ 334,778,915.50</u>

**Series O Bonds**

Sources of Funds	
Series O Bonds .....	\$ 3,025,000.00
Total .....	<u>\$ 3,025,000.00</u>
Uses of Funds	
Repayment of certain GDB Notes <sup>3</sup> .....	\$ 2,553,060.07
Payment of capitalized interest on Series O Bonds.....	446,171.44
Underwriting discount and estimated legal, printing and other financing expenses.....	25,768.49
Total.....	<u>\$ 3,025,000.00</u>

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<sup>1</sup> Available Debt Service Funds.  
<sup>2</sup> Represents principal and a portion of the interest due on the GDB Notes.  
<sup>3</sup> Represents a portion of the interest due on the GDB Notes.

## **Standby Bond Purchase Agreement**

In connection with the Series M-3 Bonds, the Authority will enter into the Standby Purchase Agreement, whereby, unless certain events have occurred, the Initial Liquidity Facility Provider will be required to purchase the Series M-3 Bonds which are optionally or mandatorily tendered by their Owners and are not remarketed. The obligation of the Initial Liquidity Facility Provider to purchase Series M-3 Bonds under the Standby Purchase Agreement will expire on December 20, 2010, prior to the final maturity of the Series M-3 Bonds, unless extended or terminated in accordance with its terms. THE INITIAL LIQUIDITY FACILITY PROVIDER'S OBLIGATION TO PURCHASE SERIES M-3 BONDS IS TERMINATED OR SUSPENDED AUTOMATICALLY UNDER CERTAIN CIRCUMSTANCES WITH NO OPPORTUNITY FOR THE HOLDERS OF SUCH BONDS TO TENDER THEM PRIOR TO SUCH TERMINATION OR SUSPENSION. If the obligation of the Initial Liquidity Facility Provider to purchase Series M-3 Bonds under the Standby Purchase Agreement has been terminated or suspended prior to, or the conditions to such obligation are not satisfied as of, the date on which the payment of the purchase price of such Bonds is required, funds to pay such purchase price will not be available under the Initial Liquidity Facility. See "Purchase of the Variable Rate Bonds" under *Description of the Bonds* herein. THE AUTHORITY IS NOT OBLIGATED TO PURCHASE SERIES M-3 BONDS IN THE EVENT THAT PAYMENTS ARE NOT MADE UNDER THE LIQUIDITY FACILITY. See "Initial Liquidity Facility" under *Description of the Bonds* herein.

As of the date of this Official Statement, the Authority has not provided and does not intend to provide any liquidity facility for the payment of the purchase price payable upon the mandatory tender of the Series M-2 Bonds on July 1, 2017 nor is there any requirement that such liquidity facility be obtained.

## **Interest Rate Swap**

The Authority has entered into the Interest Rate Swap with the Swap Provider in accordance with the requirements of Act No. 39 of the Legislature of Puerto Rico, approved on August 1, 2005, as amended ("Act No. 39 of 2005"), pursuant to which (i) the Authority will pay a fixed amount to the Swap Provider, and (ii) the Swap Provider will pay a variable amount to the Authority based on LIBOR and a notional amount equal to the aggregate principal amount of the Series M-3 Bonds. The notional amount of the Interest Rate Swap will amortize in accordance with the principal amortization of the Series M-3 Bonds.

Under the terms of the Interest Rate Swap, which is scheduled to terminate on the maturity of the Series M-3 Bonds, the Interest Rate Swap may be terminated by the Authority, upon obtaining MBIA's consent, at any time and may also be terminated upon the occurrence of certain credit events. If the Interest Rate Swap is terminated prior to its scheduled maturity, the Authority may be obligated to pay to the Swap Provider an amount based on the Interest Rate Swap's market value. Such amount may be substantial.

Certain of the Authority's obligations under the Interest Rate Swap will be insured by MBIA.

## **DESCRIPTION OF THE BONDS**

### **General**

The Bonds will be dated, will bear interest at such rates, will be payable at such times, and will mature on July 1 of the years and in the principal amounts set forth in the inside cover page of this Official Statement. The Bonds are subject to redemption and mandatory tender at the times and at the prices set forth below and in "Redemption." The Bonds, other than the Series M-3 Bonds, will be issued in denominations of \$5,000 and any multiple thereof as described below under "Book-Entry Only System." The Series M-3 Bonds will be issued in denominations of \$100,000 and multiples of \$5,000 in excess thereof as described below under "Book-Entry Only System." U.S. Bank Trust National Association serves as the Fiscal Agent under the 1995 Bond Resolution.

Reference is made to the 1995 Bond Resolution, as supplemented by the Series Resolution, for the complete terms of the Bonds. Terms used in this Official Statement and not defined herein have the respective meanings ascribed to them in the 1995 Bond Resolution, as supplemented by the Series Resolution.

*Series M-1 Bonds.* The Series M-1 Bonds shall bear interest, payable semiannually to the maturity thereof on the 1<sup>st</sup> days of January and July in each year, beginning July 1, 2008, at the rates, and shall be stated to mature in annual installments on the 1<sup>st</sup> day of July in the years and in the amounts, as set forth in the inside cover page of this Official Statement.

*Series M-2 Bonds.* The Series M-2 Bonds shall be term bonds stated to mature on July 1, 2034 (the "2034 Series M-2 Term Bonds") and July 1, 2035 (the "2035 Series M-2 Term Bonds"). The 2034 Series M-2 Term Bonds shall initially bear interest, payable on January 1 and July 1 of each year, beginning July 1, 2008, at the rate of 5.75% per annum, to and including June 30, 2017. The 2035 Series M-2 Term Bonds shall initially bear interest, payable on January 1 and July 1 of each year, beginning July 1, 2008, at the rate of 5.50% per annum, to and including June 30, 2017. The Series M-2 Bonds shall be subject to mandatory tender for purchase on July 1, 2017 as further described in the Series Resolution. Thereafter, the interest rates on the Series M-2 Bonds shall, unless the Authority by written notice given to the Fiscal Agent and Tender Agent at least thirty (30) days prior to July 1, 2017, elects to convert the Series M-2 Bonds to one or more other Interest Rate Periods as permitted and as set forth in the Series Resolution, convert to the Weekly Interest Rate (as defined herein).

If the Series M-2 Bonds are not remarketed on July 1, 2017, the Series M-2 Bonds shall be returned to the owners thereof, shall be deemed to continue in the Initial Term Rate Period, and shall bear interest from July 1, 2017 at the rate of 10% per annum until (but not including) the date such bonds are remarketed, on which date the Series M-2 Bonds shall again be subject to mandatory tender for purchase in accordance with the provisions of the Series Resolution. In the event the Series M-2 Bonds are not remarketed on July 1, 2017, the Authority shall cause the Series M-2 Bonds to be converted to one or more Interest Rate Periods on the earliest Business Day after July 1, 2017 at which all of such Series M-2 Bonds may be remarketed.

During the Initial Term Rate Period, the Series M-2 Bonds shall not be Variable Rate Bonds under the Series Resolution and shall not be subject to the provisions applicable to Variable Rate Bonds. After the end of the Initial Term Rate Period, the Series M-2 Bonds shall be deemed to be Variable Rate Bonds for purposes of establishing, from time to time, the interest rates thereon, and shall bear interest at such rates, shall be payable on such dates and shall have such other terms and provisions as set forth in the Series Resolution for Variable Rate Bonds. See "Description of the Variable Rate Bonds" for a description of possible Interest Rate Periods.

The 2035 Series M-2 Term Bonds will be insured by Ambac Assurance.

In connection with the Series M-2 Bonds, Lehman Brothers serves as the Series M-2 Remarketing Agent under the Series M-2 Remarketing Agreement. U.S. Bank Trust National Association will serve as Tender Agent for the Series M-2 Bonds. As of the date of this Official Statement, the Authority has not provided and does not intend to provide any liquidity facility for the payment of the purchase price payable upon the mandatory tender of the Series M-2 Bonds at the end of the Initial Term Rate Period, nor is there any requirement that such liquidity facility be obtained. The Tender Purchase Price (as defined in the Series Resolution) for the Series M-2 Bonds is expected to be obtained from the remarketing thereof. After the end of the Initial Term Rate Period, the Authority may provide a liquidity facility for the Series M-2 Bonds.

*Series M-3 Bonds.* The Series M-3 Bonds are being initially issued in a Weekly Interest Rate Period and will bear interest at a Weekly Interest Rate until converted to another Interest Rate Period; provided that the initial interest rate shall be determined by the Underwriters on or about December 19, 2007 as being the lowest rate that in the sole judgment of the Underwriters would be necessary to market the Series M-3 Bonds at par on December 20, 2007 for the period ending December 26, 2007. While the Series M-3 Bonds are in a Weekly Interest Rate Period, interest shall be payable on the first Business Day of each calendar month, beginning January 1, 2008. See "Description of Variable Rate Bonds" herein.

U.S. Bank Trust National Association will serve as Tender Agent for the Series M-3 Bonds. The Authority will enter into the Standby Purchase Agreement with the Initial Liquidity Facility Provider providing for the purchase of Series M-3 Bonds that are tendered and not remarketed, which agreement will expire, subject to earlier termination under certain circumstances or extension, prior to the final maturity of said Series M-3 Bonds. See "Initial Liquidity Facility" and "Initial Liquidity Facility Provider" herein.

The Series M-3 Bonds will be insured by MBIA.

In connection with the Series M-3 Bonds, Lehman Brothers will serve as the Series M-3 Remarketing Agent under the Series M-3 Remarketing Agreement with the Authority. In order to effectively fix the interest cost to the Authority of said Series M-3 Bonds, the Authority has entered into the Interest Rate Swap with Swap Provider.

*Series N Bonds.* The Series N Bonds shall bear interest, payable semiannually to the maturity thereof on the 1<sup>st</sup> days of January and July in each year, beginning July 1, 2008, at the rates, and shall be stated to mature in annual installments on the 1<sup>st</sup> day of July in the years and in the amounts, as set forth in the inside cover page of this Official Statement.

*Series O Bonds.* The Series O Bonds shall bear interest, payable semiannually to the maturity thereof on the 1<sup>st</sup> days of January and July in each year, beginning July 1, 2008, at the rate, and shall be stated to mature on such date, and in the amount, as set forth in the inside cover page of this Official Statement.

### **Description of the Variable Rate Bonds**

The following is a summary of certain provisions of the Series M-2 Bonds after the Initial Term Rate Period, and of the Series M-3 Bonds. Reference is made to the Series M-2 Bonds and the Series M-3 Bonds for their complete text and to the 1995 Bond Resolution, as supplemented by the Series Resolution, for a more detailed description of the provisions of the Series M-2 Bonds after the Initial Term Rate Period, and the Series M-3 Bonds. Each of the Series M-2 Bonds after the end of the Initial Term Rate Period, and the Series M-3 Bonds, are referred to in this section as Variable Rate Bonds, and may bear interest at the Interest Rate Periods described below. The Series M-2 Remarketing Agent and the Series M-3 Remarketing Agent are referred to in this section as the "Remarketing Agent." MBIA and Ambac Assurance are referred to in this section individually as the "Bond Insurer."

*General.* At the direction of the Authority, from time to time, the Variable Rate Bonds may be converted in whole, from an Interest Rate Period to another Interest Rate Period, including the Daily Interest Rate Period (the "Daily Interest Rate Period"), the Weekly Interest Rate Period (the "Weekly Interest Rate Period"), the Long-Term Interest Rate Period (the "Long-Term Interest Rate Period"), the Short-Term Interest Rate Period (the "Short-Term Interest Rate Period"), the ARS Rate Period (the "ARS Rate Period") and the Indexed Put Interest Rate Period (the "Indexed Put Interest Rate Period"). The Daily Interest Rate Period, the Weekly Interest Rate Period, the Long-Term Interest Rate Period, the Short-Term Interest Rate Period, the ARS Rate Period and the Indexed Put Interest Rate Period are herein referred to individually as an "Interest Rate Period" and collectively as the "Interest Rate Periods." *This Official Statement provides information concerning the Variable Rate Bonds only while bearing interest at a Weekly Interest Rate. There are significant differences in the terms of the Variable Rate Bonds if they are bearing interest at a Long-Term Interest Rate (the "Long-Term Interest Rate"), a Bond Interest Term Rate during each Bond Interest Term in a Short-Term Interest Rate Period (the "Bond Interest Term Rate"), an Auction Period Rate ("Auction Period Rate"), a Daily Interest Rate ("Daily Interest Rate") or the Indexed Put Rate (the "Indexed Put Rate"). This Official Statement does not provide information with respect to the Variable Rate Bonds other than Variable Rate Bonds in a Weekly Interest Rate Period.*

The Variable Rate Bonds shall be in Authorized Denominations as described in the Series Resolution. As described below under the caption "Book-Entry Only System," when issued, the Variable Rate Bonds will be registered in the name of Cede & Co., as Bondholder and nominee of The Depository Trust Company, New York, New York, which will act as securities depository for the Variable Rate Bonds.

*Interest Payment.* All Variable Rate Bonds of a subseries shall initially bear interest at the same interest rate. Variable Rate Bonds bearing interest at the Weekly Interest Rate shall not, at any time, bear interest in excess of 12% per annum (the "Maximum Bond Interest Rate"). Interest on the Variable Rate Bonds shall be paid on each Interest Payment Date, any redemption date and on the Maturity Date. Variable Rate Bonds in the Weekly Interest Rate Period shall accrue interest on the basis of the actual number of days elapsed during the Interest Rate Period and a year of 365 days (366 in a leap year). Thereafter, the Interest Payment Date for the Variable Rate Bonds in the Weekly Interest Rate Period will be the first Business Day of each calendar month.

*Place of Payment.* The principal and Tender Price of and premium, if any, and interest on the Variable Rate Bonds in the Weekly Interest Rate Period shall be paid by the Fiscal Agent by wire transfer of immediately available funds to the respective Holders thereof on the applicable Record Date to an account specified by the Holder thereof in a writing delivered to the Fiscal Agent.

*Remarketing Agent; Tender Agent.* Lehman Brothers has been appointed Remarketing Agent for the Variable Rate Bonds. All determinations for the Variable Rate Bonds of interest rates shall be conclusive and binding upon the Authority, the Fiscal Agent, the Tender Agent, the Remarketing Agent, the Initial Liquidity Facility Provider and the Variable Rate Bond Bondholders, as applicable. At the direction of the Authority, the Variable Rate Bonds may be converted, in whole, from one Interest Rate Period to another Interest Rate Period.

*Weekly Interest Rate and Weekly Interest Rate Period.* During each Weekly Interest Rate Period, the Variable Rate Bonds shall bear interest at the Weekly Interest Rate, which shall be determined by the Remarketing Agent by 5:00 p.m., New York City time, on Wednesday of each week during the Weekly Interest Rate Period, or if such day is not a Business Day, then on the next succeeding Business Day. The first Weekly Interest Rate for each Weekly Interest Rate Period shall be determined on or prior to the first day of such Weekly Interest Rate Period and shall apply to the period commencing on the first day of such Weekly Interest Rate Period and ending on and including the next succeeding Wednesday. Thereafter, each Weekly Interest Rate shall apply to the period commencing on and including Thursday and ending on and including the next succeeding Wednesday, unless such Weekly Interest Rate Period ends on a day other than Wednesday, in which event the last Weekly Interest Rate for such Weekly Interest Rate Period shall apply to the period commencing on and including the Thursday preceding the last day of such Weekly Interest Rate Period and ending on and including the last day of such Weekly Interest Rate Period.

Each Weekly Interest Rate with respect to the Variable Rate Bonds shall be the rate of interest per annum determined by the Remarketing Agent (based on an examination of tax-exempt obligations comparable, in the judgment of the Remarketing Agent, to the Variable Rate Bonds and known by it to have been priced or traded under then-prevailing market conditions) to be the minimum interest rate which, if borne by such Variable Rate Bonds, would enable the Remarketing Agent to sell all of such Variable Rate Bonds on the effective date of that rate at a price (without regard to accrued interest) equal to the principal amount thereof.

If the Remarketing Agent fails to establish a Weekly Interest Rate for any week with respect to the Variable Rate Bonds bearing interest at such rate, then the Weekly Interest Rate for such week with respect to such Variable Rate Bonds shall be equal to the Index. The Fiscal Agent shall give notice by first-class mail of a Conversion to a Weekly Interest Rate Period to the Holders of the Variable Rate Bonds not less than 30 days prior to the proposed effective date of such Weekly Interest Rate Period, in accordance with requirements under the Bond Resolution.

### **Conversion Provisions**

*General.* If the Authority elects to convert the interest rate of the Variable Rate Bonds, the written direction furnished by the Authority to the Fiscal Agent, the Tender Agent, the Initial Liquidity Facility Provider, the Remarketing Agent, the Auction Agent (if any), the Broker-Dealer (if any) and the Bond Insurer as required, shall be made by registered or certified mail, or by telecopy confirmed by registered or certified mail. In connection with any Conversion of the Interest Rate Period for the Variable Rate Bonds, the Authority shall have the right to deliver to the Fiscal Agent, the Tender Agent, the Bond Insurer, the Remarketing Agent, the Auction Agent (if any), the Broker-Dealer (if any) and the Initial Liquidity Facility Provider on or prior to 11:00 a.m., New York City time, on the second Business Day preceding the effective date of any such Conversion, a notice to the effect that the Authority elects to rescind its election to make such Conversion. If such election to convert is rescinded, then the Variable Rate Bonds shall bear interest at a Weekly Interest Rate commencing on the date which would have been the effective date of the Conversion. In any event, if notice of a Conversion has been mailed to the Holders of such Bonds and the Authority rescinds its election to make such Conversion, then the Variable Rate Bonds shall continue to be subject to mandatory tender for purchase on the date which would have been the effective date of the Conversion.

No Conversion from one Interest Rate Period to another shall take effect unless each of the following conditions, to the extent applicable, shall have first been satisfied:

(1) With respect to the new Interest Rate Period, there shall be in effect a Liquidity Facility if and as required under the Bond Resolution.

(2) The Fiscal Agent shall have received a Favorable Opinion of Bond Counsel with respect to such Conversion dated the effective date of such Conversion.

(3) In the case of any Conversion with respect to which there shall be no Liquidity Facility in effect to provide funds for the purchase of Variable Rate Bonds on the Conversion Date, the remarketing proceeds available on the Conversion Date shall not be less than the amount required to purchase all of the Variable Rate Bonds at the Tender Price (not including any premium).

(4) In the case of any Conversion of the Variable Rate Bonds to any Indexed Put Interest Rate Period, prior to the Conversion Date, the Authority shall have appointed a Tender Agent and a Remarketing Agent.

In the case of failure to meet these conditions: (1) the Variable Rate Bonds shall bear interest at a Weekly Interest Rate commencing on the date which would have been the effective date of the Conversion and (2) the Variable Rate Bonds shall continue to be subject to mandatory tender for purchase on the date which would have been the effective date of the Conversion.

*Conversion to Weekly Interest Rate.* The Authority may, from time to time, by written direction to the Fiscal Agent, the Tender Agent, the Initial Liquidity Facility Provider, the Remarketing Agent, the Auction Agent (if any), the Broker-Dealer (if any) and the Bond Insurer, elect that the Variable Rate Bonds shall bear interest at a Weekly Interest Rate. Such direction shall specify, among other things, (1) the proposed effective date of the Conversion to a Weekly Interest Rate, which shall be a Business Day not earlier than the 30<sup>th</sup> day following the second Business Day after receipt by the Fiscal Agent of such direction and (2) the Tender Date for the Variable Rate Bonds to be purchased, which shall be such proposed effective date. In addition, such direction shall be accompanied by a form of notice to be mailed to the Holders of the Variable Rate Bonds by the Fiscal Agent. During each Weekly Interest Rate Period for the Variable Rate Bonds commencing on a date so specified and ending on the day immediately preceding the effective date of the next succeeding Interest Rate Period, the interest rate borne by such Bonds shall be a Weekly Interest Rate.

### **Purchase of the Variable Rate Bonds**

*During Weekly Interest Rate Period.* Variable Rate Bonds (other than a Bank Bond) bearing interest at a Weekly Interest Rate shall be purchased in an Authorized Denomination from its Bondholder at the option of the Bondholder on any Business Day at a purchase price equal to the Tender Price, payable in immediately available funds, upon delivery to the Tender Agent at its designated office for delivery of the Variable Rate Bonds, to the Fiscal Agent at its corporate trust office and to the Remarketing Agent of an irrevocable notice by Electronic Means which states the principal amount of such Variable Rate Bonds, the principal amount thereof to be purchased and the date on which the same shall be purchased, which date shall be a Business Day not prior to the seventh day after the date of the delivery of such notice to the Tender Agent. Any notice delivered to the Tender Agent after 5:00 p.m., New York City time, shall be deemed to have been received on the next succeeding Business Day. Bank Bonds may not be tendered for purchase at the option of the Holder thereof. For payment of the Tender Price on the Tender Date, such Variable Rate Bonds must be delivered at or prior to 11:00 a.m., New York City time, on the Tender Date to the Tender Agent at its designated office for delivery of the Variable Rate Bonds accompanied by an instrument of transfer, in form satisfactory to the Tender Agent executed in blank by the Bondholder or its duly-authorized attorney, with such signature guaranteed by a commercial bank, trust company, member firm of the New York Stock Exchange or other eligible guarantor.

During any Weekly Interest Rate Period for which the book-entry-only system (see "Book-Entry Only System" herein) is in effect, any Variable Rate Bonds bearing interest at the Weekly Interest Rate or portion thereof in an Authorized Denomination shall be purchased on the date specified in the notice referred to below at the Tender



Price. The irrevocable notice by Electronic Means by the Participant shall be delivered on any Business Day by the Participant for such Variable Rate Bonds to the Tender Agent at its designated office for the delivery of such Variable Rate Bonds, to the Fiscal Agent at its corporate trust office and to the Remarketing Agent. That notice shall state the principal amount of such Bonds or portion thereof to be purchased and the date on which the same shall be purchased, which date shall be a Business Day at least seven days after the date of delivery of such notice to the Fiscal Agent. Upon confirmation by the Securities Depository to the Fiscal Agent that such Participant has an ownership interest in the Variable Rate Bonds at least equal to the amount of Variable Rate Bonds specified in such irrevocable written notice, payment of the Tender Price of such Bonds shall be made by 4:00 p.m., New York City time, or as soon as practicably possible thereafter, upon the receipt by the Fiscal Agent of the Tender Price on the Business Day specified in the notice upon the transfer on the registration books of the Securities Depository of the beneficial ownership interest in such Variable Rate Bonds tendered for purchase to the account of the Tender Agent, or a Participant acting on behalf of such Tender Agent, at or prior to 11:00 a.m., New York City time, on the date specified in such notice.

*Mandatory Tender for Purchase on First Day of Each Interest Rate Period.* The Variable Rate Bonds shall be subject to mandatory tender for purchase on the first day of each Interest Rate Period at the Tender Price, payable in immediately available funds. For payment of the Tender Price on the Tender Date, Variable Rate Bonds must be delivered at or prior to 11:00 a.m., New York City time, on the Tender Date. If delivered after that time, the Tender Price shall be paid on the next succeeding Business Day.

*Mandatory Tender for Purchase upon Termination, Replacement or Expiration of Liquidity Facility or on Bond Insurance Substitution Date; Mandatory Standby Tender.* If at any time the Fiscal Agent gives notice that the Tender Price on the Variable Rate Bonds tendered for purchase shall cease to be subject to purchase pursuant to the Liquidity Facility then in effect with respect to said Variable Rate Bonds as a result of (i) the termination, replacement or expiration of the term, as extended, of such Liquidity Facility, including but not limited to termination at the option of the Authority in accordance with the terms of such Liquidity Facility, or (ii) the occurrence of a Mandatory Standby Tender (as defined below), then each such Variable Rate Bond shall be purchased or deemed purchased at the Tender Price. Any purchase of such Variable Rate Bonds pursuant to the foregoing events shall occur: (1) on the fifth Business Day preceding any such termination, replacement or expiration of such Liquidity Facility without replacement by an Alternate Liquidity Facility or upon any termination thereof as a result of a Mandatory Standby Tender, and (2) on the date of the replacement of a Liquidity Facility, in any case where an Alternate Liquidity Facility has been delivered to the Tender Agent. In the case of any replacement, the existing Liquidity Facility will be drawn to pay the Tender Price, if necessary, rather than the Alternate Liquidity Facility. No such mandatory tender will be effected upon the replacement of a Liquidity Facility in the case where the Liquidity Facility is failing to honor conforming draws. "Mandatory Standby Tender" means the mandatory tender of the Variable Rate Bonds upon receipt by the Fiscal Agent of written notice from the Liquidity Facility Provider that an event with respect to the Liquidity Facility has occurred which gives the Liquidity Facility Provider the option to terminate such Liquidity Facility upon notice. Mandatory Standby Tender shall not include circumstances where the Liquidity Facility Provider may suspend or terminate its obligations to purchase Variable Rate Bonds without notice, in which case there will be no mandatory tender.

If at any time the Fiscal Agent receives notice that a substitute bond insurance policy will be delivered, then each Variable Rate Bond shall be purchased or deemed purchased at the Tender Price. Any purchase of such Variable Rate Bond shall occur on the Business Day preceding the delivery of a substitute bond insurance policy.

Payment of the Tender Price of any such Variable Rate Bonds shall be made in immediately available funds by 4:00 p.m., New York City time, on the Tender Date upon delivery of such Variable Rate Bonds to the Tender Agent at its designated office for delivery of Variable Rate Bonds, accompanied by an instrument of transfer, in form satisfactory to the Tender Agent, executed in blank by the Bondholder with the signature of such Bondholder guaranteed by a commercial bank, trust company, member firm of the New York Stock Exchange or other eligible guarantor, at or prior to 12:00 noon, New York City time, on the Tender Date. If, as a result of any such Mandatory Standby Tender, expiration, termination with notice or replacement of a Liquidity Facility, the Variable Rate Bonds are no longer subject to purchase pursuant to such Liquidity Facility, the Tender Agent (upon receipt from the Holder thereof in exchange for payment of the Tender Price thereof) shall present such Variable Rate Bonds to the Fiscal Agent for notation of such fact thereon.

*Consent and Notice.* The Authority may not enter into any agreement or consent to or participate in any arrangement pursuant to which the Variable Rate Bonds are tendered or purchased for any purpose other than the redemption and cancellation of such Bonds without the prior written consent of the Bond Insurer. In connection with any mandatory tender for purchase of the Variable Rate Bonds, the Fiscal Agent shall give the notice in accordance with the Bond Resolution.

Such notice shall state (i) in the case of a mandatory tender for purchase on the first day of each Interest Rate Period, the type of Interest Rate Period to commence on such mandatory purchase date; (ii) in the case of a mandatory tender for purchase upon termination, replacement or expiration of the Liquidity Facility, on a bond insurance substitution date or Mandatory Standby Tender, that the Liquidity Facility will expire, terminate or be replaced and that the Variable Rate Bonds will no longer be payable from the Liquidity Facility and that any rating applicable to such Variable Rate Bonds may be reduced or withdrawn; (iii) that the Tender Price of any Variable Rate Bonds subject to mandatory tender for purchase shall be payable only upon surrender of that Variable Rate Bond or Obligations to the Tender Agent at its designated office for delivery of applicable Variable Rate Bonds, accompanied by an instrument of transfer, in form satisfactory to the Tender Agent, executed in blank by the Bondholder or its duly-authorized attorney, with such signature guaranteed by a commercial bank, trust company, member firm of the New York Stock Exchange or other eligible guarantor; (iv) that, provided that moneys sufficient to effect such purchase shall have been provided through the remarketing of such Variable Rate Bonds by the Remarketing Agent, through said Liquidity Facility or funds provided by the Authority, all Variable Rate Bonds subject to mandatory tender for purchase shall be purchased on the mandatory Tender Date; and (v) that if any Holder of a Variable Rate Bond subject to mandatory tender for purchase does not surrender that Variable Rate Bond to the Tender Agent for purchase on the mandatory Tender Date, then that Variable Rate Bond shall be deemed to be an Undelivered Bond, no interest shall accrue on that Variable Rate Bond on and after the mandatory Tender Date and such Holder shall have no rights under the Bond Resolution other than to receive payment of the Tender Price.

*Payment of Tender Price by Authority.* If all or a portion of the Variable Rate Bonds tendered for purchase cannot be remarketed and the Liquidity Facility Provider fails to purchase all or any part of the unremarketed portion of such tendered Variable Rate Bonds in accordance with the Liquidity Facility on a Tender Date, the Authority may at its option, but shall not be obligated to, pay to the Tender Agent as soon as practicable on a Tender Date immediately available funds (together with any remarketing proceeds and any funds provided under said Liquidity Facility) sufficient to pay the Tender Price on the Variable Rate Bonds tendered for purchase. The Tender Agent shall deposit the amount paid by the Authority, if any, in the Authority Purchase Account of the Bond Purchase Fund pending application of the money to the payment of the Tender Price.

### **Initial Liquidity Facility**

*General.* In connection with the Series M-3 Bonds, the Authority has initially arranged for the Initial Liquidity Facility Provider to provide an Initial Liquidity Facility, in the form of a Standby Bond Purchase Agreement, to be dated as of December 20, 2007, by and among the Initial Liquidity Facility Provider, the Tender Agent and the Authority (the "Standby Purchase Agreement"). The obligation of the Initial Liquidity Facility Provider to purchase Series M-3 Bonds under the Standby Purchase Agreement will expire on December 20, 2010, prior to the final maturity of the Series M-3 Bonds, unless extended or terminated in accordance with its terms.

During the term of the Standby Purchase Agreement, the Initial Liquidity Facility Provider will provide liquidity for the purchase of the Series M-3 Bonds, which Series M-3 Bonds are delivered to the Tender Agent pursuant to an optional or mandatory tender but not remarketed by the Series M-3 Remarketing Agent. In addition, the Standby Purchase Agreement will provide liquidity for the mandatory purchase of Tendered Bonds (i) upon certain changes in interest rate periods, (ii) upon the expiration (without extension) of the Standby Purchase Agreement, (iii) except as otherwise provided in the Bond Resolution, upon the replacement of the Standby Purchase Agreement with an Alternate Liquidity Facility and (iv) at the direction of the Initial Liquidity Facility Provider following the occurrence of certain Events of Termination or Events of Default. The Authority has the right and may elect to terminate the Standby Purchase Agreement in its discretion. Unless otherwise noted, all capitalized terms in this summary of the Standby Purchase Agreement shall have the respective meanings ascribed to such terms in the Standby Purchase Agreement.

UNDER CERTAIN CIRCUMSTANCES THE OBLIGATIONS OF THE INITIAL LIQUIDITY FACILITY PROVIDER TO PURCHASE SERIES M-3 BONDS TENDERED BY THE OWNERS THEREOF OR SUBJECT TO MANDATORY TENDER MAY BE TERMINATED OR SUSPENDED WITHOUT A PURCHASE BY THE INITIAL LIQUIDITY FACILITY PROVIDER. IN SUCH EVENT, SUFFICIENT FUNDS MAY NOT BE AVAILABLE TO PURCHASE SERIES M-3 BONDS TENDERED BY THE OWNERS THEREOF OR SUBJECT TO MANDATORY PURCHASE. IN ADDITION, THE STANDBY PURCHASE AGREEMENT DOES NOT PROVIDE SECURITY FOR THE PAYMENT OF PRINCIPAL OF OR INTEREST OR PREMIUMS, IF ANY, ON THE SERIES M-3 BONDS. THE STANDBY PURCHASE AGREEMENT PROVIDES FOR THE PURCHASE OF APPLICABLE TENDERED SERIES M-3 BONDS ONLY.

*Purchase of Tendered Bonds by Provider.* The Initial Liquidity Facility Provider has agreed to purchase during the Purchase Period, Eligible Bonds which have been tendered for optional purchase or which are tendered for mandatory purchase and which are not remarketed as provided in the Bond Resolution. The Purchase Period begins on the date of initial delivery of the Series M-3 Bonds (expected to be December 20, 2007) and ends on the earliest of (a) the respective dates set forth in the first paragraph under "General" above or the last day of any extension of such date pursuant to the terms of the Standby Purchase Agreement (the "Stated Expiration Date"); (b) the date of receipt by the Initial Liquidity Facility Provider of a certificate signed by the Tender Agent stating that the Standby Purchase Agreement has been terminated pursuant to the terms of the Bond Resolution because (i) an Alternate Liquidity Facility has become effective under the Bond Resolution provided that the Standby Purchase Agreement shall not terminate until the Initial Liquidity Facility Provider has purchased any Series M-3 Bonds required to be purchased pursuant to any mandatory tender resulting from the provision of an Alternate Liquidity Facility; (ii) no Series M-3 Bonds are outstanding under the Bond Resolution; or (iii) all of the Series M-3 Bonds have been converted to a Non-Covered Interest Rate provided that the Standby Purchase Agreement shall not terminate until the Initial Liquidity Facility Provider has purchased any Series M-3 Bonds required to be purchased pursuant to such conversion; (c) the date specified in a written notice delivered by the Authority to the Initial Liquidity Facility Provider and the Tender Agent that the Authority has elected to terminate the Standby Purchase Agreement pursuant to its terms; (d) the occurrence of an Event of Termination (as further described below); and (e) the date on which the Initial Liquidity Facility Provider's commitment has been terminated in its entirety and the Initial Liquidity Facility Provider is no longer obligated to purchase Series M-3 Bonds. The price to be paid by the Initial Liquidity Facility Provider for such Bonds will be equal to the aggregate principal amount on such Bonds without premium, plus interest accrued thereon on the Purchase Date, unless, in the case of interest, the Purchase Date is an Interest Payment Date. As described below, under certain circumstances the obligation of the Provider to purchase Tendered Bonds will be automatically suspended or terminated, without prior notice or demand, and the Tender Agent will be unable to require the purchase of Series M-3 Bonds under the Standby Purchase Agreement.

Each of the following is an "Event of Termination" under the Standby Purchase Agreement:

(a) (i) Any principal or interest due on the Series M-3 Bonds is not paid when due and such principal or interest is not paid by the Bond Insurer when, as, and in the amounts required to be paid pursuant to the terms of the MBIA Insurance Policy or (ii) the Authority provides notice that the Bond Insurer shall be substituted as insurer of the Series M-3 Bonds, or the MBIA Insurance Policy is surrendered, cancelled, terminated, or modified in any material respect, without the Initial Liquidity Facility Provider's prior written consent; or

(b) The Bond Insurer in writing shall claim that the MBIA Insurance Policy with respect to the payment of principal of or interest on the Series M-3 Bonds is not valid and binding on it, and repudiate its obligations under the MBIA Insurance Policy with respect to payment of principal of or interest on the Bonds or it shall initiate any legal proceedings to seek an adjudication that such policy, with respect to the payment of principal or interest or special redemption of the Series M-3 Bonds, is not valid and binding, or any court or Governmental Authority with jurisdiction to rule on the validity of the MBIA Insurance Policy shall find or rule that the MBIA Insurance Policy is not so valid and binding; or

(c) The occurrence of an Insurer Event of Insolvency (as defined in the Standby Bond Purchase Agreement); or

(d) The withdrawal or suspension by S&P, Moody's and Fitch of the financial strength rating of the Bond Insurer or the reduction of such rating below BBB- in the case of S&P, Baa3 in the case of Moody's, and BBB- in the case of Fitch; or

(e) Any default by the Bond Insurer in making payment when, as, and in the amounts required to be made pursuant to the express terms and provisions of any other financial guaranty insurance policy issued by it insuring publicly-rated bonds and such failure shall continue for thirty (30) days unless its obligation to pay is being contested by the Bond Insurer in good faith by appropriate proceedings; or

(f) The Bond Insurer shall fail to maintain a financial strength or claims paying ability rating by Moody's of Aa3 (or its equivalent) or higher or by S&P of AA- (or its equivalent) or higher or by Fitch of AA- (or its equivalent) or higher for the applicable grace period specified in the Standby Purchase Agreement.

Each of the following is an "Event of Default" under the Standby Purchase Agreement:

(a) Any material representation or warranty made by the Authority under or in connection with the Standby Purchase Agreement shall prove to be untrue in any material respect on the date as of which it was made; or

(b) Non-payment of any commitment fees within ten (10) days after the Tender Agent, the Bond Insurer and the Authority have received written notice from the Initial Liquidity Facility Provider that the same were not paid when due; or

(c) Non-payment of any other fees or amounts payable under the Standby Purchase Agreement (together with interest thereon at the Default Rate) within twenty (20) days after the Tender Agent, the Bond Insurer and the Authority have received written notice thereof from the Initial Liquidity Facility Provider that the same were not paid when due; or

(d) The breach by the Authority of certain covenants under the Standby Purchase Agreement;  
or

(e) The breach by the Authority of any terms or provisions of the Standby Purchase Agreement for which no cure period is otherwise specifically provided with respect thereto which is not remedied within thirty (30) days after the Bond Insurer and the Authority have received written notice thereof from the Initial Liquidity Facility Provider; or

(f) (i) The Authority shall commence any case, proceeding or other action under any existing or future applicable law, (A) relating to bankruptcy, insolvency, reorganization or relief of debtors, seeking to have an order for relief entered with respect to it, or seeking to adjudicate it a bankrupt or insolvent, or seeking reorganization, arrangement, adjustment, winding-up, liquidation, dissolution, composition or other relief with respect to it or its debts, or (B) seeking appointment of a receiver, trustee, custodian or other similar official for it or for all or any substantial part of its assets, or the Authority shall make a general assignment for the benefit of its creditors; or (ii) there shall be commenced against the Authority any case, proceeding or other action of a nature referred to in clause (i) above which (A) results in an order for such relief or in the appointment of a receiver or similar official or (B) remains undismissed, undischarged or unbonded for a period of sixty (60) days; or (iii) there shall be commenced against the Authority any case, proceeding or other action seeking issuance of a warrant of attachment, execution, distraint or similar process against all or any substantial part of its assets, which results in the entry of an order for any such relief which shall not have been vacated, discharged, or stayed or bonded pending appeal within sixty (60) days from the entry thereof; or (iv) the Authority shall take any action in furtherance of, or indicating its consent to, approval of, or acquiescence in, any of the acts set forth in clause (i), (ii) or (iii) above; or (v) the Authority shall generally not, or shall be unable to, or shall admit in writing its inability to, pay its debts; or

(g) Any material provision of the Standby Purchase Agreement or any Related Document (other than the MBIA Insurance Policy) shall at any time for any reason cease to be valid and binding on the Authority or shall be declared to be null and void, or the validity or enforceability thereof shall be contested by the Authority or by any Governmental Authority having jurisdiction, or the Authority shall deny that it has any further liability or obligation under any such document, or such document is cancelled or terminated without the Initial Liquidity Facility Provider's prior written consent; or

(h) The occurrence of any "event of default" as defined in any of the Related Documents, which occurrence is not waived pursuant to the terms thereof and which occurrence is not otherwise described in the Standby Purchase Agreement, other than the failure of the Initial Liquidity Facility Provider to provide funds for the purchase of Tendered Bonds when required by the terms and conditions of the Standby Purchase Agreement; or

(i) The Authority shall have defaulted in the payment or performance of any obligation of a principal amount of \$10,000,000 or more, which constitutes Debt, and such default permits the acceleration of the payment of moneys; or

(j) The rating assigned by S&P or Moody's to the Authority's long-term debt (without taking into account third party credit enhancement) is withdrawn, suspended or reduced below BBB- (or its equivalent rating) by S&P or Baa3 (or its equivalent rating) by Moody's; or

(k) One or more judgments or orders for the payment of money in an aggregate amount in excess of \$10,000,000 shall be rendered against the Authority and such judgments or orders shall remain undischarged or unstayed for a period of thirty (30) days, or any action shall be taken by a judgment creditor to levy upon assets or properties of the Authority to enforce any such judgment or order.

*Remedies Upon an Event of Termination or an Event of Default.* If any Event of Termination or Event of Default occurs and is continuing, the Initial Liquidity Facility Provider has the following remedies under the Standby Purchase Agreement:

In the case of an Event of Termination specified in paragraphs (a), (c), (d), or (e) above, the Available Commitment, the Purchase Period and the obligation of the Initial Liquidity Facility Provider to purchase Series M-3 Bonds shall immediately terminate without notice or demand (a "Termination Event"), and thereafter the Initial Liquidity Facility Provider shall be under no obligation to purchase such Series M-3 Bonds. Promptly upon the Initial Liquidity Facility Provider's obtaining knowledge of any such Event of Termination, the Initial Liquidity Facility Provider shall give written notice of the same to the Tender Agent, the Authority, the Series M-3 Remarketing Agent and the Bond Insurer, and the Initial Liquidity Facility Provider shall incur no liability or responsibility whatsoever by reason of its failure to give such notice and such failure shall in no manner affect the immediate termination of its Available Commitment and of its obligation to purchase Series M-3 Bonds pursuant to the Standby Purchase Agreement.

In the case of an Event of Termination specified in paragraph (f) above, or non-payment of certain amounts specified in the Standby Purchase Agreement, the Initial Liquidity Facility Provider may terminate its Available Commitment and Purchase Period by giving written notice to the Tender Agent, the Authority, the Series M-3 Remarketing Agent and the Bond Insurer, specifying the date on which such Available Commitment and Purchase Period shall terminate, which shall be not less than thirty (30) days from the date of receipt of such notice by the Tender Agent (the "Purchase Termination Date"). On and after the Purchase Termination Date, the Initial Liquidity Facility Provider shall be under no further obligation to purchase Series M-3 Bonds under the Standby Purchase Agreement.

In the case of an Event of Termination specified in paragraph (b) above, the Initial Liquidity Facility Provider's obligation to purchase Series M-3 Bonds shall be immediately suspended without notice or demand and thereafter the Initial Liquidity Facility Provider shall be under no obligation to purchase Series M-3 Bonds until the Available Commitment is reinstated as described in the Standby Purchase Agreement. Promptly upon the Initial Liquidity Facility Provider's obtaining knowledge of any such Event of Termination, it shall give written notice of the same to the Authority, the Tender Agent, the Series M-3

Remarketing Agent and the Bond Insurer, and the Initial Liquidity Facility Provider shall incur no liability or responsibility whatsoever by reason of its failure to give such notice and such failure shall in no way affect the suspension of the Initial Liquidity Facility Provider's obligation to purchase Series M-3 Bonds. If a court with jurisdiction to rule on the validity of the MBIA Insurance Policy shall thereafter enter a final, nonappealable judgment that it is not valid and binding on the Bond Insurer, then the Initial Liquidity Facility Provider's obligation to purchase Series M-3 Bonds shall immediately terminate. If such court shall find or rule that the MBIA Insurance Policy is valid and binding, the Initial Liquidity Facility Provider's obligation to purchase Series M-3 Bonds shall be automatically reinstated and the terms of the Standby Purchase Agreement will continue in full force and effect (unless otherwise terminated or suspended by its terms). Notwithstanding the foregoing, if, upon the earlier of the Stated Expiration Date and the date which is three (3) years after the effective date of suspension of the Initial Liquidity Facility Provider's obligation, litigation is still pending and a judgment regarding the validity of the MBIA Insurance Policy as is the subject of such Event of Termination has not been obtained, then the corresponding Available Commitment and the obligation of the Initial Liquidity Facility Provider to purchase Series M-3 Bonds shall at such time immediately terminate, and thereafter the Initial Liquidity Facility Provider shall be under no obligation to purchase such Series M-3 Bonds.

During the pendency of an Event of Termination pursuant to paragraphs (c) (with respect to an order described in clause (i) of paragraph (c), and prior to the expiration of the specified period) or (e) (prior to the expiration of the specified period) above (each a "Potential Event of Termination"), the Initial Liquidity Facility Provider's obligation to purchase Series M-3 Bonds shall be immediately suspended without notice or demand and thereafter the Provider shall be under no obligation to purchase Series M-3 Bonds until the Available Commitment is reinstated as described hereafter. Promptly upon the Initial Liquidity Facility Provider obtaining knowledge of any such Potential Event of Termination, it shall give written notice of the same to the Authority, the Tender Agent, the Series M-3 Remarketing Agent and the Bond Insurer, and it shall incur no liability or responsibility whatsoever by reason of its failure to give such notice and such failure shall in no way affect the suspension of its obligations under the Standby Purchase Agreement. In the event such Potential Event of Termination is cured prior to becoming a Termination Event, the Initial Liquidity Facility Provider's obligations shall be automatically reinstated and the terms of the Standby Purchase Agreement will continue in full force and effect (unless it is otherwise terminated or suspended by its terms).

In addition to the rights and remedies set forth in the preceding paragraphs, in the case of any Event of Termination or Event of Default, upon the election of the Initial Liquidity Facility Provider: (i) all amounts payable under the Standby Purchase Agreement (other than payments of principal and redemption price of and interest on the Series M-3 Bonds or payments of Excess Bond Interest related thereto) shall upon notice to the Authority become immediately due and payable without presentment, demand, protest or further notice of any kind, all of which are expressly waived by the Authority; and (ii) the Initial Liquidity Facility Provider shall have all the rights and remedies available to it under the Standby Purchase Agreement, the Related Documents, the MBIA Insurance Policy or otherwise pursuant to law or equity, but it shall not have the right to terminate its obligation to purchase Series M-3 Bonds or to declare any amount due hereunder due and payable except as expressly provided, or to accelerate the maturity date of any such Bonds except as provided in the Bond Resolution. Without limiting the generality of the foregoing, the Initial Liquidity Facility Provider agrees to purchase Series M-3 Bonds on the terms and conditions of the Standby Purchase Agreement notwithstanding the institution or pendency of any bankruptcy, insolvency or similar proceeding with respect to the Commonwealth. The Initial Liquidity Facility Provider will not assert as a defense to its obligation to purchase Series M-3 Bonds under the Standby Purchase Agreement (A) the institution or pendency of a bankruptcy, insolvency or similar proceeding with respect to the Authority, or (B) a determination by a court of competent jurisdiction in a bankruptcy, insolvency or similar proceeding with respect to the Authority that the Standby Purchase Agreement is not enforceable against the Authority under applicable bankruptcy, insolvency or similar laws. This paragraph shall not limit the exercise of its remedies expressly provided for above.

*Extension, Reduction, Adjustment or Termination of the Standby Purchase Agreement.* The Standby Purchase Agreement will expire on the date set forth under "General" above unless earlier terminated or, with the

consent of the Initial Liquidity Facility Provider in its sole and absolute discretion, extended for an additional period or periods, in each case in accordance with the provisions of the Standby Purchase Agreement.

Upon (i) any redemption, defeasance or other payment of all or any portion of the principal amount of the Series M-3 Bonds or (ii) any purchase by the Initial Liquidity Facility Provider of Series M-3 Bonds tendered or deemed tendered in accordance with the terms of the Bond Resolution, the Initial Liquidity Facility Provider's purchase commitment under the Standby Purchase Agreement with respect to principal of Series M-3 Bonds shall automatically be reduced by the principal amount of such Series M-3 Bonds so redeemed, defeased or otherwise paid or purchased, as the case may be. The Initial Liquidity Facility Provider's commitment with respect to interest initially shall be equal to \$1,726,028 (an amount equal to thirty-five (35) days' interest on the Series M-3 Bonds, computed as if such Series M-3 Bonds bore interest at the rate of twelve percent (12%) per annum), based on a year of 365/366 days actual days elapsed. The commitment with respect to interest will be adjusted downward by an amount in proportion to the reduction of the commitment as to principal because of the redemption, defeasance or other payment of Series M-3 Bonds or the purchase by the Initial Liquidity Facility Provider of Series M-3 Bonds tendered or deemed tendered in accordance with the terms of the Bond Resolution.

*Limitations of the Standby Purchase Agreement.* The ability to obtain funds under a Standby Purchase Agreement in accordance with its terms may be limited by federal or state law. Bankruptcy, conservatorship, receivership and similar laws governing financial institutions or any issuer of a standby purchase agreement may prevent or restrict payment under the Standby Purchase Agreement. To the extent the short-term rating on the Series M-3 Bonds depends on the rating of the Initial Liquidity Facility Provider, the short-term ratings on such Series M-3 Bonds could be downgraded or withdrawn if the Initial Liquidity Facility Provider were to be downgraded, placed on credit watch or have its ratings suspended or withdrawn or were to refuse to perform under the Standby Purchase Agreement.

The obligation of the Initial Liquidity Facility Provider to purchase unremarketed Series M-3 Bonds pursuant to the Standby Purchase Agreement is subject to the conditions and limitations set forth therein, and is also subject to all rights and defenses available to contracting parties generally. The Standby Purchase Agreement is not a guaranty to pay the purchase price of Series M-3 Bonds tendered for purchase. The Standby Purchase Agreement is a general contract, subject to certain conditions and limitations, but is not a letter of credit. Purchasers of the Series M-3 Bonds should consult their legal counsel for an explanation of the differences between a general contract and a letter of credit or guaranty.

### **Initial Liquidity Facility Provider**

JPMorgan Chase Bank, National Association ("the Bank") is a wholly owned bank subsidiary of JPMorgan Chase & Co., a Delaware corporation whose principal office is located in New York, New York. The Bank offers a wide range of banking services to its customers, both domestically and internationally. It is chartered and its business is subject to examination and regulation by the Office of the Comptroller of the Currency.

As of September 30, 2007, JPMorgan Chase Bank, National Association, had total assets of \$1,244.0 billion, total net loans of \$456.4 billion, total deposits of \$699.0 billion, and total stockholder's equity of \$102.9 billion. These figures are extracted from the Bank's unaudited Consolidated Reports of Condition and Income as at September 30, 2007, prepared in accordance with regulatory instructions that do not in all cases follow U.S. generally accepted accounting principles, which are filed with the Federal Deposit Insurance Corporation.

Additional information, including the most recent Form 10-K for the year ended December 31, 2006, of JPMorgan Chase & Co., the 2006 Annual Report of JPMorgan Chase & Co., and additional annual, quarterly and current reports filed with or furnished to the Securities and Exchange Commission by JPMorgan Chase & Co., as they become available, may be obtained without charge by each person to whom this Official Statement is delivered upon the written request of any such person to the Office of the Secretary, JPMorgan Chase & Co., 270 Park Avenue, New York, New York 10017.

The information contained in the preceding three paragraphs relates to and has been obtained from the Bank. The delivery of this Official Statement shall not create any implication that there has been no change in the affairs of the Bank since the date hereof, or that the information contained or referred to above is correct as of any time subsequent to its date.

## **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. The Authority does not 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 each series of the Bonds, each in the aggregate principal amount of such maturity, and will be deposited with DTC.

DTC, the world's largest depository, is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934, as amended. DTC holds and provides asset servicing for over 2.2 million issuers of U.S. and non-U.S. equity, corporate and municipal debt issues, and money market instruments from over 100 countries that DTC participants ("Direct Participants") deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions, in deposited securities through electronic computerized book-entry transfers and pledges between Direct Participants' accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("DTCC"). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Fixed Income Clearing Corporation, and Emerging Markets Clearing Corporation (NSCC, FICC, and EMCC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("Indirect Participants"). DTC has S&P's highest rating: "AAA." The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at [www.dtcc.com](http://www.dtcc.com) and [www.dtc.org](http://www.dtc.org).

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

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

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time. Beneficial Owners may wish to take certain steps to augment the transmission to them of notices of significant events with respect to the Bonds, such as redemptions, tenders, defaults, and proposed amendments to the bond



documents. For example, Beneficial Owners may wish to ascertain that the nominee holding the Bonds for their benefit has agreed to obtain and transmit notices to Beneficial Owners. In the alternative, Beneficial Owners may wish to provide their names and addresses to the Fiscal Agent and request that copies of notices be provided directly to them.

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

Neither DTC nor Cede & Co. (nor such other DTC nominee) will consent or vote with respect to the Bonds unless authorized by a Direct Participant in accordance with DTC's Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Authority 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).

Redemption proceeds, distributions, and dividend payments on the Bonds will be made to Cede & Co., or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts on payable dates in accordance with their respective holdings shown on DTC's records unless DTC has reason to believe that it will not receive payment on any such payable dates. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, nor its nominee, Fiscal Agent, or the Authority, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of redemption proceeds, distributions, and dividend payments to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Authority or the Fiscal Agent, disbursement of such payments to Direct Participants will be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners will be the responsibility of Direct and Indirect Participants.

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

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

### **Payments and Transfers**

No assurance can be given by the Authority that DTC will make prompt transfer of payments to the Participants or that Participants will make prompt transfer of payments to Beneficial Owners. The Authority 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 the Bonds shall be payable in lawful money of the United States of America at the corporate trust office of the Fiscal Agent, in New York, New York. Interest on the Bonds (other than the Series M-3 Bonds, the interest of which will be payable by wire transfer) will be payable by check mailed to the respective addresses of the registered owners determined as of the fifteenth (15<sup>th</sup>) day of the month preceding the interest payment date (or in the case of the Series M-3 Bonds, the Business Day immediately preceding the interest payment date) as shown on the registration books of the Authority maintained by the Fiscal Agent. The Bonds will be issued only as registered bonds without coupons in denominations of \$5,000 (\$100,000 in the case of the Series M-3 Bonds) or any integral

multiple thereof. The transfer of the Bonds will be registrable and they may be exchanged at the corporate trust office of the Fiscal Agent in New York, New York, upon the payment of any taxes or other governmental charges required to be paid with respect to such transfer or exchange.

## Redemption Provisions

### *Optional Redemption*

Series M-1 Bonds. The Series M-1 Bonds are not subject to optional redemption prior to maturity.

Series M-2 Bonds. During the Initial Term Rate Period, the Series M-2 Bonds shall be subject to redemption, at the option of the Authority, from any moneys that may be available for that purpose (other than moneys deposited in the Sinking Fund in respect of an Amortization Requirement), on July 1, 2017 and any day thereafter, in whole or in part, in the principal amount of the Series M-2 Bonds to be redeemed, together with the accrued interest thereon to the date fixed for redemption without premium. After the Initial Term Rate Period, the Series M-2 Bonds bearing interest at a Weekly Interest Rate shall be subject to redemption at the option of the Authority, in whole or in part (and if in part, such order of maturity as the Authority shall determine), at a redemption price of 100% of the principal amount thereof at any time. Any such redemption shall be made in the manner and under the terms and conditions provided in the 1995 Bond Resolution.

Series M-3 Bonds. Series M-3 Bonds bearing interest at a Weekly Interest Rate shall be subject to redemption at the option of the Authority, from any moneys that may be available for that purpose (other than moneys deposited in the Sinking Fund in respect of an Amortization Requirement) in whole or in part (and if in part, as the Authority shall determine), at a redemption price of 100% of the principal amount thereof at any time. Any such redemption shall be made in the manner and under the terms and conditions provided in the 1995 Bond Resolution.

Series N Bonds. The Series N Bonds maturing after July 1, 2017 at the time outstanding may be redeemed prior to their respective maturities, at the option of the Authority, from any moneys that may be available for that purpose (other than moneys deposited in the Sinking Fund in respect of an Amortization Requirement) either (a) in whole on any date not earlier than July 1, 2017, or (b) in part as directed by the Authority, on any date not earlier than July 1, 2017, at the principal amount of the Series N Bonds to be redeemed, together with the interest accrued thereon to the date fixed for redemption and without premium. Any such redemption shall be made in the manner and under the terms and conditions provided in the 1995 Bond Resolution.

Series O Bonds. The Series O Bonds are not subject to optional redemption prior to maturity.

### *Mandatory Redemption*

Series M-1 Bonds. The Series M-1 Bonds maturing on July 1, 2031, are subject to mandatory redemption prior to maturity, to the extent of the respective amortization requirements therefor set forth below at a redemption price equal to 100% of the outstanding principal amount thereof, together with accrued interest to the date fixed for redemption:

<u>Year</u>	<u>Amortization Requirements</u>
2029	\$ 4,660,000
2030	31,775,000
2031	29,815,000*

Series M-2 Bonds. The Series M-2 Bonds maturing on July 1, 2034 and 2035, are subject to mandatory redemption to the extent of the respective amortization requirements therefor set forth below at a redemption price

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\* Maturity.

equal to 100% of the outstanding principal amount thereof, together with accrued interest to the date fixed for redemption:

<u>Year</u>	<u>Amortization Requirements</u>	
	<u>2034</u>	<u>2035</u>
2031	\$ 85,000	
2032	2,160,000	
2033	2,145,000	
2034	64,910,000*	\$ 26,620,000
2035		33,380,000*

Series M-3 Bonds. The Series M-3 Bonds are subject to mandatory redemption to the extent of the respective amortization requirements therefor set forth below at a redemption price equal to 100% of the outstanding principal amount thereof, together with accrued interest to the date fixed for redemption:

<u>Year</u>	<u>Amortization Requirements</u>
2023	\$ 11,645,000
2024	34,785,000
2025	29,750,000
2026	5,740,000
2027	32,295,000
2028	35,785,000*

Notwithstanding anything to the contrary in the Bond Resolution, no amount of Series M-3 Bonds may be redeemed (other than pursuant to a sinking fund redemption) unless a proportionate amount of the Interest Rate Swap is terminated or reduced so that following such redemption the remaining notional amount of the Interest Rate Swap is not greater than the remaining principal amount of the Series M-3 Bonds, unless MBIA waives the requirement for such reduction of the Interest Rate Swap. The reduction in notional amount of the swap transaction shall be accomplished without causing the Authority to be in violation of, or in default under, the Bond Resolution and the Interest Rate Swap transaction documents.

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\* Maturity.

Series N Bonds. The Series N Bonds maturing on July 1, 2032 and 2037 are subject to mandatory redemption to the extent of the respective amortization requirements therefor set forth below at a redemption price equal to 100% of the outstanding principal amount thereof, together with accrued interest to the date fixed for redemption:

<b><u>Amortization</u></b>		
<b><u>Requirements</u></b>		
<b><u>Year</u></b>	<b><u>2032</u></b>	<b><u>2037</u></b>
2028	\$ 14,685,000	
2029	15,420,000	
2030	16,190,000	
2031	17,000,000	
2032	17,850,000*	
2033		\$ 18,740,000
2034		19,680,000
2035		20,660,000
2036		21,695,000
2037		22,780,000*

*Mandatory Tender*

The Series M-2 Bonds, during the Initial Term Rate Period, shall be subject to mandatory tender as set forth in the Series Resolution and described in *Description of the Bonds* herein. The Variable Rate Bonds are subject to mandatory tender as set forth in the Series Resolution and as described in "Description of the Variable Rate Bonds" under *Description of the Bonds* herein.

**Notice of Redemption; Effect of Redemption**

Any redemption of the Bonds, either in whole or in part, shall be made upon at least a 30-day prior notice by mail to DTC or, if the book-entry only system described above has been discontinued, by registered or certified mail, postage prepaid, to all registered owners of the Bonds to be redeemed 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 accrued interest on the Bonds or portions thereof so called for redemption being held by the Fiscal Agent, interest on the Bonds or portions thereof so called for redemption shall cease to accrue.

Each notice of redemption shall contain, among other things, the particular Bonds (or portions 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 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 of a subseries of Bonds are called for redemption, Bank Bonds of such subseries shall be selected for redemption by the Fiscal Agent by such method as it deems proper, before any other Bonds of such subseries shall be selected. All other Bonds of such subseries so called for redemption shall be selected (in Authorized Denominations) by the Fiscal Agent by such method as it deems fair and appropriate.

**SECURITY**

All Government Facilities Bonds will be secured equally and ratably by a pledge of rentals of the Leased Facilities. The Leased Facilities will not be mortgaged or otherwise encumbered to secure any Government

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\* Maturity.

Facilities Bonds. The Enabling Act provides that the good faith and credit of the Commonwealth are pledged for the payment of rentals under any lease agreement with any department of the Commonwealth and to the making of advances by the Secretary of the Treasury to the Authority of any unpaid portion of rentals payable to the Authority by any agency or instrumentality of the Commonwealth. The Enabling Act also provides that the good faith and credit of any municipality entering into a lease agreement with the Authority are pledged for the payment of any rentals thereunder.

**The Bonds are further secured by the guaranty of the Commonwealth, under which the Commonwealth pledges to draw from any funds available in the Treasury of Puerto Rico such sums as may be necessary to cover any deficiency in the amount required for the payment of principal of and interest on the Bonds. The good faith and credit of the Commonwealth, as in the case of the Commonwealth's general obligation bonds, are pledged for such payments.**

### **Commonwealth Guaranty**

As provided in Act No. 17 of the Legislature of Puerto Rico, approved on April 11, 1968, as amended (the "Guaranty Act") the Commonwealth guarantees the payment of the principal of and interest on the Government Facilities Bonds as described below.

"The Commonwealth of Puerto Rico hereby guarantees payment of the principal and the interest on bonds outstanding at any one time, in an aggregate principal amount not exceeding \$3,325,000,000 issued from time to time by the Authority for the development of its capital improvements as authorized by Act No. 56. The bonds covered by this guaranty shall be those specified by the Authority, and a statement of such guaranty shall be set forth on the face of such bonds. If at any time the revenues or income, and any other moneys of the Authority, pledged for the payment of the principal and the interest on such bonds, are not sufficient to pay such principal and interest as the same fall due, or to maintain the reserve fund that the Authority has pledged itself to maintain for such bonds, the Secretary of the Treasury shall draw from any funds available in the Treasury of Puerto Rico, such sums as may be necessary to cover the deficiency in the amount required for the payment of such principal and interest and to restore said reserve fund to the maximum requirement agreed to by the Authority, and shall direct that the sums so drawn be applied to such payment and purpose. For the purposes of this Section, the bonds that have been refinanced and for which the payment thereof when due or redeemed has been reserved through a special reserve, a secured investment contract or other acceptable guarantee, shall not be deemed as outstanding bonds. The good faith and credit of the Commonwealth of Puerto Rico are hereby pledged for such payments."

The Bonds have been specified by the Authority to be guaranteed by the Commonwealth under the Guaranty Act. Following the issuance of the Bonds, the Authority will have \$3,098,773,182 aggregate principal amount of bonds outstanding which are covered by the Guaranty Act, consisting of \$54,515,000 of bonds issued under Resolution No. 77, adopted by the Authority on November 16, 1970, as amended (the "1970 Bond Resolution"), \$97,655,000 of bonds issued under Resolution No. 158, adopted by the Authority on February 14, 1978, as amended (the "1978 Bond Resolution"), and \$2,946,603,182 of bonds issued under the 1995 Bond Resolution, calculated in each case by excluding the accretion on capital appreciation bonds and convertible capital appreciation bonds. See *Debt of the Authority and Debt Service Requirements*.

To date, no payments have ever been required under the Guaranty Act.

### **Opinion of the Secretary of Justice of the Commonwealth**

Prior to or concurrently with the delivery of the Bonds, the Secretary of Justice of the Commonwealth will have rendered his opinion to the Authority stating:

"I have examined Act No. 56 of the Legislature of Puerto Rico, approved June 19, 1958, as amended, creating the Puerto Rico Public Buildings Authority (the "Authority") as a body corporate and politic constituting an instrumentality of the Commonwealth of Puerto Rico exercising public and essential governmental functions. I have also examined Act No. 17 of the Legislature of Puerto Rico, approved April 11, 1968, as amended (the "Guaranty Act"), providing for the guaranty of the Commonwealth of

Puerto Rico of the payment of the principal of and interest on a principal amount of bonds of the Authority outstanding at any one time, not exceeding \$3,325,000,000, specified by the Authority to be covered by such guaranty, to the extent that the revenues and other moneys of the Authority pledged to the payment of such principal and interest are not sufficient for that purpose. I have also examined the Puerto Rico Constitution and such other laws of the Commonwealth of Puerto Rico as I consider necessary for the purpose of the following opinion.

From such examination, I am of the opinion that:

1. The Authority is lawfully authorized to specify up to \$3,325,000,000 aggregate principal amount of bonds of the Authority outstanding at any one time, issued for any of its authorized purposes, to be covered by the guaranty of the Commonwealth of Puerto Rico under the Guaranty Act, and the Commonwealth of Puerto Rico will be obligated to pay the principal of and the interest on the bonds so specified to be covered by said guaranty, if and to the extent that the revenues and other moneys of the Authority pledged to the payment of such principal and interest are not sufficient to make such payments as the same become due.

2. Any amounts required to be paid by the Commonwealth of Puerto Rico under said guaranty will constitute public debt within the meaning of Section 8 of Article VI of the Puerto Rico Constitution which provides:

In case the available revenues including surplus for any fiscal year are insufficient to meet the appropriations made for that year, interest on the public debt and amortization thereof shall first be paid, and other disbursements shall thereafter be made in accordance with the order of priorities established by law and will accordingly be entitled to the same priority of payment under such Section as the direct bonded indebtedness of the Commonwealth of Puerto Rico.

3. Because of its sovereign immunity, the Commonwealth of Puerto Rico cannot be sued without the consent of the Legislature of Puerto Rico. However, the Secretary of the Treasury can be required in a court of justice under the provisions of Section 2 of Article VI of the Puerto Rico Constitution to apply the available revenues including surplus to the payment of interest on the public debt and the amortization thereof in any case provided for by Section 8 of Article VI, including any payments required to be made under said guaranty, at the suit of any holder of bonds issued by the Authority and guaranteed pursuant to the Guaranty Act.

4. The Commonwealth guaranty of the \$562,850,000 Puerto Rico Public Buildings Authority Government Facilities Revenue Refunding Bonds, Series M; the \$329,415,000 Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds, Series N; and the \$3,025,000 Puerto Rico Public Buildings Authority Government Facilities Revenue Refunding Bonds, Series O constitutes a general obligation of the Commonwealth to which its full faith and credit and taxing power are pledged.

5. Although without specific judicial decision on point, I firmly understand and am of the opinion that, for purposes of the principal amount limitation expressed in the Guaranty Act, the initial principal amount of any capital appreciation bonds constitutes the principal amount of such bonds until such bonds are retired and any accreted value above said initial principal amount constitutes interest on such bonds."

## **Lease Agreements**

In accordance with the provisions of the 1995 Bond Resolution, the Authority has entered into certain lease agreements (the "Lease Agreements") with various departments, agencies, instrumentalities, and municipalities of the Commonwealth with respect to the Leased Facilities. The Lease Agreements require the corresponding lessees to pay to the Authority annual rentals in substantially equal monthly installments. The rentals are calculated by taking into account the following factors: (1) the interest on and principal of (including any amortization requirements) and redemption premium, if any, on Government Facilities Bonds issued to finance or refinance such Leased Facilities; (2) any amounts necessary to pay the general administrative expenses of the Authority related to

the Leased Facilities; and (3) any amounts necessary to provide and maintain a reserve fund for the replacement of major items of equipment comprising a portion of such Leased Facilities. The Lease Agreements may also require the lessees to pay certain amounts on account of the principal of and interest on outstanding notes issued to provide interim financing for the initial development and construction of the Leased Facilities.

Each Lease Agreement with respect to a specific facility or facilities terminates when the Government Facilities Bonds (as well as any notes issued to provide interim financing) which were issued to finance or refinance the acquisition or construction of such facility or facilities have been paid in full. All Lease Agreements provide for the adjustment of rentals so that the total amounts payable will be sufficient to meet the required debt service charges. Additionally, each Lease Agreement provides that the obligation of the lessee to pay rentals is absolute and unconditional.

Under the 1995 Bond Resolution, the Authority is required to forward, upon receipt, the portion of the rental payment from the lessees corresponding to the debt service payments on the Bonds (as well as any notes issued to provide interim financing) to the Fiscal Agent. The Authority has experienced certain delays in the payment of monthly rentals by some lessees. In an effort to eliminate these delays, the Authority entered into an Inter-Agency Agreement (the "Inter-Agency Agreement") with Government Development Bank, the Puerto Rico Office of Management and Budget ("OMB"), and the Puerto Rico Department of the Treasury (the "Treasury Department") in 2001. Under the Inter-Agency Agreement, OMB instructs the Treasury Department to forward the funds necessary to pay rentals under Lease Agreements to Government Development Bank, which funds are, in turn, deposited in a special account of the Authority at Government Development Bank. The portion of such rentals that is to be used to pay debt service on the Bonds remains in such account pending delivery to the Fiscal Agent prior to the debt service becoming due and payable. The remainder is forwarded to the Authority to cover its general administrative expenses related to the Lease Facilities as well as any amounts necessary to provide and maintain a reserve fund for the replacement of major items of equipment comprising a portion of such Leased Facilities.

During recent fiscal years, the Commonwealth has experienced a budget imbalance. Given the budgetary constraints of the Commonwealth, the Legislature has not appropriated sufficient funds to provide the Authority with the aggregate amount of rental payments provided for in the Lease Agreements. Consequently, OMB has been unable to instruct the Treasury Department to forward to Government Development Bank the full amount of rental payments payable under the Lease Agreements. Nevertheless, OMB has always instructed the Treasury Department to forward to Government Development Bank sufficient funds to pay all interest on and principal of (including any amortization requirements) and redemption premium, if any, on Government Facilities Bonds as well as a portion of general administrative expenses of the Authority related to the Leased Facilities. No funds have been provided to replenish or maintain the reserve for the replacement of major items of equipment comprising a portion of such Leased Facilities, which as of November 30, 2007, has no funds deposited therein.

In recent years there has been a shortfall between the amounts budgeted by the Authority to cover all of its expenses and the actual amounts which the Authority is required to receive in payments under Lease Agreements to cover its operating (non-debt service) expenses and contribution to reserves. For fiscal year 2008 the expected shortfall is approximately \$67 million.

The Authority, in anticipation of past and current budgeted shortfalls, has undertaken and continues to undertake certain fiscal measures to cover such shortfalls, including:

- Obtaining a \$75 million line of credit from Government Development Bank to cover the budgetary shortfall in fiscal year 2006.
- Divesting itself of real estate which the Authority does not contemplate developing or constructing. For fiscal year 2008, the Authority expects to generate approximately \$45 million from such sales of real estate.
- Implementing a hiring freeze for new employees, with the exception of select technical positions.
- Implementing various operational cost saving measures aimed at obtaining administrative efficiencies as well as a managerial reorganization, including a voluntary employee reduction plan

and the merging of various job positions throughout the Authority. The Authority expects the voluntary employee reduction plan to generate annual savings estimated at \$16 million.

- Implementing effective collection methods for past due rentals and entering into payment plans with departments, agencies, instrumentalities, and municipalities for the collection of such past due rentals. In addition, debt service savings generated by the issuance of the Series M Bonds will be directed to reduce the balance of past due rentals payable by such departments, agencies, instrumentalities, and municipalities to the Authority.

The Authority also anticipates that for fiscal year 2009 and beyond, as the Commonwealth's budgetary imbalance corrects, the Legislature will be able to appropriate sufficient funds to cover the aggregate amount of rental payments provided for in the Lease Agreements. Accordingly, the budgetary shortfalls currently being experienced by the Authority are expected to be reduced or eliminated. However, should the Authority experience budgetary shortfalls in the future, the divestiture of additional real estate which the Authority does not contemplate developing or constructing is projected to provide additional resources to cover a portion of such shortfalls through fiscal year 2009.

The shortfalls in the payment of rentals have not affected the Authority's ability to pay its debt service, and there have been no defaults or delays in the payment of the principal of or interest on any indebtedness of the Authority.

#### **Pledge of the Commonwealth to Pay or Advance Rentals**

Under the 1995 Bond Resolution, the Authority has covenanted that if any department, agency, instrumentality or municipality fails to pay any rent when due, the Authority will promptly notify the Secretary of the Treasury.

As provided in the Enabling Act, the good faith and credit of the Commonwealth are pledged for the payment of the rent under any lease agreement with the Authority executed by any of the Commonwealth's executive departments (including, among others, the Department of Education, the Department of Health and the Department of Corrections) and any other governmental body created by the Legislature and depending mainly on legislative appropriations to meet its operating expenses.

The Enabling Act also provides that if any rent payable to the Authority by any agency or instrumentality (other than a department) under a lease contract is not paid when due, then the Commonwealth shall advance the unpaid balance to the Authority. The Commonwealth pledges its good faith and credit to the making of such advances. Any advances so made are required to be reimbursed by the particular agency or instrumentality involved. Payments or advances of rentals by the Commonwealth are subject to annual appropriations by the Legislature, which appropriations are required to be made. However, the obligation to make such appropriations is not legally enforceable, in view of the sovereign immunity of the Commonwealth. Unlike the obligation to make payments under the guaranty of the Government Facilities Bonds and the other outstanding bonds of the Authority, the obligation to pay or advance rentals does not constitute "public debt" within the meaning of Section 8 of Article VI of the Puerto Rico Constitution.

See "Lease Agreements" above for a discussion of the Legislature's insufficient appropriation of funds for the payment of rentals under the Lease Agreements.

#### **Additional Bonds**

Under and in accordance with the provisions and restrictions of the 1995 Bond Resolution, the Authority may issue additional Government Facilities Bonds from time to time to finance additional government facilities or complete the construction of existing government facilities or to refund any Government Facilities Bonds. See "Additional Bonds" under *Summary of Certain Provisions of the 1995 Bond Resolution*.



## BOND INSURANCE

### The MBIA Insurance Policy

The following information has been furnished by MBIA for use in this Official Statement. Reference is made to *Appendix III* for a specimen of the MBIA Insurance Policy.

MBIA does not accept any responsibility for the accuracy or completeness of this Official Statement or any information or disclosure contained herein, or omitted herefrom, other than with respect to the accuracy of the information regarding the MBIA Insurance Policy and MBIA set forth under the heading "The MBIA Insurance Policy." Additionally, MBIA makes no representation regarding the Bonds or the advisability of investing in the Bonds.

The MBIA Insurance Policy unconditionally and irrevocably guarantees the full and complete payment required to be made by or on behalf of the Authority to the Fiscal Agent or its successor of an amount equal to (i) the principal of (either at the stated maturity or by an advancement of maturity pursuant to a mandatory sinking fund payment) and interest on, the Series M-3 Bonds as such payments shall become due but shall not be so paid (except that in the event of any acceleration of the due date of such principal by reason of mandatory or optional redemption or acceleration resulting from default or otherwise, other than any advancement of maturity pursuant to a mandatory sinking fund payment, the payments guaranteed by the MBIA Insurance Policy shall be made in such amounts and at such times as such payments of principal would have been due had there not been any such acceleration, unless MBIA elects in its sole discretion, to pay in whole or in part any principal due by reason of such acceleration); and (ii) the reimbursement of any such payment which is subsequently recovered from any owner of the Series M-3 Bonds pursuant to a final judgment by a court of competent jurisdiction that such payment constitutes an avoidable preference to such owner within the meaning of any applicable bankruptcy law (a "Preference").

The MBIA Insurance Policy does not insure against loss of any prepayment premium which may at any time be payable with respect to any Series M-3 Bonds. The MBIA's Policy does not, under any circumstance, insure against loss relating to: (i) optional or mandatory redemptions (other than mandatory sinking fund redemptions); (ii) any payments to be made on an accelerated basis; (iii) payments of the purchase price of the Series M-3 Bonds upon tender by an owner thereof; or (iv) any Preference relating to (i) through (iii) above. The MBIA Insurance Policy also does not insure against nonpayment of principal of or interest on the Series M-3 Bonds resulting from the insolvency, negligence or any other act or omission of the Fiscal Agent or any other paying agent for the Series M-3 Bonds.

The Policy for the Series M-3 Bonds has been endorsed to provide for cancellation of the Policy upon delivery of a substitute bond insurance policy for such Bonds to the Fiscal Agent in accordance with the terms of the Bond Resolution. The Policy for the Series M-3 Bonds will, however, remain in effect with respect to claims for Preferences resulting from payments made under the Policy for such Bonds prior to the effective date of the cancellation of the Policy.

Upon receipt of telephonic or telegraphic notice, such notice subsequently confirmed in writing by registered or certified mail, or upon receipt of written notice by registered or certified mail, by MBIA from the Fiscal Agent or any owner of a MBIA Insured Bond the payment of an insured amount for which is then due, that such required payment has not been made, MBIA on the due date of such payment or within one business day after receipt of notice of such nonpayment, whichever is later, will make a deposit of funds, in an account with U.S. Bank Trust National Association, in New York, New York, or its successor, sufficient for the payment of any such insured amounts which are then due. Upon presentment and surrender of such Series M-3 Bonds or presentment of such other proof of ownership of the Series M-3 Bonds, together with any appropriate instruments of assignment to evidence the assignment of the insured amounts due on the Series M-3 Bonds as are paid by MBIA, and appropriate instruments to effect the appointment of MBIA as agent for such owners of the Series M-3 Bonds in any legal proceeding related to payment of insured amounts on the Series M-3 Bonds, such instruments being in a form satisfactory to U.S. Bank Trust National Association, U.S. Bank Trust National Association shall disburse to such owners or the Fiscal Agent payment of the insured amounts due on such Series M-3 Bonds, less any amount held by the Fiscal Agent for the payment of such insured amounts and legally available therefor.

### *MBIA Insurance Corporation*

MBIA is the principal operating subsidiary of MBIA Inc., a New York Stock Exchange listed company (the "Company"). The Company is not obligated to pay the debts of or claims against MBIA. MBIA is domiciled in the State of New York and licensed to do business in and subject to regulation under the laws of all 50 states, the District of Columbia, the Commonwealth, the Commonwealth of the Northern Mariana Islands, the Virgin Islands of the United States and the Territory of Guam. MBIA, either directly or through subsidiaries, is licensed to do business in the Republic of France, the United Kingdom and the Kingdom of Spain and is subject to regulation under the laws of those jurisdictions. In February 2007, the Company incorporated a new subsidiary, MBIA México, S.A. de C.V. ("MBIA Mexico"), and in September 2007 it became licensed to write financial guarantee insurance in Mexico.

The principal executive offices of MBIA are located at 113 King Street, Armonk, New York 10504 and the main telephone number at that address is (914) 273-4545.

### *Regulation*

As a financial guaranty insurance company licensed to do business in the State of New York, MBIA is subject to the New York Insurance Law which, among other things, prescribes minimum capital requirements and contingency reserves against liabilities for MBIA, limits the classes and concentrations of investments that are made by MBIA and requires the approval of policy rates and forms that are employed by MBIA. State law also regulates the amount of both the aggregate and individual risks that may be insured by MBIA, the payment of dividends by MBIA, changes in control with respect to MBIA and transactions among MBIA and its affiliates.

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

### *Financial Strength Ratings of MBIA*

Moody's Investors Service, Inc. rates the financial strength of MBIA "Aaa."

Standard & Poor's, a division of The McGraw-Hill Companies, Inc., rates the financial strength of MBIA "AAA."

Fitch Ratings rates the financial strength of MBIA "AAA."

Each rating of MBIA should be evaluated independently. The ratings reflect the respective rating agency's current assessment of the creditworthiness of MBIA and its ability to pay claims on its policies of insurance. Any further explanation as to the significance of the above ratings may be obtained only from the applicable rating agency.

The above ratings are not recommendations to buy, sell or hold the Bonds, and such ratings may be subject to revision or withdrawal at any time by the rating agencies. Any downward revision or withdrawal of any of the above ratings may have an adverse effect on the market prices of the Series M-3 Bonds. MBIA does not guaranty the market prices of the Bonds nor does it guaranty that the ratings on the Bonds will not be revised or withdrawn.

### *MBIA Financial Information*

As of December 31, 2006, MBIA had admitted assets of \$10.9 billion (audited), total liabilities of \$6.9 billion (audited), and total capital and surplus of \$4.0 billion (audited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities. As of September 30, 2007, MBIA had admitted assets of \$11 billion (unaudited), total liabilities of \$6.8 billion (unaudited), and total capital and surplus of \$4.2 billion (unaudited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities.

For further information concerning MBIA, see the consolidated financial statements of MBIA and its subsidiaries as of December 31, 2006 and December 31, 2005 and for each of the three years in the period ended December 31, 2006, prepared in accordance with generally accepted accounting principles, included in the Annual Report on Form 10-K of the Company for the year ended December 31, 2006 and the consolidated financial statements of MBIA and its subsidiaries as of September 30, 2007 and for the nine month periods ended September 30, 2007 and September 30, 2006 included in the Quarterly Report on Form 10-Q of the Company for the quarter ended September 30, 2007, which are hereby incorporated by reference into this Official Statement and shall be deemed to be a part hereof.

Copies of the statutory financial statements filed by MBIA with the State of New York Insurance Department are available over the Internet at the Company's web site at <http://www.mbia.com> and at no cost, upon request to MBIA at its principal executive offices.

#### *Incorporation of Certain Documents by Reference*

The following documents filed by the Company with the Securities and Exchange Commission (the "SEC") are incorporated by reference into this Official Statement:

- (1) The Company's Annual Report on Form 10-K for the year ended December 31, 2006; and
- (2) The Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2007.

Any documents, including any financial statements of MBIA and its subsidiaries that are included therein or attached as exhibits thereto, filed by the Company pursuant to Sections 13(a), 13(c), 14 or 15(d) of the Exchange Act after the date of the Company's most recent Quarterly Report on Form 10-Q or Annual Report on Form 10-K, and prior to the termination of the offering of the Bonds offered hereby shall be deemed to be incorporated by reference in this Official Statement and to be a part hereof from the respective dates of filing such documents. Any statement contained in a document incorporated or deemed to be incorporated by reference herein, or contained in this Official Statement, 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 other subsequently filed document which also is or is deemed to be incorporated by reference herein 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 Company files annual, quarterly and special reports, information statements and other information with the SEC under File No. 1-9583. Copies of the Company's SEC filings (including (1) the Company's Annual Report on Form 10-K for the year ended December 31, 2006, and (2) the Company's Quarterly Reports on Form 10-Q for the quarters ended March 31, 2007, June 30, 2007 and September 30, 2007) are available (i) over the Internet at the SEC's web site at <http://www.sec.gov>; (ii) at the SEC's public reference room in Washington D.C.; (iii) over the Internet at the Company's web site at <http://www.mbia.com>; and (iv) at no cost, upon request to MBIA at its principal executive offices.

#### **The Ambac Insurance Policy**

The following information has been furnished by Ambac Assurance for use in this Official Statement. Reference is made to *Appendix IV* for a specimen of the Ambac Insurance Policy.

#### *Payment Pursuant to Financial Guaranty Insurance Policy*

Ambac Assurance Corporation ("Ambac Assurance") has made a commitment to issue a financial guaranty insurance policy (the "Financial Guaranty Insurance Policy") relating to a portion of the Bonds identified in the inside front cover of this Official Statement (the "Ambac Insured Bonds"), effective as of the date of issuance of such Bonds. Under the terms of the Financial Guaranty Insurance Policy, Ambac Assurance will pay to The Bank of New York, in New York, New York, or any successor thereto (the "Insurance Trustee"), that portion of the principal of and interest on the Ambac Insured Bonds that shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Obligor (as such terms are defined in the Financial Guaranty Insurance Policy). Ambac Assurance will make such

payments to the Insurance Trustee on the later of the date on which such principal and/or interest becomes due for Payment or within one business day following the date on which Ambac Assurance shall have received notice of Nonpayment from the Fiscal Agent. The insurance will extend for the term of the Ambac Insured Bonds and, once issued, cannot be canceled by Ambac Assurance.

The Financial Guaranty Insurance Policy will insure payment only on stated maturity dates and on mandatory sinking fund installment dates, in the case of principal, and on stated dates for payment, in the case of interest. If the Ambac Insured Bonds become subject to mandatory redemption and insufficient funds are available for redemption of all outstanding Ambac Insured Bonds, Ambac Assurance will remain obligated to pay the principal of and interest on outstanding Ambac Insured Bonds on the originally scheduled interest and principal payment dates, including mandatory sinking fund redemption dates. In the event of any acceleration of the principal of the Ambac Insured Bonds, the insured payments will be made at such times and in such amounts as would have been made had there not been an acceleration, except to the extent that Ambac Assurance elects, in its sole discretion, to pay all or a portion of the accelerated principal and interest accrued thereon to the date of acceleration (to the extent unpaid by the Obligor). Upon payment of all such accelerated principal and interest accrued to the acceleration date, Ambac Assurance's obligations under the Financial Guaranty Insurance Policy shall be fully discharged.

In the event the Fiscal Agent has notice that any payment of principal of or interest on an Ambac Insured Bond that has become Due for Payment and that is made to a holder by or on behalf of the Obligor has been deemed a preferential transfer and theretofore recovered from its registered owner pursuant to the United States Bankruptcy Code in accordance with a final, non-appealable order of a court of competent jurisdiction, such registered owner will be entitled to payment from Ambac Assurance to the extent of such recovery if sufficient funds are not otherwise available.

The Financial Guaranty Insurance Policy does **not** insure any risk other than Nonpayment (as set forth in the Financial Guaranty Insurance Policy). Specifically, the Financial Guaranty Insurance Policy does **not** cover:

1. payment on acceleration, as a result of a call for redemption (other than mandatory sinking fund redemption) or as a result of any other advancement of maturity;
2. payment of any redemption, prepayment or acceleration premium; and
3. nonpayment of principal or interest caused by the insolvency or negligence of the Trustee, Paying Agent or Bond Registrar, if any.

If it becomes necessary to call upon the Financial Guaranty Insurance Policy, payment of principal requires surrender of the Ambac Insured Bonds to the Insurance Trustee together with an appropriate instrument of assignment so as to permit ownership of such Ambac Insured Bonds to be registered in the name of Ambac Assurance to the extent of the payment under the Financial Guaranty Insurance Policy. Payment of interest pursuant to the Financial Guaranty Insurance Policy requires proof of holder entitlement to interest payments and an appropriate assignment of the holder's right to payment to Ambac Assurance.

Upon payment of the insurance benefits, Ambac Assurance will become the owner of the Ambac Insured Bonds, appurtenant coupon, if any, or right to payment of the principal of or interest on such Ambac Insured Bonds and will be fully subrogated to the surrendering holder's rights to payment.

The Financial Guaranty Insurance Policy does not insure against loss relating to payments of the purchase price of the Ambac Insured Bonds upon tender by a registered owner thereof or any preferential transfer relating to payments of the purchase price of the Ambac Insured Bonds upon tender by a registered owner thereof.

#### *Ambac Assurance Corporation*

Ambac Assurance is a Wisconsin-domiciled stock insurance corporation regulated by the Office of the Commissioner of Insurance of the State of Wisconsin, and is licensed to do business in 50 states, the District of Columbia, the Territory of Guam, the Commonwealth of Puerto Rico and the U.S. Virgin Islands, with admitted assets of approximately \$10,608,000,000 (unaudited) and statutory capital of approximately \$6,893,000,000 (unaudited) as of September 30, 2007. Statutory capital consists of Ambac Assurance's policyholders' surplus and statutory contingency

reserve. Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc., Moody's Investors Service, Inc. and Fitch Ratings have each assigned a triple-A financial strength rating to Ambac Assurance.

Ambac Assurance has obtained a ruling from the Internal Revenue Service to the effect that the insuring of an obligation by Ambac Assurance will not affect the treatment for federal income tax purposes of interest on such obligation and that insurance proceeds representing maturing interest paid by Ambac Assurance under policy provisions substantially identical to those contained in the Financial Guaranty Insurance Policy shall be treated for federal income tax purposes in the same manner as if such payments were made by the Obligor.

Ambac Assurance makes no representation regarding the Ambac Insured Bonds or the advisability of investing in the Ambac Insured Bonds and makes no representation regarding, nor has it participated in the preparation of, this Official Statement other than the information supplied by Ambac Assurance and presented under the heading "*Bond Insurance*" above.

#### *Available Information*

The parent company of Ambac Assurance, Ambac Financial Group, Inc. (the "Company"), is subject to the informational requirements of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), and in accordance therewith files reports, proxy statements and other information with the Securities and Exchange Commission (the "SEC"). These reports, proxy statements and other information can be read and copied at the SEC's public reference room at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Please call the SEC at 1-800-SEC-0330 for further information on the public reference room. The SEC maintains an internet site at <http://www.sec.gov> that contains reports, proxy and information statements and other information regarding companies that file electronically with the SEC, including the Company. These reports, proxy statements and other information can also be read at the offices of the New York Stock Exchange, Inc., 20 Broad Street, New York, New York 10005.

Copies of Ambac Assurance's financial statements prepared in accordance with statutory accounting standards are available from Ambac Assurance. The address of Ambac Assurance's administrative offices is One State Street Plaza, 19th Floor, New York, New York 10004, and its telephone number is (212) 668-0340.

#### *Incorporation of Certain Documents by Reference*

The following documents filed by the Company with the SEC (File No. 1-10777) are incorporated by reference in this Official Statement:

1. The Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2006 and filed on March 1, 2007;
2. The Company's Current Report on Form 8-K dated and filed on April 25, 2007;
3. The Company's Quarterly Report on Form 10-Q for the fiscal quarterly period ended March 31, 2007 and filed on May 10, 2007;
4. The Company's Current Report on Form 8-K dated and filed on July 25, 2007;
5. The Company's Current Report on Form 8-K dated and filed on August 3, 2007;
6. The Company's Quarterly Report on Form 10-Q for the fiscal quarterly period ended June 30, 2007 and filed on August 9, 2007;
7. The Company's Current Report on Form 8-K dated October 10, 2007 and filed on October 11, 2007;
8. The Company's Current Report on Form 8-K dated and filed on October 24, 2007; and
9. The Company's Quarterly Report on Form 10-Q for the fiscal quarterly period ended September 30, 2007 and filed on November 9, 2007.

All documents subsequently filed by the Company pursuant to the requirements of the Exchange Act after the date of this Official Statement will be available for inspection in the same manner as described above in "Available Information."

### **Concerning the Insurance Policies of MBIA and Ambac Assurance**

Each of MBIA and Ambac Assurance shall be deemed the owner of the bonds each has insured in lieu of the Beneficial Owners, as long as MBIA and Ambac Assurance shall not then be in default of their obligations under their respective insurance policy, for the purpose of giving of consents to the adoption of any resolution supplemental to the Bond Resolution.

## **PROVISIONS RELATING TO PUBLIC DEBT OF THE COMMONWEALTH**

### **Payment of Public Debt**

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, according to opinions heretofore rendered by the Secretary of Justice of Puerto Rico, also any payments required to be made by the Commonwealth under its guarantees of bonds and notes issued by its public instrumentalities. Any such guaranty payments, including guaranty payments under the Guaranty Act, are equal in their claim on such Commonwealth revenues to claims for the payment of debt service on general obligation bonds and notes of the Commonwealth.

The Commonwealth has allocated certain motor vehicle fuel taxes, crude oil, and derivative products excise taxes and license fees to 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 had to apply such amounts to the payment of its public debt.

Since fiscal year 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 had to apply such amounts to the payment of its public debt.

In 2006, the Commonwealth allocated a portion of the Sales Tax to service the bonds issued by the Sales Tax Financing Corporation to refinance a portion of the Commonwealth's outstanding extra constitutional debt (including the Sales Tax Bonds). The legislation making such allocation provides that the portion so set aside is not "available Commonwealth resources" for purposes of the above Constitutional provision. The Puerto Rico Supreme Court has not addressed the validity of such "set aside" vis-à-vis the Constitutional provision referred to above, and the Commonwealth cannot give any assurance that the Puerto Rico Supreme Court if faced with this issue in a properly briefed and litigated proceeding would agree that such segregated sales tax revenues are "unavailable."

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 resources, including surplus, to the payment of principal of and interest on public debt when due.

### **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 of 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, sales and use taxes and excise taxes. Certain revenues, such as federal excise taxes on offshore shipments of alcoholic beverages and tobacco products and customs duties, which are collected by the United States Government and returned to the Treasury 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 some of these revenues may be available for the payment of debt service. In addition, the portion of the Sales Tax allocated to the Sales Tax Financing Corporation is also not included as internal revenues consistent with the legislation creating the Sales Tax Financing Corporation, which legislation provides that such portion is not "available resources" under the Constitutional provisions relating to the Bonds.

All or a portion of the proceeds of certain refunding bonds issued by the Commonwealth were invested in guaranteed investment contracts or federal agency securities (in each case rated in the highest rating category by Moody's and S&P), none of which is eligible to be used for legal defeasance under Puerto Rico law ("non-eligible investments"). Since bonds refunded with proceeds invested in non-eligible investments are not legally defeased, such bonds are treated as outstanding for purposes of the 15% debt limitation.

Joint Resolution No. 2104 of September 30, 2004 ("Joint Resolution No. 2104"), authorized the Commonwealth to enter into interest rate exchange agreements with respect to the Commonwealth's \$447,875,000 Public Improvement Refunding Bonds, Series 2004 B (the "Series 2004 B Bonds"), which were issued as variable rate bonds. Joint Resolution No. 2104 allows the Commonwealth to calculate the constitutional debt limitation using (i) the fixed rate it is required to pay under any interest rate exchange agreement entered into by the Commonwealth in connection with the Series 2004 B Bonds, and (ii) the lesser of (A) the maximum interest rate allowed by law, and (B) the maximum interest rate set forth in the resolution approving the bonds, if any, in connection with the Commonwealth's \$279,240,000 Public Improvement Refunding Bonds, Series 2004 A (the "Series 2004 A Bonds") and any Series 2004 B Bonds for which no interest rate exchange agreement is executed. In November 2004, the Commonwealth entered into two interest rate exchange agreements with respect to the Series 2004 B Bonds.

Act No. 39 of 2005 authorizes the Commonwealth and the Authority to enter into interest rate exchange agreements with respect to its general obligation bonds, subject to certain conditions, including that the agreements are entered into to reduce certain financial risks associated with issuing variable rate obligations. In August 2006, the Commonwealth issued its \$500,000,000 Public Improvement Bonds of 2006, Series A, a portion of which bonds bear interest at a rate that will change periodically based on changes in the United States consumer price index, and in connection with such consumer price index floating rate bonds (said portion, the "2006 CPI Bonds") entered into an interest rate exchange agreement, the effect of which on said bonds will economically enable the Commonwealth to pay a fixed rate of interest in respect thereof. Act No. 39 of 2005 allows the Commonwealth to calculate the constitutional debt limit in a manner identical to that utilized in Joint Resolution No. 2104. In addition, the Commonwealth has also executed under the authority granted in Act No. 39 of 2005, interest rate exchange agreements in which the Commonwealth is making payments (1) on \$1,698,370,000 notional amount of public improvement bonds based on a short-term interest rate index published by Securities Industry and Financial Markets Association ("SIFMA") and is receiving from its counterparties payments on the same notional amount based on the published three-month London Interbank Offered Rate index (the "basis swap") and (2) on \$850,000,000 notional amount of public improvement bonds based on the published short-term SIFMA municipal swap rate and is receiving from its counterparties payments on the same notional amount based on a published index of municipal bonds having a maturity of ten (10) years (the "constant maturity swap"). In connection with the issuance of the portion of the Public Improvement Refunding Bonds, Series 2007A bearing interest at floating interest rates (said

portion, the "2007 A variable rate bonds"), the Commonwealth has entered into certain interest rate exchange agreements, the effect of which will economically enable the Commonwealth to pay fixed rates of interest in respect of the 2007 A variable rate bonds.

Future maximum annual debt service for the Commonwealth's outstanding general obligation debt is \$859,632,840 in the fiscal year ending June 30, 2020 (based on the assumption that (i) the bonds refunded with non-eligible investment are treated as being outstanding, (ii) the Series 2004 A Bonds bear interest at their actual rate per annum through July 1, 2012 and thereafter at 12% per annum, and (iii) the Series 2004 B Bonds, the 2006 CPI Bonds and the 2007 A variable rate bonds bear interest at 12% per annum. The sum of those amounts, \$859,632,840, is equal to 10.3% of \$8,344,210,500, which is the average of the adjusted internal revenues for the fiscal year ended June 30, 2006 and the currently estimated adjusted internal revenues for the fiscal year ended June 30, 2007. If the bonds refunded with non-eligible investments were treated as not being outstanding, and the interest on the Series 2004 B Bonds, the 2006 CPI Bonds and the 2007 A variable rate bonds is calculated using the fixed rate paid by the Commonwealth under the interest rate exchange agreements executed in connection with such bonds, the percentage referred to in the preceding sentence would be 8.63%.

Debt service for the Puerto Rico Aqueduct and Sewer Authority ("PRASA") guaranteed bonds of approximately \$30 million was paid by PRASA during each of the last two fiscal years, and thus, is not included in the calculation of the 15% debt limitation. See "Other Public Corporations – Aqueduct and Sewer Authority" under Public Corporations in the Commonwealth Report. In the event PRASA is unable to make any portion of the future debt service payments on its guaranteed bonds, the Commonwealth would be required to make such payments under its guarantee from the General Fund, and such debt service would, to the extent paid by the Commonwealth, be included in the calculation of the 15% debt limitation.

## **THE AUTHORITY**

### **General**

The Authority, a body corporate and politic constituting an instrumentality of the Commonwealth exercising public and essential governmental functions, was created on June 19, 1958 by the Enabling Act.

Under the Enabling Act, the primary duties of the Authority are to design and construct office buildings, quarters, courts, warehouses, shops, schools, health facilities, social welfare facilities and related facilities for lease to the Commonwealth or any of its departments, agencies, instrumentalities or municipalities.

The executive offices of the Authority are located at Roberto Sánchez Vilella Government Center, North Building, 6<sup>th</sup> Floor, De Diego Avenue, San Juan, Puerto Rico 00940, telephone number (787) 722-0101.

### **Powers**

The Authority has broad powers under the Enabling Act, including among others: to make contracts and to execute all instruments necessary or convenient for the exercise of any of its powers; to acquire any kind of properties and rights therein in any lawful manner, including, without limitation, acquisition by purchase, either by agreement or through the exercise of the power of eminent domain, lease or bequest, and to possess, lease, use and operate any properties or facilities; to prepare plans, projects and cost estimates for the construction, improvement or repair of any property or facility; to contract with any Commonwealth department, agency or official, or with any private person or entity with regard to the administration of any properties or facilities of the Authority; to sell, transfer, lease, sublease, cede, mortgage, pledge, grant concessions, or guarantee contracts or in any other way dispose or transfer any properties or facilities; to borrow money and issue bonds of the Authority for any of its corporate purposes, and to secure payment of its bonds by pledge of all or any of its properties, revenues and income; to create subsidiaries, affiliate or associates, in or outside the Commonwealth, to acquire stock, enter into participation agreements and purchase bonds of other corporations and entities; to enter into interest rate swap agreements and any similar financial instruments; and to do all acts necessary or convenient to carry out the powers granted to it.



## Management

The Enabling Act provides that the Authority shall be governed by a Governing Board (the "Board") composed of seven (7) members. The Secretary of Education, the Secretary of Transportation and Public Works and the President of Government Development Bank serve *ex officio* as members of the Board, and the other four (4) members are appointed for 6-year terms by the Governor of Puerto Rico with the advice and consent of the Senate.

The current members of the Board and their occupations and expiration of their terms are:

José M. Izquierdo Encarnación.....	Engineer	June 2010
Roberto Montalvo Carbia.....	Attorney	July 2010
Rafael Aragunde Torres.....	Secretary of Education	Ex-officio
Carlos González Miranda.....	Secretary of Transportation and Public Works	Ex-officio
Antonio Vidal Santiago.....	Attorney	November 2008
Reynaldo Encarnación .....	Engineer	March 2012
Jorge Irizarry Herrans.....	President of Government Development Bank for Puerto Rico	Ex-officio

The current Executive Director of the Authority is Leila Hernández Umpierre. Ms. Hernández Umpierre is an attorney, who obtained her Juris Doctor from the Interamerican University of Puerto Rico. She also holds a Master's Degree in Urban Planning from the University of Puerto Rico. At the time of her appointment she was the Deputy Director of the Authority.

## PROGRAMS AND FACILITIES OF THE AUTHORITY

The Authority has an approximately \$601 million Five-Year Capital Improvement Program (the "CIP"), which reflects the Authority's construction priorities for fiscal year 2006 through fiscal year 2010. A portion of the Authority's \$601 million CIP is expected to be spent after fiscal year 2008 to complete projects begun in the fiscal year 2001 to fiscal year 2006 period. The CIP includes office buildings, school buildings, health facilities, correctional facilities, and other facilities, as described below. A portion of the facilities were financed with outstanding Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds, Series A, B, D, E, G, I and L and Puerto Rico Public Buildings Authority Government Facilities Revenue Refunding Bonds, Series C, F, H, J and K (collectively, the "Outstanding Government Facilities Bonds"). The remainder of the costs of the CIP will be paid for through interim financings, future bond issues and Commonwealth appropriations.

### Office Buildings Program

Under its office buildings program, the Authority has completed construction of 218 office buildings (including police stations, courthouses, and related parking facilities), amounting to approximately 8.8 million square feet of rentable space, for the use of and lease to various departments, agencies and instrumentalities of the Commonwealth. As of June 30, 2007, the estimated total cost of construction completed under the office buildings program was approximately \$515 million, which was provided principally by the Authority through the issuance of Public Buildings Authority Revenue Bonds under the 1970 Bond Resolution and Government Facilities Bonds under the 1995 Bond Resolution.

The Authority has under planning and construction one office center, 2 fire stations, 4 police facilities, and improvements to 20 office buildings (including police stations and courthouses), at an estimated total cost of \$80.8 million.

The currently outstanding Public Buildings Authority Revenue Bonds issued under the 1970 Bond Resolution and Government Facilities Bonds issued under the 1995 Bond Resolution are secured by a pledge of the rentals of public buildings and related facilities financed by such bonds. In addition, they are secured by a pledge of the Commonwealth to pay or advance rentals under the Enabling Act and the Commonwealth guaranty of bonds issued by the Authority under the Guaranty Act. The Authority reserves the right to issue additional Revenue Bonds

and Government Facilities Bonds to provide for the payment of any then outstanding notes issued in connection with or the cost of construction of any facilities included in the office buildings program.

### **School Buildings Program**

Under its school buildings program, the Authority has completed the construction of 356 school buildings, amounting to approximately 20.4 million square feet of rentable space, all of which has been leased to the Department of Education. As of June 30, 2007, the estimated total cost of construction completed under the school buildings program was \$2,009,910,550, which was provided principally by the Authority through the issuance of Public Buildings Authority Public Education and Health Facilities Bonds under the 1978 Bond Resolution and Government Facilities Bonds under the 1995 Bond Resolution.

The Authority has under planning and construction 25 new school buildings and improvements to 10 school buildings amounting to approximately 7.6 million square feet of rentable space to be leased to the Department of Education. The estimated total cost of construction of such school buildings and improvements is \$512 million.

The currently outstanding Public Buildings Authority Public Education and Health Facilities Bonds issued under the 1978 Bond Resolution and Government Facilities Bonds issued under the 1995 Bond Resolution are secured by a pledge of rentals of public education and health facilities financed by such bonds. In addition, they are secured by a pledge of the Commonwealth to pay rentals under the Enabling Act and the Commonwealth guaranty of bonds issued by the Authority under the Guaranty Act. The Authority reserves the right to issue additional Public Education and Health Facilities Bonds and Government Facilities Bonds to provide for the payment of any then outstanding notes issued in connection with or the cost of construction of any facilities included in the school buildings program.

### **Health Facilities Program**

Under its health facilities program, the Authority completed construction and owns 18 health facilities amounting to approximately 1.5 million square feet of rentable space, all of which has been leased to the Department of Health. As of June 30, 2007, the estimated total cost of construction completed and owned under the health facilities program was \$203 million, which was provided principally by the Authority through the issuance of Public Buildings Authority Public Education and Health Facilities Bonds under the 1978 Bond Resolution.

The currently outstanding Public Buildings Authority Public Education and Health Facilities Bonds issued under the 1978 Bond Resolution and Government Facilities Bonds issued under the 1995 Bond Resolution are secured by a pledge of rentals of public education and health facilities financed by such bonds. In addition, they are secured by a pledge of the Commonwealth to pay rentals under the Enabling Act and the Commonwealth guaranty of bonds issued by the Authority under the Guaranty Act. The Authority reserves the right to issue additional Public Education and Health Facilities Bonds and Government Facilities Bonds to provide for the payment of any then outstanding notes issued in connection with or the cost of construction of any facilities included in the health facilities program.

### **Correctional Facilities Program**

In 1994, the Department of Corrections, in cooperation with the Authority, began a program to provide for the construction, operation and maintenance of new Commonwealth correctional facilities to be leased to the Department of Corrections by the Authority. These facilities were constructed as part of the Commonwealth's effort to alleviate overcrowding in its correctional system and achieve compliance with certain federal court mandated minimum inmate living space requirements. Three facilities have been completed, with a total cost of constructing of approximately \$132 million. The Department of Corrections operates the facilities. An additional government-operated facility was completed with a construction cost of \$7 million.

The Authority has under construction improvements to one of the correctional facilities. The estimated total cost of construction of such improvements is approximately \$7.8 million.

**Other Facilities**

The Authority also constructs office buildings, schools and health facilities that are financed by a combination of Federal grants and Commonwealth appropriations. The Authority is also empowered to undertake construction on behalf of and as an agent for other public agencies of the Commonwealth.

The Authority currently has under planning and construction 2 correctional facilities and 2 fire stations, which have an estimated total cost of construction of approximately \$18 million, to be financed through Commonwealth appropriations.

Under the Enabling Act, the Authority is also empowered to construct social welfare facilities. Any such facilities that may be constructed can be financed by bonds of the Authority under the 1995 Bond Resolution. The Authority has not issued any bonds or other obligations to finance such facilities.

**DEBT OF THE AUTHORITY AND DEBT SERVICE REQUIREMENTS**

**Debt**

The following table sets forth the outstanding principal debt of the Authority:

	<u>As of November 30, 2007</u> <sup>1</sup>	<u>As Adjusted</u> <sup>2</sup>
Bonded Debt:		
Bonds outstanding under the 1970 Bond Resolution...	\$ 54,515,000	\$ 54,515,000
Bonds outstanding under the 1978 Bond Resolution...	97,655,000	97,655,000
Bonds outstanding under the 1995 Bond Resolution...	<u>2,602,405,310</u>	<u>2,946,603,182</u>
Total Bonded Debt.....	\$ 2,754,575,310	\$ 3,098,773,182

1 Calculated by excluding all interest accretion on outstanding capital appreciation bonds and convertible capital appreciation bonds from their respective dates of issuance.

2 Reflects the outstanding debt of the Authority after giving effect to the issuance of the Bonds (calculated by excluding all interest accretion on outstanding capital appreciation bonds and convertible capital appreciation bonds from their respective dates of issuance) and the refunding of the Refunded Bonds.

The Authority has caused to be deposited to the credit of the respective reserve accounts under the 1970 Bond Resolution and the 1978 Bond Resolution reserve account letters of credit issued by The Bank of Nova Scotia acting through its San Juan Branch ("BNS") (each, a "BNS Reserve Account Letter of Credit" and, collectively, the "BNS Reserve Account Letters of Credit") in the respective amounts required by said resolutions to be held to the credit of such reserve accounts. The scheduled expiration date of the BNS Reserve Account Letters of Credit is July 15, 2008. Among other things, the BNS Reserve Account Letters of Credit authorize drawings thereunder for the payment of any amount required to be paid out of moneys in the reserve account to which such BNS Reserve Account Letter of Credit relates after the withdrawal from the applicable reserve account of all cash and securities therein.

The obligations of the Authority under the reimbursement agreements between BNS and the Authority are not payable from the portion of the rentals received by the Authority in respect of the government facilities financed or refinanced with the proceeds of any Government Facilities Bonds and allocable to such Government Facilities Bonds.

No reserve account is established under the 1995 Bond Resolution.

## Debt Service Requirements

Debt service requirements of the Authority for the Outstanding Government Facilities Bonds (after the refunding of the Refunded Bonds and the interest due July 1, 2008 on certain other outstanding Government Facilities Bonds) and the Bonds as shown in the following table, consist in any fiscal year of the sum of the amounts required to pay (i) the interest that is payable on January 1 in such fiscal year and July 1 in the following fiscal year, (ii) the principal of serial bonds that is payable on July 1 in the following fiscal year, and (iii) the amortization requirements for term bonds for the following fiscal year.

Fiscal Year Ended June 30	Total Debt Service on Bonds Outstanding under 1970, 1978 and 1995 Bond Resolutions		The Bonds			Total Debt Service				
			Principal	Interest	Total					
2008	\$	154,350,517	\$	0	\$	24,595,720	\$	178,946,237		
2009		177,012,149		7,480,000		46,358,425		230,850,574		
2010		175,008,057		10,950,000		45,965,725		231,923,782		
2011		179,256,357		11,550,000		45,363,475		236,169,832		
2012		171,683,944		12,180,000		44,728,225		228,592,169		
2013		145,259,663		22,930,000		44,058,325		212,247,988		
2014		145,098,178		24,170,000		42,823,088		212,091,266		
2015		144,944,647		25,505,000		41,486,113		211,935,759		
2016		144,696,155		26,915,000		40,075,000		211,686,155		
2017		144,645,863		28,425,000		38,566,188		211,637,051		
2018		150,622,520		9,535,000		34,649,825		194,807,345		
2019		137,012,368		12,130,000		34,130,100		183,272,468		
2020		127,695,580		22,115,000		33,462,950		183,273,530		
2021		121,762,466		29,325,000		32,183,900		183,271,366		
2022		115,096,664		37,735,000		30,426,800		183,258,464		
2023		110,871,936		44,265,000		28,148,238		183,285,174		
2024		110,878,212		46,640,000		25,803,643		183,321,854		
2025		115,749,372		42,255,000		23,986,320		181,990,692		
2026		140,849,838		18,935,000		22,301,920		182,086,758		
2027		114,517,554		46,215,000		21,383,905		182,116,459		
2028		113,148,482		50,470,000		19,536,423		183,154,904		
2029		145,583,112		20,080,000		17,603,375		183,266,487		
2030		118,770,788		47,965,000		16,541,125		183,276,913		
2031		122,633,401		46,900,000		13,745,688		183,279,088		
2032		152,236,288		20,010,000		11,028,850		183,275,138		
2033		152,341,006		20,885,000		10,049,950		183,275,956		
2034		63,855,136		111,210,000		9,027,150		184,092,286		
2035		159,353,344		54,040,000		4,475,120		217,868,464		
2036		159,359,270		21,695,000		2,223,750		183,278,020		
2037				22,780,000		1,139,000		23,919,000		
Total	\$	4,014,292,866	\$	895,290,000	\$	805,868,312	\$	1,701,158,312	\$	5,715,451,179

## SUMMARY OF CERTAIN PROVISIONS OF THE 1995 BOND RESOLUTION

The following statements are brief summaries of certain provisions of the 1995 Bond Resolution. Such statements do not purport to be complete and reference is made to the 1995 Bond Resolution, copies of which are available for examination at the office of the Fiscal Agent. For the purposes of this summary, the terms "Bond" or "Bonds" shall refer to the Government Facilities Revenue Bond or Bonds.

### Revenues

The Authority covenants that each Lease Agreement which it enters into for any government facilities financed or refinanced under the 1995 Bond Resolution ("Authority Facilities") will require the Lessee thereunder to pay rentals which in the aggregate will be sufficient and timely to provide the sums needed from time to time to pay the interest on all Bonds issued by the Authority for the financing or refinancing of the Authority Facilities covered by such Lease Agreement, the principal of all such Bonds which are serial Bonds and the Amortization Requirements and redemption premium for any such Bonds which are term Bonds ("1995 Debt Service Rentals").

(Section 701). All 1995 Debt Service Rentals received from the leasing of Authority Facilities are pledged as hereinafter provided.

### **1995 Sinking Fund**

A special fund is created by the 1995 Bond Resolution and designated "Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds Sinking Fund" (the "1995 Sinking Fund"). Two separate accounts are created in the 1995 Sinking Fund, namely, the "1995 Bond Service Account" and the "1995 Redemption Account." (Section 502).

The Authority covenants that all 1995 Debt Service Rentals will be collected by the Authority and immediately deposited with the Fiscal Agent to the credit of the following accounts in the following order:

(1) To the 1995 Bond Service Account, such amount thereof as may be required to make the amount then to the credit of the 1995 Bond Service Account equal to the amount of interest then due and payable and the interest which will accrue up to the next interest payment date on all Bonds of each series then outstanding and the principal of all serial Bonds, if any, which will become due and payable within the next ensuing twelve (12) months;

(2) To the 1995 Redemption Account, such amount of the balance remaining after making the deposit under paragraph (1) above as may be required to make the amounts so deposited in the then current fiscal year equal to the Amortization Requirement, if any, for such fiscal year for the term Bonds of each series then outstanding, plus the premium, if any, which would be payable on a like principal amount of Bonds if such principal amount of Bonds should be redeemed on the next redemption date from moneys in the 1995 Sinking Fund; and

(3) The balance, if any, shall be deposited to the credit of the 1995 Bond Service Account. (Section 502).

The requirements specified in paragraphs (1) and (2) above shall be cumulative (Section 502).

### **1995 Redemption Account**

Moneys in the 1995 Redemption Account shall be applied to the retirement of Bonds as follows:

(a) Subject to the provisions of paragraph (c) below, the Fiscal Agent shall endeavor to purchase outstanding Bonds, whether or not such Bonds shall then be subject to redemption, at the most advantageous price obtainable with reasonable diligence, having regard to interest rate and price, such price not to exceed the principal of such Bonds plus the amount of the premium, if any, which would be payable on the next redemption date to the holders of such Bonds if such Bonds should be called for redemption on such date from moneys in the 1995 Sinking Fund. The Fiscal Agent shall pay the interest accrued on such Bonds to the date of delivery thereof from the 1995 Bond Service Account and the purchase price from the 1995 Redemption Account, but no such purchase shall be contracted for within forty-five (45) days next preceding any interest payment date on which such Bonds are subject to call for redemption.

(b) Subject to the provisions of paragraph (c) below, the Fiscal Agent shall call for redemption on each date on which Bonds are subject to redemption from moneys which are in the 1995 Sinking Fund on the 45<sup>th</sup> day prior to such redemption date such amount of Bonds then subject to redemption as, with the redemption premium, if any, will exhaust the 1995 Redemption Account as nearly as may be; provided, however, that not less than \$50,000 principal amount of Bonds shall be called for redemption at any one time. Not less than thirty (30) days before the redemption date the Fiscal Agent shall withdraw from the 1995 Bond Service Account and from the 1995 Redemption Account and set aside in separate accounts the respective amounts required for paying the interest on, and the principal of and redemption premium on, the Bonds so called for redemption.

(c) Moneys in the 1995 Redemption Account shall be applied by the Fiscal Agent in each fiscal year to the purchase or redemption of Bonds of each series then outstanding in the following order:

*first*, term Bonds of each series to the extent of the Amortization Requirement, if any, for such fiscal year for such term Bonds of each such series then outstanding plus the applicable premium, if any, and if the amount available in such fiscal year shall not be equal thereto, then, in proportion to the Amortization Requirement, if any, for such fiscal year for the term bonds of each series then outstanding, plus the applicable premium, if any;

*second*, any balance then remaining shall be applied to the purchase of any Bonds whether or not such Bonds shall be subject to redemption in accordance with paragraph (a) above;

*third*, any balance then remaining shall be applied to the redemption of term Bonds of each series in proportion to the Amortization Requirement, if any, for such fiscal year for the term Bonds of each such series then outstanding plus the applicable premium, if any; and

*fourth*, after the retirement of all term Bonds, any balance still remaining shall be applied to the retirement of the serial Bonds of each series in proportion to the aggregate principal amount of the serial Bonds of such series originally issued under the provisions of the 1995 Bond Resolution. (Section 504).

The term "Principal and Interest Requirements" for any fiscal year, as applied to the Bonds of any series under the 1995 Bond Resolution, shall mean the sum of:

(a) the amount required to pay the interest on all outstanding Bonds of such series which is payable after July 31 of such fiscal year and on or before July 31 in the following fiscal year;

(b) the amount required to pay the principal of all outstanding serial Bonds of such series which is payable after July 31 of such fiscal year and on or before July 31 in the following fiscal year; and

(c) the Amortization Requirement for the term Bonds of such Series for such fiscal year. The following rules shall apply in determining the amount of the Principal and Interest Requirements for any period:

(i) in the case of Capital Appreciation Bonds, the Accreted Value becoming due at maturity or by virtue of an Amortization Requirement shall be included when due and payable as part of the principal or Amortization Requirements in accordance with the above provisions;

(ii) in the case of Capital Appreciation and Income Bonds, the Appreciated Value becoming due at maturity or by virtue of an Amortization Requirement shall be included when due and payable as part of principal or Amortization Requirements in accordance with the above provisions;

(iii) the interest rate on Bonds issued with a variable, adjustable, convertible or similar rate of interest shall be the average rate of interest per annum on such Bonds for the preceding twelve months or such shorter period that such Bonds shall have been outstanding, or if such Bonds had not been outstanding prior to the date of calculation, the rate of interest on such Bonds on the date of calculation;

(iv) in the case of Bonds which by their terms may be tendered by and at the option of the holder thereof for payment prior to maturity, the tender date or dates shall be ignored if the tender price for such Bonds is payable from a letter of credit or insurance policy or similar credit or liquidity facility and the stated dates for Amortization Requirements and principal payments shall be used; provided, however, that if on the date of calculation the issuer of the letter of credit or insurance policy or similar credit or liquidity facility has advanced funds thereunder and such amount has not been repaid, Principal and Interest Requirements shall include the repayment obligations thereof in accordance with the principal repayment

schedule and interest rate or rates specified in (or specified in the agreement authorizing the issuance of) the letter of credit or insurance policy or similar credit or liquidity facility;

(v) in the case of Bonds the maturity of which may be extended by and at the option of the holder thereof or the Authority, the Bonds shall be deemed to mature on the later of the stated maturity date and the date to which such stated maturity date has been extended; and

(vi) in the case of Bonds (A) which are expected to be repaid from the proceeds of Bonds or other indebtedness or (B) on which interest is payable periodically and for which 25% or more of the principal amount matures during any one year and for which no Amortization Requirements have been established, the debt service requirements on the Bonds may be excluded and in lieu thereof the Bonds shall be treated, for purposes of the computation of Principal and Interest Requirements, as debt securities having a comparable federal tax status to that of such Bonds, maturing in substantially equal annual payments of principal and interest over a period of not more than thirty years from the date of issuance thereof, bearing interest at a fixed rate per annum equal to the average interest rate per annum for such debt securities on the date of issuance of the Bonds and issued by issuers having a credit rating, issued by Moody's Investors Service, Inc. or any successors thereto or Standard & Poor's Ratings Services or any successors thereto, comparable to that of the Authority, as shown by a certificate of an underwriting or investment banking firm experienced in marketing such securities. (Section 101).

Notwithstanding the foregoing, if the Authority has notified the Fiscal Agent that an interest rate swap agreement is in effect in respect of any Bonds, then for all purposes of the above paragraphs, except for the purpose of determining the required deposits to the 1995 Sinking Fund pursuant to Section 502 of the 1995 Bond Resolution, the interest rate on such Bonds shall be the interest rate calculated with reference to such interest rate swap agreement; and if such rate calculated with reference to such interest rate swap agreement is a variable rate, the interest rate on such Bonds (except for the purpose specified above in this Sentence) shall be the average interest rate calculated with reference to such interest rate swap agreement for the preceding twelve months or such shorter period that the interest rate swap agreement has been in effect, or if such interest rate swap agreement had not been in effect prior to the date of calculation, the interest rate calculated with reference to such interest rate swap agreement on the date of calculation. (Section 101).

### **1995 Construction Fund**

The balance of proceeds of Bonds issued under Section 208 of the 1995 Bond Resolution available for payment of construction costs is required to be deposited to the credit of the Construction Fund under the 1995 Bond Resolution (the "1995 Construction Fund") and applied to the payment of the cost of the Initial Facilities, Additional Facilities, Improvements and uncompleted Facilities for which such Bonds were issued. (Section 208).

Payments from the 1995 Construction Fund shall be disbursed by check signed by the Treasurer of the Authority or by any officer or employee of the Authority designated by resolution of the Authority. (Section 402). Any balance remaining in the 1995 Construction Fund from time to time after the completion of the Authority Facilities and Improvements theretofore financed by the Authority may, at the option of the Authority, be deposited to the credit of the 1995 Redemption Account or the 1995 Bond Service Account. (Section 404).

### **Additional Bonds**

Additional Bonds may be issued from time to time to provide funds to pay all or any part of any remaining costs of the Initial Facilities or to pay all or any part of the cost of any Additional Facilities or Improvements to Authority Facilities financed under the 1995 Bond Resolution or of any uncompleted part of the Initial Facilities or Additional Facilities or Improvements, and to pay any notes or other obligations of the Authority theretofore issued, or to repay any advances made from any source, to finance such costs; provided that no such Bonds shall be issued unless under the then existing law such Bonds may be specified by the Authority to be covered by the guaranty of the Commonwealth of Puerto Rico under the Guaranty Act and the Authority so specifies such Bonds by resolution. Before any such Additional Bonds may be issued there must be filed with the Fiscal Agent, among other things, a certificate signed by the Executive Director of the Authority stating that on the basis of all Lease Agreements or amendments or supplements thereto, as executed and delivered or as expected to be executed and delivered, the

1995 Debt Service Rentals, as calculated by the Authority, will be sufficient and timely to pay the principal of, and the redemption premium if any, and interest on, such Bonds and all Bonds then outstanding. (Section 208).

Refunding bonds, including crossover refunding bonds, may be issued by the Authority at any time or times for the purpose of providing funds for refunding at or prior to their maturity or maturities all or any part of (i) the outstanding Bonds of any series, or (ii) the outstanding debt of the Authority incurred to finance Authority Facilities as defined in the 1970 Bond Resolution or in the 1978 Bond Resolution, in either case including the payment of any redemption premium thereon and interest which will accrue on such Bonds to the redemption date or maturity date or dates occurring prior thereto; provided that no such refunding bonds shall be issued unless under the then existing law such bonds may be specified by the Authority to be covered (as of the crossover date with respect to crossover refunding bonds) by the guaranty of the Commonwealth under the Guaranty Act and the Authority so specifies such refunding bonds by resolution. (Section 209).

### **Investment of Funds**

The 1995 Bond Resolution provides for the following types of investments:

(a) Government Obligations which are (i) direct obligations of, or obligations the principal of and interest on which are unconditionally guaranteed by, the United States Government, (ii) obligations (including participation certificates) issued or guaranteed by an agency of the United States of America or person controlled or supervised by and acting as an instrumentality of the United States of America pursuant to authority granted by the Congress, including but not limited to those of the Federal Home Loan Mortgage Corporation, Federal Home Loan Banks, the Farm Credit System, Federal National Mortgage Association and the Student Loan Marketing Association, (iii) municipal obligations, the payment of the principal of, interest and redemption premium, if any, on which are irrevocably secured by obligations described in clause (i) or (ii) above or (iv) below and which obligations are not subject to redemption prior to the date on which the principal of the obligations are to be used and have been deposited in an escrow account which is irrevocably pledged to the payment of the principal of and interest and redemption premium, if any, on such municipal obligations and which municipal obligations are rated in the highest category (without regard to any gradation within such category) by both Moody's Investors Service or any successors thereto and Standard & Poor's Ratings Services or any successors thereto, and (iv) evidences of ownership of proportionate interests in future interest or principal payments on obligations specified in clauses (i), (ii) and (iii) above held by a national banking association or bank (including the Fiscal Agent) or trust company as custodian, under which the owner of said interests is the real party in interest and has the right to proceed directly and individually against the obligor on the underlying obligations described above, and which underlying obligations are not available to satisfy any claim of the custodian or any person claiming through the custodian or to whom the custodian may be obligated.

(b) Investment Obligations which are (i) Government Obligations, (ii) obligations of any state or territory of the United States of America which are rated, on the date of investment therein, in one of the three highest rating categories (without regard to any gradation within such categories) by both Moody's Investors Service or any successors thereto and Standard & Poor's Ratings Services or any successors thereto, (iii) bankers' acceptances, certificates of deposit or time deposits of any bank or national banking association (including the Fiscal Agent), any trust company or any savings and loan association (including any investment in pools of such bankers' acceptances, certificates of deposit or time deposits), which to the extent that such obligations are not insured by the Federal Deposit Insurance Corporation, are either (A) issued by a bank, national banking association, trust company or savings and loan association having a combined capital and surplus aggregating at least \$50,000,000 or (B) collateralized at all times by such securities as are described in clause (i) or (ii) above, having a market value at least equal to the principal amount of such bankers' acceptances, certificates of deposit or time deposits (or portion thereof not so insured); provided that the Fiscal Agent has a perfected first security interest in the collateral and that such collateral is held free and clear of claims by third parties, (iv) any repurchase, reverse repurchase or investment agreement with any bank or trust company organized under the laws of any state of the United States or the Commonwealth of Puerto Rico or any national banking association (including the Fiscal Agent), insurance company, or government bond dealer reporting to, trading with, and recognized as a primary dealer by the Federal Reserve Bank of New York and a member of the Security Investors



Protection Corporation, which agreement is secured by any one or more of the securities described in clause (i) or (ii) above, in which securities the Fiscal Agent has a perfected first security interest and such securities are held free and clear of claims by third parties, or if not so secured, meets the rating requirements set forth in clause (vii) below, (v) participating shares in a mutual fund or investment pool for local government investment; provided that the investments of such mutual fund or investment pool are rated in one of the three highest rating categories (without regard to any gradations within such categories) by both Moody's Investors Service or any successors thereto, and Standard & Poor's Ratings Services or any successors thereto, (vi) (1) shares of stock in a corporation rated in the highest rating category by Moody's Investors Service or any successors thereto and Standard & Poor's Ratings Services or any successors thereto (without regard to gradations within such category) and (a) is a regulated investment company within the meaning of Section 851(a) of the Internal Revenue Code of 1986, as amended, and meets the requirements of Section 852(a) of said Code for the calendar year; (b) invests all of its assets in Government Obligations or in Investment Obligations described in clause (ii) above; and (c) has at least 98% of (I) its gross income derived from interest on, or gain from the sale of or other disposition of, such obligations or (II) the weighted average of its assets is represented by investments in such obligations or (2) money market accounts of the Fiscal Agent or any state or federally chartered bank, banking association, trust company or subsidiary trust company that is rated or whose parent state bank is rated in the highest short-term rating category or in one of the two highest long-term rating categories by Moody's Investors Service or any successors thereto and Standard & Poor's Ratings Services or any successors thereto (without regard to gradations within such category), and (vii) any other investment obligations which are rated, which are issued by issuers which are rated, or which are backed by letters of credit or lines of credit the provider of which is rated, on the date of investment therein, in one of the three highest rating categories (without regard to any gradation within such categories) by both Moody's Investors Service or any successors thereto and Standard & Poor's Ratings Services or any successors thereto or which are collateralized by such Investment Obligations. (Section 101).

Moneys held in the 1995 Construction Fund, the 1995 Bond Service Account and the 1995 Redemption Account shall, as nearly as practicable, be invested and reinvested in Investment Obligations, which mature, or are subject to redemption by the holder thereof at the option of such holder not later than the dates when the moneys held for the credit thereof will be required for the purposes intended. (Section 602).

### **General Covenants**

The Authority covenants that it will not agree to any amendment, modification or termination of any Lease Agreements of any Authority Facilities (or exercise any right it may have to rescind the lease of any lessee of space in any Authority Facilities) which would reduce the amounts of rental payments below the amounts required by Section 701 of the 1995 Bond Resolution or postpone the times of making such rental payments or which would otherwise materially and adversely affect the security of the bondholders (Section 702), that it will not create or suffer to be created any lien or charge upon the Authority Facilities or any part thereof or upon the 1995 Debt Service Rentals therefrom, other than the liens and charges created or permitted under the 1995 Bond Resolution (Section 705), and that each Lease Agreement will provide that the obligation of the Lessee to pay timely the required rentals thereunder shall be absolute and unconditional. (Section 709).

The Authority covenants that it will not dispose of or encumber any Authority Facilities, unless (a) the Authority determines that notwithstanding such disposition or encumbrance, total rentals under each Lease Agreement will be sufficient to provide the sums required under Section 701 of the 1995 Bond Resolution, and (b) the Authority will receive as the price for any such disposition (but not an encumbrance), together with any other available moneys, the total amount of the 1995 Debt Service Rentals which would otherwise have been payable by the lessees of such Authority Facilities during the remaining term of the related Lease Agreements plus such additional amounts as will be necessary to pay the fees and expenses of the Fiscal Agent and all other expenses in connection with the application of the proceeds of such sale to the payment of the principal of and interest on outstanding Bonds issued by the Authority under the 1995 Bond Resolution including any redemption premiums. The proceeds of any such disposition (other than an encumbrance) shall be promptly deposited in the 1995 Redemption Account. (Section 708).

The Authority may also from time to time dispose of or encumber any fixtures or movable property in connection with the Authority Facilities or any materials used in connection therewith, if the Authority determines that such articles are no longer needed or useful in connection with the construction or operation or maintenance of the Authority Facilities and the proceeds thereof (other than an encumbrance) shall be applied to the replacement of the property so disposed of or at the option of the Authority shall be deposited to the credit of the 1995 Redemption Account. (Section 708).

Each Lease Agreement is required to provide that it may not be assigned or otherwise transferred in whole or in part by either party (unless the conditions set forth under the 1995 Bond Resolution for a termination of such Lease Agreement have been met), and will provide that all or any part of the Authority Facilities covered by such Lease Agreement may be subleased as a whole or in part by the lessee if, among other things the following conditions have been met: (a) the sublessee under the sublease shall be a department, agency or instrumentality of the Commonwealth unless the Authority shall have obtained an opinion of nationally recognized bond counsel that such sublease will not cause interest on any Bonds to be includable in gross income of the owners thereof for federal income tax purposes (other than Bonds for which such interest is intended not to be excludable in gross income for such purposes); (b) such lessee shall acknowledge in writing that it shall continue to remain liable for the payment of all rentals under such Lease Agreement; and (c) there shall have been delivered to the Authority and such lessee (i) if the sublessee is a department of the Commonwealth, a certificate, signed by the Secretary or an Assistant Secretary of such department, stating that, on the basis of budgeted appropriations for the fiscal year in which the sublease is to become effective, the sublessee will have available funds sufficient to pay timely all rentals which will be due and payable during such fiscal year, or (ii) if the sublessee is an agency or instrumentality of the Commonwealth, a certificate, signed by the chief executive officer of the sublessee, stating that on the basis of budgeted appropriations and/or estimated revenues for the sublessee, for the fiscal year in which the sublease is to become effective, the sublessee will have available funds sufficient to pay timely all rentals which will be due and payable during such fiscal year. (Section 710).

The Authority covenants that it will cause audits to be made of its books and accounts by an independent firm of certified public accountants chosen by the Authority. Reports of such audits shall, among other things, set forth the findings of such certified public accountants as to whether the moneys received by the Authority under the 1995 Bond Resolution have been applied in accordance with the provisions thereof. Copies of such reports shall be filed with the Fiscal Agent and shall be mailed by the Authority to each bondholder who shall have filed his name and address with the Secretary of the Authority for such purpose. (Section 712).

### **Modifications**

The Authority may adopt resolutions supplemental to the 1995 Bond Resolution without the consent of the bondholders to cure any ambiguity, formal defect or omission or to correct any inconsistent provisions or errors in the 1995 Bond Resolution; provided such action shall not adversely affect the interests of the bondholders, or to grant or confer upon the bondholders any additional rights, remedies, powers, authority or security that may lawfully be granted to or conferred upon the bondholders, or to add to the conditions, limitations and restrictions on the issuance of Bonds, or to add to the covenants and agreements of the Authority in the 1995 Bond Resolution or to surrender any right or power reserved to or conferred upon the Authority. (Section 901).

The holders of not less than a majority in aggregate principal amount of the Bonds then outstanding shall have the right to consent to and approve the adoption of such resolution or resolutions supplemental to the 1995 Bond Resolution as shall be deemed necessary or desirable by the Authority for the purpose of modifying, altering, amending, adding to or rescinding any of the terms and provisions contained in the 1995 Bond Resolution; provided, however, that nothing contained in the 1995 Bond Resolution shall permit, or be construed as permitting, (a) an extension of the maturity of the principal of or the interest on any Bond or (b) a reduction in the principal amount of any Bond or the redemption premium or the rate of interest thereon, or (c) the creation of a lien upon or a pledge of 1995 Debt Service Rentals other than the liens and pledges created by or pursuant to the 1995 Bond Resolution, or (d) a preference or priority of any Bond or Bonds over any other Bond or Bonds, or (e) a reduction in the aggregate principal amount of the Bonds required for consent to such supplemental resolution. (Section 902). No supplemental resolution may, however, change, amend or modify the rights or obligations of the Fiscal Agent under the 1995 Bond Resolution without the written consent of the Fiscal Agent. (Section 904).

## Notice of Default

In the event that on the second business day prior to the date on which a payment of interest, principal, or premium, if any, is due on any Bond there is not an amount sufficient in such account or fund as the Fiscal Agent may draw upon for the payment on such due date of such interest, principal, or premium, or the Authority shall default in the due and punctual making of any 1995 Sinking Fund deposit required by Section 502 of the 1995 Bond Resolution, the Fiscal Agent shall promptly give written notice of such insufficiency or default, as the case may be, to the Authority, the Secretary of the Treasury of the Commonwealth and Government Development Bank. In the event that the Authority shall default in the due and punctual performance of any other covenants or agreements in the Bonds or the 1995 Bond Resolution and the Fiscal Agent shall have knowledge of, or is notified of, such default, and the Authority shall fail to correct such default within thirty (30) days after notice thereof to the Authority by the Fiscal Agent, the Fiscal Agent shall promptly give notice of such default to the Secretary of the Treasury of the Commonwealth and Government Development Bank. (Section 804).

The 1995 Bond Resolution and the Bonds do not provide for acceleration of the maturities of the Bonds in the event of a default thereunder or in any other circumstances and do not provide that the bondholders may require the Fiscal Agent to take any action on their behalf.

## TAX MATTERS

*Series M Bonds and Series N Bonds.* In the opinion of Squire, Sanders & Dempsey L.L.P., Bond Counsel, under existing law (i) interest on the Series M Bonds and the Series N Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), and is not an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations, and (ii) the Series M Bonds and the Series N Bonds and the interest thereon are exempt from state, Commonwealth, and local income taxation. Bond Counsel will express no opinion as to any other tax consequences regarding the Series M Bonds and the Series N Bonds.

The opinion on tax matters will be based on and will assume the accuracy of certain representations and certifications, and continuing compliance with certain covenants, of the Authority contained in the transcript of proceedings and that are intended to evidence and assure the foregoing, including that the Series M Bonds and the Series N Bonds are and will remain obligations the interest on which is excluded from gross income for federal income tax purposes. Bond Counsel will not independently verify the accuracy of the Authority's certifications and representations or the continuing compliance with the Authority's covenants.

The opinion of Bond Counsel is based on current legal authority and covers certain matters not directly addressed by such authority. It represents Bond Counsel's legal judgment as to exclusion of interest on the Series M Bonds and the Series N Bonds from gross income for federal income tax purposes but is not a guaranty of that conclusion. The opinion is not binding on the Internal Revenue Service ("IRS") or any court. Bond Counsel expresses no opinion about (i) the effect of future changes in the Code and the applicable regulations under the Code or (ii) the interpretation and the enforcement of the Code or those regulations by the IRS.

The Code prescribes a number of qualifications and conditions for the interest on state and local government obligations to be and to remain excluded from gross income for federal income tax purposes, some of which require future or continued compliance after issuance of the obligations. Noncompliance with these requirements by the Authority may cause the loss of such status and result in the interest on the Series M Bonds and the Series N Bonds being included in gross income for federal income tax purposes retroactively to the date of issuance of the Series M Bonds and the Series N Bonds. The Authority has covenanted, to the extent permitted by the Constitution and the laws of the Commonwealth, to take the actions required of it for the interest on the Series M Bonds and the Series N Bonds to be and to remain excluded from gross income for federal income tax purposes, and not to take any actions that would adversely affect that exclusion. After the date of issuance of the Series M Bonds and the Series N Bonds, Bond Counsel will not undertake to determine (or to so inform any person) whether any actions taken or not taken, or any events occurring or not occurring, or any other matters coming to Bond Counsel's attention, may adversely affect the exclusion from gross income for federal income tax purposes of interest on the Series M Bonds and the Series N Bonds or the market prices of the Series M Bonds and the Series N Bonds. Bond

Counsel is not aware of any provision of the Constitution or laws of the Commonwealth that would prevent the Authority from complying with the requirements of the Code.

A portion of the interest on the Series M Bonds and the Series N Bonds earned by certain corporations may be subject to a federal corporate alternative minimum tax. In addition, interest on the Series M Bonds and the Series N Bonds may be subject to a federal branch profits tax imposed on certain foreign corporations doing business in the United States and to a federal tax imposed on excess net passive income of certain S corporations.

Under the Code, the exclusion of interest from gross income for federal income tax purposes may have certain adverse federal income tax consequences on items of income, deduction or credit for certain taxpayers, including financial institutions, certain insurance companies, recipients of Social Security and Railroad Retirement benefits, those that are deemed to incur or continue indebtedness to acquire or carry tax-exempt obligations, and individuals otherwise eligible for the earned income tax credit. The applicability and extent of these and other tax consequences will depend upon the particular tax status or other tax items of the owner of the Series M Bonds and the Series N Bonds. Bond Counsel will express no opinion regarding those consequences.

Ownership of tax-exempt obligations, including the Series M Bonds and the Series N Bonds, may also result in collateral income tax consequences under Puerto Rico law to financial institutions doing business in Puerto Rico.

Legislation affecting tax-exempt obligations is regularly considered by the United States Congress. There can be no assurance that legislation enacted or proposed, or actions by a court, after the date of issuance of the Series M Bonds and the Series N Bonds, will not have an adverse effect on the tax status of interest on the Series M Bonds and the Series N Bonds or the market values of the Series M Bonds and the Series N Bonds.

On May 21, 2007, the United States Supreme Court agreed to hear *Dep't of Revenue of Kentucky v. Davis*. In the *Davis* case, the Kentucky Court of Appeals held that Kentucky's exemption from taxation of interest on bonds issued by Kentucky and its political subdivisions and its taxation of interest on bonds issued by other states and their political subdivisions violates the Commerce Clause of the United States Constitution. This ruling does not apply directly to bonds of the Authority (including the Series M Bonds and the Series N Bonds) because the interest on those bonds is exempt from state and local income taxation by virtue of federal law. If the United States Supreme Court sustains the *Davis* decision, however, one possible outcome could be that states with income tax laws similar to Kentucky's would cease to tax interest on bonds of other states and their political subdivisions. The introduction or enactment of any such future legislation might adversely affect the market value of the Series M Bonds and the Series N Bonds, as such legislation could reduce the current tax advantage of bonds of the Authority. It is not possible to predict how the United States Supreme Court will decide the *Davis* case or to predict any change in state law that would be occasioned by the affirmance of the *Davis* decision, nor is it possible to predict the effect, if any, of that affirmance or any change in state law on the market value of the Series M Bonds and the Series N Bonds.

Prospective purchasers of the Series M Bonds and the Series N Bonds should consult their tax advisers regarding pending or proposed federal and state tax legislation, the *Davis* case, and other court proceedings, and prospective purchasers of the Series M Bonds and the Series N Bonds at other than their original issuance at the respective prices or yields indicated in the inside cover page of this Official Statement should also consult their tax advisers regarding other tax considerations such as the consequences of market discount, as to all of which Bond Counsel expresses no opinion.

Bond Counsel's engagement with respect to the Series M Bonds and the Series N Bonds ends with the issuance of the Series M Bonds and the Series N Bonds, and, unless separately engaged, Bond Counsel is not obligated to defend the Authority or the beneficial owners regarding the tax status of interest on the Series M Bonds and the Series N Bonds in the event of an audit examination by the IRS. The IRS has a program to audit tax-exempt obligations to determine whether the interest thereon is includible in gross income for federal income tax purposes. If the IRS does audit the Series M Bonds and the Series N Bonds, under current IRS procedures, the IRS will treat the Authority as the taxpayer and the beneficial owners of the Series M Bonds and the Series N Bonds will have only limited rights, if any, to obtain and participate in judicial review of such audit. Any action of the IRS, including but not limited to selection of the Series M Bonds and the Series N Bonds for audit, or the course or result

of such audit, or an audit of other obligations presenting similar tax issues, may affect the market prices for the Series M Bonds and the Series N Bonds.

*Series O Bonds.* In the opinion of Quiñones & Sánchez PSC, Special Tax Counsel, under existing law (i) interest on the Series O Bonds is exempt from Commonwealth of Puerto Rico taxation; (ii) interest on the Series O Bonds, under most circumstances, is exempt from United States income taxation to residents of Puerto Rico and (iii) interest on the Series O Bonds is not excludable from gross income for federal income tax purposes under Section 103 of the Code. This section does not purport to cover all of the Puerto Rico tax and United States federal income tax consequences arising from the purchase and ownership of the Series O Bonds. The following is based upon laws and regulations now in effect and is subject to change.

In the opinion of Special Tax Counsel, based on the provisions of the Puerto Rico Internal Revenue Code of 1994, as amended, and regulations promulgated thereunder (the "P.R. Code"), as now in force:

1. Interest on the Series O Bonds received by, or "original issue discount" (within the meaning of Sections 1272 and 1273 of the P.R. Code) accrued to, a corporation (i) organized under the laws of the Commonwealth and subject to income tax under the P.R. Code as a corporation, or (ii) otherwise constituting a foreign corporation that is subject to income tax under the P.R. Code as a corporation, is not, in the hands of such corporation, subject to income taxation under the P.R. Code provided such interest or "original issue discount" is not effectively connected, or treated as effectively connected, with or attributable to the conduct of a trade or business within the United States by such corporation.

2. Interest on the Series O Bonds received by, or "original issue discount" (within the meaning of Sections 1272 and 1273 of the P.R. Code) accrued to, an individual who is a bona fide resident of the Commonwealth (within the meaning of Sections 933 and 937(a) of the P.R. Code and the regulations issued thereunder) during the entire taxable year in which such interest is received or "original issue discount" is accrued will constitute gross income from sources within the Commonwealth and, therefore, is excludable from gross income pursuant to Section 933(1) of the P.R. Code, provided such interest and original issue discount are not effectively connected with the conduct of a trade or business within the United States by such individual.

3. Interest on the Series O Bonds and any original issue discount accrued or received thereon is not excludable from the gross income of the recipient thereof for United States federal income tax purposes under Section 103(a) of the P.R. Code.

4. Pursuant to Notice 89-40 issued by the IRS on March 27, 1989, gain on the sale, or exchange or redemption of the Series O Bonds by an individual who is a bona fide resident of the Commonwealth (within the meaning of Sections 933 and 937(a) of the P.R. Code and the regulations issued thereunder) during the entire taxable year will constitute income from sources within the Commonwealth and, therefore, qualify for the exclusion from gross income provided in Section 933(1) of the P.R. Code, provided such Series O Bonds do not constitute inventory in the hands of such individual and at the time that the Series O Bonds were acquired by such individual, such individual was a bona fide resident of the Commonwealth (within the meaning of Sections 933 and 937(a) of the P.R. Code and the regulations issued thereunder).

5. The transfer of the Series O Bonds by death or gift will not be subject to estate or gift tax under the P.R. Code in the case of decedents or donors who, at the time of death or gift, are (i) residents of the Commonwealth and (ii) United States citizens that acquired such citizenship solely by reason of birth or residence in the Commonwealth.

Prospective owners of the Series O Bonds should also be aware that the Code provides special rules for the taxation of shareholders of foreign corporations that qualify as "controlled foreign corporations," "personal holding companies," or "passive foreign investment companies," as such terms are defined by the Code.

## **Original Issue Discount and Original Issue Premium**

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

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

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

## **VERIFICATION OF MATHEMATICAL COMPUTATIONS**

The arithmetical accuracy of (a) the mathematical computations of the adequacy of the outstanding maturing amount of and interest on the government obligations and other available moneys to be deposited in escrow to pay (i) the redemption prices of the Refunded Bonds on their respective redemption dates, together with all payments of interest thereon coming due on or prior to such dates and (ii) the interest due on July 1, 2008 on certain other outstanding Government Facilities Bonds (see *Plan of Financing*), and (b) the mathematical computations supporting the conclusion of Bond Counsel that the Series M Bonds and the Series N Bonds are not "arbitrage bonds" under Section 148 of the Code, will be verified by Samuel Klein and Company, Certified Public Accountants.

## **UNDERWRITING**

The Underwriters have jointly and severally agreed, subject to certain conditions, to purchase the Bonds from the Authority at an aggregate discount of \$4,210,071.27 from the initial offering prices of such bonds. The obligation of the Underwriters to purchase the Bonds is subject to certain conditions precedent, and they will be obligated to purchase all the Bonds, if any 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.

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

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

Santander Securities Corporation ("SSC") and Banc of America Securities LLC ("BAS") have entered into an agreement to jointly pursue municipal securities underwriting opportunities with the Commonwealth, its agencies, municipalities and governmental conduit issuers in the Commonwealth. Under the agreement SSC and BAS will be entitled to receive a portion of each other's revenues from the underwriting of the Bonds in consideration for their professional services.

Oriental Financial Services Corporation ("OFS") and Bear, Stearns & Co., Inc. ("Bear Stearns") have entered into a joint venture agreement under which the parties shall provide services and advice to each other and take risk related to the structuring and execution of certain municipal finance transactions with governmental entities located in the Commonwealth. Pursuant to the terms of such joint venture agreement and in compliance with applicable rules, the parties will be entitled to receive a portion of each other's net profits from the underwriting of the Bonds as consideration for their professional services.

Loop Capital LLC ("LC") and TCM Capital, Inc. ("TCM") have entered into an agreement to jointly pursue municipal securities underwriting opportunities with the Commonwealth, its agencies, municipalities and governmental conduit issuers in the Commonwealth. Under the agreement LC and TCM will be entitled to receive a portion of each other's revenues from the underwriting of the Bonds in consideration for their professional services.

J.P. Morgan Securities Inc. ("JPMSI") and Scotia Capital (USA) Inc. ("SCUSA") have entered into an agreement to assist the Commonwealth, its public corporations, agencies, instrumentalities, and municipalities in structuring and facilitating the issuance of their municipal securities. For each issuance of municipal securities for which both parties act as co-senior manager or co-manager, any sales commissions or takedowns shall be allocated based on actual sales of municipal securities by JPMSI or SCUSA.

#### **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.

#### **LEGAL MATTERS**

The proposed forms of opinions of Squire, Sanders & Dempsey L.L.P., Miami, Florida, as Bond Counsel, and Quiñones & Sánchez PSC, San Juan, Puerto Rico, as Special Tax Counsel, are set forth in *Appendix II*.

#### **GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO**

As required by Act No. 272 of the Legislature, approved on May 15, 1945, as amended, Government Development Bank has acted as financial advisor to the Authority in connection with the Bonds offered hereby. As financial advisor, Government Development Bank participated in the selection of the Underwriters of the Bonds.

Certain of the Underwriters have been selected by Government Development Bank to serve from time to time as underwriters of its obligations and the obligations of the Commonwealth, its instrumentalities and public corporations.

### INDEPENDENT ACCOUNTANTS

The financial statements as of June 30, 2006, of the Authority, are attached hereto as *Appendix I*. Said financial statements were audited by Parissi PSC, certified independent accountants, as set forth in its report therein.

### RATINGS

Moody's Investors Service, Inc. ("Moody's") and Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc. ("S&P"), have given the Bonds underlying ratings of Baa3 and BBB-, respectively. Moody's and S&P are expected to give the Ambac Insured Bonds a rating of Aaa and AAA, respectively, based on the Ambac Insurance Policy to be issued by Ambac Assurance on the date of delivery of such Bonds. Moody's and S&P are expected to give the Series M-3 Bonds ratings of Aaa/VMIG-1 and AAA/A-1+, respectively, based on the issuance of the MBIA Insurance Policy by MBIA and the delivery of the Initial Liquidity Facility by JPMorgan, on the date of delivery of such Bonds. 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 Authority, the Commonwealth, the 1995 Bond Resolution, the Bonds and other relevant information. 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 any ratings obtained 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 15c2-12, as amended (the "Rule"), promulgated by the Securities and Exchange Commission (the "SEC"), the Commonwealth and the Authority have covenanted to the following for the benefit of the beneficial owners of the Bonds (generally the tax owners of the Bonds).

1. the Commonwealth has agreed to file, within 305 days after the end of each fiscal year commencing with the fiscal year ending June 30, 2007, 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, in each case generally found in this Official Statement (including such data concerning the Authority); and
2. The Authority has agreed to file, within 305 days after the end of each fiscal year commencing with the fiscal year ending June 30, 2007, with each NRMSIR and with any Commonwealth SID, the Authority's audited financial statements for the prior fiscal year prepared in accordance with generally accepted accounting principles in effect from time to time; and



3. The Authority has agreed to file, in a timely manner, with each NRMSIR or with the Municipal Securities Rulemaking Board and with any Commonwealth SID, notice of any failure of the Authority to comply with paragraph 2 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. unscheduled 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 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 changes.

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

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

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

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

The Commonwealth expects to provide the information described in paragraph 1 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 a separate document containing such information.

As of the date of this Official Statement, there is no Commonwealth SID, and the NRMSIRs are: Bloomberg Municipal Repository, 100 Business Park Drive, Skillman, New Jersey 08558; Standard & Poor's Securities Evaluations, Inc., 55 Water Street, 45th Floor, New York, New York 10041; FT Interactive Data, Attn: NRMSIR, 100 William Street, 15th Floor, New York, New York 10038; and DPC Data Inc., One Executive Drive, Fort Lee, New Jersey 07024.

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

The Commonwealth and the Authority acknowledge that their respective 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 their respective undertaking shall be limited to a right to obtain specific enforcement of the Authority's or the Commonwealth's obligations thereunder.

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 Authority and the Commonwealth written notice of any request to cure such breach, and the Authority or the Commonwealth, as applicable, 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 and 2A of Act No. 104, approved on June 29, 1955, as amended, 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, the failure to comply with which 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 Authority, 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 Authority; 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 Authority elects that the Covenants shall be deemed amended accordingly.

The Authority and the Commonwealth have 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 to comply with the Rule.

#### MISCELLANEOUS

The foregoing references to and summaries of certain provisions of the 1970 Bond Resolution, the 1978 Bond Resolution, the 1995 Bond Resolution, the Series Resolution, the Lease Agreements with respect to the facilities that are to be financed or refinanced in whole or in part by the Bonds, the Commonwealth Report, the Commonwealth's Annual Financial Report, and the various Acts and the Bonds 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 are the financial statements as of June 30, 2006 of the Authority (*Appendix I*), the Proposed Forms of Opinions of Squire, Sanders & Dempsey L.L.P., Bond Counsel, and Quiñones & Sánchez PSC, Special Tax Counsel (*Appendix II*), the specimen of the MBIA Insurance Policy (*Appendix III*) and the specimen of the Ambac Insurance Policy (*Appendix IV*).

The information set forth in *Recent Developments of the Commonwealth* and in the Commonwealth Report 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, respectively. The information set forth in this Official Statement, except the information appearing in "Initial Liquidity Facility Provider" and "Book Entry Only System" under *Description of the Bonds, Bond Insurance, Provisions Relating to Public Debt of the Commonwealth*, and *Underwriting*, was supplied by the Executive Director of the Authority in her official capacity as such Executive Director and is included in this Official Statement on her authority. The information pertaining to

DTC, Ambac Assurance, MBIA, and the information pertaining to JPMorgan under the caption "Initial Liquidity Facility Provider," was supplied by DTC, Ambac Assurance, MBIA and JPMorgan, respectively.

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

This Official Statement will be filed with each NRMSIR.

**PUERTO RICO PUBLIC BUILDINGS AUTHORITY**

By: /s/ Leila Hernández Umpierre  
Leila Hernández Umpierre  
Executive Director

**APPENDIX I**

**THE FINANCIAL STATEMENTS OF THE AUTHORITY**

**Public Buildings Authority**  
(A Blended Component Unit of the Commonwealth of Puerto Rico)  
Basic Financial Statements, Required Supplementary  
Information and Other Supplementary Information  
For the year ended June 30, 2006 and 2005

**PUBLIC BUILDINGS AUTHORITY**  
**(A Blended Component Unit of the Commonwealth of Puerto Rico)**  
**BASIC FINANCIAL STATEMENTS**  
**AND OTHER SUPPLEMENTARY INFORMATION**  
**For the years ended June 30, 2006 and 2005**

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## **Section I**

### **Independent Auditors' Report**



**PARISSI P.S.C.**  
Certified Public Accountants, Tax & Business Advisors

## **INDEPENDENT AUDITORS' REPORT**

The Board of Directors of  
Public Buildings Authority

We have audited the accompanying basic financial statements as listed in the table of content of the Public Buildings Authority ("the Authority"), a blended component unit of the Commonwealth of Puerto Rico, as of June 30, 2006 and 2005. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Authority as of June 30, 2006 and 2005, and the changes in net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

The Management's Discussion and Analysis presented in Section II is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the Management's Discussion and Analysis. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the basic financial statements taken as a whole. The other supplementary information presented in Section IV, is presented for purposes of additional analysis and is not a required part of the basic financial statements. This information is the responsibility of the Authority's management. Such information has been subjected to the auditing procedures applied in the audit of the 2006 basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the 2006 basic financial statements taken as a whole.

San Juan, Puerto Rico  
**December 19, 2006**

Stamp No. 2181027 was affixed to  
the original of this report.  
License Exp. December 1, 2008



## **Section II**

### **Management's Discussion and Analysis**

**PUBLIC BUILDINGS AUTHORITY**  
**(A Blended Component Unit of the Commonwealth of Puerto Rico)**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
For the years ended June 30, 2006 and 2005

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Following is an overview and analysis of the financial activities of the Public Building Authority (the "Authority") for the fiscal years ended June 30, 2006 and 2005. This discussion and analysis is designed to assist the reader in focusing on the significant financial issues and activities and to identify any significant changes in financial position. It is intended to serve as an introduction to the Authority's financial statements, which are comprised of the basic financial statements and the notes to the financial statement. We encourage readers to consider the information presented here in conjunction with the financial statements taken as a whole.

The Statements of Net Assets present information on all of the Authority's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the Authority is improving or deteriorating. Net assets increase when revenues exceed expenses. Increases to assets without a corresponding increase to liabilities, result in increased net assets, which also indicates an improved financial position.

The Statements of Revenues, Expenses, and Changes in Net Assets present information showing how the Authority's net assets are reported as soon the underlying event occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

The Statements of Cash Flows report cash receipts, cash payments, and net changes in cash resulting from operations, non-capital financing activities, capital and related financing activities, and investing activities.

The notes to the financial statements provide additional information that is essential to the full understanding of the data provided in the basic financial statements.

In addition to the basic financial statements and accompanying notes, various schedules present certain information concerning changes in bonds sinking funds accounts, activity of operating cash accounts, detail of rental operating revenues and receivable and summary of capital improvements programs compared to budget.

**FINANCIAL HIGHLIGHTS:**

- In May 2006, Act No. 97 amended the Authority's Enabling Act broadening the Authority's powers to participate in diverse financing and development options for the betterment of the Authority's economic independence, including the leasing of facilities to municipalities and private organizations, subject to certain restrictions.
- During 2006, the Authority's management implemented a cost savings program aimed to keep and maintain at a minimum the administrative expenses. As a result, operating expenses almost remained the same as fiscal year 2005.
- The Authority's net assets continue to increase for the fiscal years 2006 and 2005. An increase of \$293,071 (.2 %) in 2006 and \$668,841 (.4%) in 2005.
- The Authority's operating income increased from \$88.3 million in 2005 to \$123.5 million in 2006, as a result of an increase in the completion of various rental buildings that are currently generating rental income.

**PUBLIC BUILDINGS AUTHORITY**  
**(A Blended Component Unit of the Commonwealth of Puerto Rico)**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
For the years ended June 30, 2006 and 2005

**Overview of the Financial Statements:**

Statements of Net Assets – Following is condensed financial information of the statement of net assets of the Authority:

<b>ANALYSIS OF 2006 AND 2005</b>			Change	
	2006	2005	In Dollars	Percentage
Current assets	\$ 182,084,846	59,114,616	122,970,230	208.0%
Capital assets	2,768,302,782	2,703,367,897	64,934,885	2.4%
Other noncurrent assets	429,584,485	554,753,965	(125,169,480)	-22.6%
<b>Total assets</b>	<b>\$ 3,379,972,113</b>	<b>3,317,236,478</b>	<b>62,735,635</b>	<b>1.9%</b>
Current liabilities	\$ 212,442,355	185,013,201	27,429,154	14.8%
Noncurrent liabilities	2,980,238,726	2,945,225,316	35,013,410	1.2%
<b>Total liabilities</b>	<b>3,192,681,081</b>	<b>3,130,238,517</b>	<b>62,442,564</b>	<b>2.0%</b>
Net assets				
Invested in capital assets, net of related debt	27,248,937	60,470,851	(33,221,914)	-54.9%
Restricted	7,743,319	13,928,666	(6,185,347)	-44.4%
Unrestricted	152,298,776	112,598,444	39,700,332	35.3%
<b>Total net assets</b>	<b>187,291,032</b>	<b>186,997,961</b>	<b>293,071</b>	<b>0.2%</b>
<b>Total liabilities and net assets</b>	<b>\$ 3,379,972,113</b>	<b>3,317,236,478</b>	<b>62,735,635</b>	<b>1.9%</b>

  

<b>ANALYSIS OF 2005 AND 2004</b>			Change	
	2005	2004	In Dollars	Percentage
Current assets	\$ 59,114,616	733,466,521	(674,351,905)	-91.9%
Capital assets	2,703,367,897	2,504,299,447	199,068,450	7.9%
Other noncurrent assets	554,753,965	68,695,143	486,058,822	707.6%
<b>Total assets</b>	<b>\$ 3,317,236,478</b>	<b>3,306,461,111</b>	<b>10,775,367</b>	<b>0.3%</b>
Current liabilities	\$ 185,013,201	172,666,325	12,346,876	7.2%
Noncurrent liabilities	2,945,225,316	2,947,465,666	(2,240,350)	-0.1%
<b>Total liabilities</b>	<b>3,130,238,517</b>	<b>3,120,131,991</b>	<b>10,106,526</b>	<b>0.3%</b>
Net assets				
Invested in capital assets, net of related debt	60,470,851	65,484,666	(5,013,815)	-7.7%
Restricted	13,928,666	19,598,633	(5,462,514)	-27.9%
Unrestricted	112,598,444	101,245,821	11,352,623	11.2%
<b>Total net assets</b>	<b>186,997,961</b>	<b>186,329,120</b>	<b>668,841</b>	<b>0.4%</b>
<b>Total liabilities and net assets</b>	<b>\$ 3,317,236,478</b>	<b>3,306,461,111</b>	<b>10,775,367</b>	<b>0.3%</b>

Analysis of Net Assets at June 30, 2006 and 2005

The net assets for 2006, compared to prior year, remained almost unchanged with a 2% increase. The balance is the result of operating income and the offset of interest on bonds and notes, amortization of deferred loss on bonds and other non-operating transactions.

**PUBLIC BUILDINGS AUTHORITY**  
**(A Blended Component Unit of the Commonwealth of Puerto Rico)**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
For the years ended June 30, 2006 and 2005

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The other non-current assets show a decrease of \$125 million (22.6 %) mainly driven by the use of the construction fund.

The Authority's investment in capital assets as of June 30, 2006 and 2005 amounted to approximately \$2,768 million and \$2,703 million, respectively, net of accumulated depreciation of approximately \$666 million and \$611 million, respectively. Capital assets include land, buildings, equipment and construction in progress. This increase arises from the ongoing capital construction program. Please refer to the Capital Assets section of this management's discussion and analysis.

Analysis of Net Assets at June 30, 2005 and 2004

The net assets for 2005, if compared to prior year, remained almost unchanged with an increase of 0.4%. The balance is a result of operating income and the offset of interest on bonds and notes, amortization of deferred loss on bonds and other non-operating transactions. For more information please refer to the Analysis of the Statement of Revenues, Expenses and Changes in net Assets 2006 and 2005.

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**PUBLIC BUILDINGS AUTHORITY**  
**(A Blended Component Unit of the Commonwealth of Puerto Rico)**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
For the years ended June 30, 2006 and 2005

Statements of Revenues, Expenses and Changes In Net Assets

	2006	2005	Change	
			In Dollars	Percent
<b>Operating revenues - rent revenue</b>	\$ 314,486,068	\$ 278,721,711	\$ 35,764,357	12.8%
<b>Non-operating revenue:</b>				
Gain on sale of real estate	11,913,675	265,342	11,648,333	4389.9%
Interest income	7,472,688	7,895,219	(422,531)	-5.4%
Other nonoperating revenue	4,362,879	5,560,847	(1,197,968)	-21.5%
<b>Total revenue</b>	<b>338,235,310</b>	<b>292,443,119</b>	<b>45,792,191</b>	<b>15.7%</b>
<b>Operating expenses:</b>				
Salaries and employee benefits	89,664,527	93,344,166	(3,679,639)	-3.9%
Depreciation	56,814,681	46,987,366	9,827,315	20.9%
Utilities	16,616,824	14,156,965	2,459,859	17.4%
Repairs and maintenance	16,001,371	11,653,448	4,347,923	37.3%
Security services	11,564,542	17,968,503	(6,403,961)	-35.6%
Rent and insurance	8,437,196	8,793,260	(356,064)	-4.0%
Other general and administrative	1,401,682	9,671,654	(8,269,972)	-85.5%
<b>Total operating expenses</b>	<b>200,500,823</b>	<b>202,575,362</b>	<b>(2,074,539)</b>	<b>-1.0%</b>
Less: Administrative expenses applied to construction in progress	(9,503,225)	(12,177,120)	2,673,895	-22.0%
<b>Net operating expenses</b>	<b>190,997,598</b>	<b>190,398,242</b>	<b>599,356</b>	<b>0.3%</b>
<b>Non-operating expenses:</b>				
Interest on bonds and notes, net of capitalized interest	133,219,037	92,377,581	40,841,456	44.2%
Amortization of deferred loss on bond defeasance	5,541,882	5,541,882	-	0.0%
Amortization of bond issue costs	456,573	456,573	-	0.0%
Settlement of legal claim and other contingencies	3,926,030	3,000,000	926,030	30.9%
Cost of abandoned projects	3,801,119	-	3,801,119	N/A
<b>Total expenses</b>	<b>337,942,239</b>	<b>291,774,278</b>	<b>46,167,961</b>	<b>15.8%</b>
<b>Excess of revenues over expenses</b>	<b>293,071</b>	<b>668,841</b>	<b>(375,770)</b>	<b>-56.2%</b>
<b>Net assets, beginning of year</b>	<b>186,997,961</b>	<b>186,329,120</b>	<b>668,841</b>	<b>0.4%</b>
<b>Net assets, end of year</b>	<b>\$ 187,291,032</b>	<b>\$ 186,997,961</b>	<b>293,071</b>	<b>0.2%</b>

Analysis of Fiscal Years 2006 and 2005

For 2006 and 2005, operating revenues were \$314.4 million and \$278.7 million, respectively. The completion of various rental buildings under the Authority's Capital Improvement Program resulted in a 13% increase of the rental income.

The net operating expenses remained unchanged compared to prior year 2005. Expenses such as Depreciation, Utilities and Repairs and maintenance increased due to the completion of new rental buildings. This increase is offset by a reduction of administrative expenses that the Authority managed to maintained at a minimum as part of a cost savings program implemented by Management.

Non-operating expenses for the year ended June 30, 2006 increased due to the increase on financing cost of Bonds Payable and Operating Line of Credit.

**PUBLIC BUILDINGS AUTHORITY**  
**(A Blended Component Unit of the Commonwealth of Puerto Rico)**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
For the years ended June 30, 2006 and 2005

	2005	2004	Change	
			In Dollars	Percent
<b>Operating revenues - rent revenue</b>	\$ 278,721,711	226,542,335	\$ 52,179,376	23.0%
<b>Non-operating revenue:</b>				
Gain on sale of real estate	265,342	4,695,000	(4,429,658)	-94.3%
Interest income	7,895,219	2,160,444	5,734,775	265.4%
Other nonoperating revenue	5,560,847	1,801,765	3,759,082	208.6%
Total revenue	<u>292,443,119</u>	<u>235,199,544</u>	<u>57,243,575</u>	<u>24.3%</u>
<b>Operating expenses:</b>				
Salaries and employee benefits	93,344,166	79,794,964	13,549,202	17.0%
Depreciation	46,987,366	43,776,983	3,210,383	7.3%
Utilities	14,156,965	12,167,816	1,989,149	16.3%
Repairs and maintenance	11,653,448	13,547,252	(1,893,804)	-14.0%
Security services	17,968,503	14,316,978	3,651,525	25.5%
Rent and insurance	8,793,260	9,081,125	(287,865)	-3.2%
Other general and administrative	9,671,654	5,966,256	3,705,398	62.1%
Total operating expenses	<u>202,575,362</u>	<u>178,651,374</u>	<u>23,923,988</u>	<u>13.4%</u>
Less: Administrative expenses applied to construction in progress	<u>(12,177,120)</u>	<u>(9,965,425)</u>	<u>(2,211,695)</u>	<u>22.2%</u>
Net operating expenses	<u>190,398,242</u>	<u>168,685,949</u>	<u>21,712,293</u>	<u>12.9%</u>
<b>Non-operating expenses:</b>				
Interest on bonds and notes, net of capitalized interest	92,377,581	76,307,553	16,070,028	21.1%
Amortization of deferred loss on bond defeasance	5,541,882	2,672,882	2,869,000	107.3%
Amortization of bond issue costs	456,573	104,075	352,498	338.7%
Settlement of legal claim and other contingencies	3,000,000	1,104,744	1,895,256	171.6%
Total expenses	<u>291,774,278</u>	<u>248,875,203</u>	<u>42,899,075</u>	<u>17.2%</u>
<b>Excess (deficiency) of revenues over (under) expenses</b>	668,841	(13,675,659)	14,344,500	-104.9%
<b>Net assets, beginning of year</b>	<u>186,329,120</u>	<u>200,004,779</u>	<u>(13,675,659)</u>	<u>-6.8%</u>
<b>Net assets, end of year</b>	<u>\$ 186,997,961</u>	<u>186,329,120</u>	<u>668,841</u>	<u>0.4%</u>

Analysis of 2005 and 2004

For fiscal years 2005 and 2004, the operating revenues were \$278.7 million and \$226.5 million, respectively. The completion of various rental buildings under the Authority's Capital Improvement Program resulted in a 23% increase of the rental income. .

In 2005 operating expenses increased by 13%, compared to prior year. In 2005 Management implemented an intensive Maintenance and Restoration Program throughout all the Authority's facilities. The need for additional resources to complete the Program resulted in an increase of 17% in the Salaries and employee benefits expense.

Non-operating expenses for that same year increased by 17% compared to 2004. Mainly, as a result of an increase in the Debt Service requirement for 2005.

**PUBLIC BUILDINGS AUTHORITY**  
**(A Blended Component Unit of the Commonwealth of Puerto Rico)**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
For the years ended June 30, 2006 and 2005

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**CAPITAL ASSETS**

The Authority's investment in capital assets as of June 30, 2006 and 2005 amounted to approximately \$2.8 billion and \$2.7 billion, respectively, net of accumulated depreciation. Capital assets include land, land improvements, construction in progress, equipment, furniture, and vehicles. Most buildings consist of governmental facilities that are leased to the Commonwealth's agencies and public corporations.

During the years ended June 30, 2006 and 2005 the Authority invested approximately \$170 and \$241 million, respectively, for the construction of buildings that will then be leased to the Commonwealth. This construction activity was financed through interim lines of credit with the Governmental Development Bank (GDB), and the proceeds of Bond Issue. The rent revenue generated by these buildings is pledged first for the payment of long term debt. (For more information, please refer to the "Debt Administration" section below).

**DEBT ADMINISTRATION**

As of June 30, 2006 and 2005, the Authority has outstanding bonds payable of \$2.77 billion and \$2.83 billion, respectively. The balance is net of unamortized bond discounts, bond premium, deferred loss on bonds refunding and bonds issuance costs. For more information, please refer to Note 11 of the Basic Financial Statements.

During fiscal year 2006, credit rating agencies Standards and Poors and Moody's Investor Services reviewed the credit rating on some of the Authority's bonds to BBB and Baa3, respectively. The revision was part of an overall credit rating revision of the Commonwealth.

**REQUEST FOR INFORMATION**

This financial report is designed to provide a general overview of the Authority's finances for all those interested parties. Questions concerning any of the information provided in this report or request for additional financial information should be addressed to the Comptroller's Office, Public Buildings Authority, PO Box 41029, San Juan, and Puerto Rico 00940-1029.

## **Section III**

### **Basic Financial Statements**



**PUBLIC BUILDINGS AUTHORITY**  
**(A Blended Component Unit of the Commonwealth of Puerto Rico)**  
**STATEMENTS OF NET ASSETS**  
**June 30, 2006 and 2005**

	<u>2006</u>	<u>2005</u>
<b>ASSETS</b>		
<b>CURRENT ASSETS:</b>		
Cash and cash equivalents	\$ 88,538,796	\$ 49,047,609
Rent receivable	88,715,809	7,106,365
Notes receivable from other governmental agencies	3,210,153	2,960,642
Other receivables, net	1,620,088	-
Total current assets	<u>182,084,846</u>	<u>59,114,616</u>
<b>NON-CURRENT ASSETS:</b>		
Restricted cash and cash equivalents :		
Bonds sinking funds	143,712,323	117,970,044
Construction funds	47,154,776	193,083,736
Funds available for construction of facilities for other governmental entities	6,209,140	12,730,857
Proceeds from sales of assets	2,492,293	3,874,452
School Renovation Fund	807,943	1,371,845
Payment of salaries under Act. No. 82	16,115	8,207
Rent receivable	69,228,028	94,112,582
Due from Commonwealth of Puerto Rico	63,615,863	57,441,956
Notes receivable from other governmental agencies	20,893,311	22,675,145
Capital assets, net	2,768,302,782	2,703,367,897
Property held for sale	14,385,532	-
Land and buildings under construction for other governmental agencies	29,886,105	17,466,507
Prepaid insurance on bonds and other assets	31,183,056	34,018,634
Total non-current assets	<u>3,197,887,267</u>	<u>3,258,121,862</u>
<b>TOTAL ASSETS</b>	<u>\$ 3,379,972,113</u>	<u>\$ 3,317,236,478</u>

Continues...

**PUBLIC BUILDINGS AUTHORITY**  
**(A Blended Component Unit of the Commonwealth of Puerto Rico)**  
**STATEMENTS OF NET ASSETS (Continued)**  
**June 30, 2006 and 2005**

	<u>2006</u>	<u>2005</u>
<b>LIABILITIES AND NET ASSETS</b>		
<b>LIABILITIES:</b>		
Current liabilities :		
Borrowings under line of credit	\$ 10,000,000	\$ -
Accounts payable	21,370,657	27,214,688
Accrued expenses	<u>5,216,936</u>	<u>5,426,929</u>
Total current liabilities	<u>36,587,593</u>	<u>32,641,617</u>
Current liabilities to be paid from restricted assets :		
Current portion of bonds payable	69,925,000	46,150,000
Interest	69,360,355	66,109,751
Due to contractors	<u>36,569,407</u>	<u>40,111,833</u>
Total current liabilities to be paid from restricted assets	<u>175,854,762</u>	<u>152,371,584</u>
Non-current liabilities :		
Bonds payable	2,769,169,646	2,829,513,624
Borrowings under lines of credit, including accrued interest	97,880,350	12,462,060
Due to contractors, including retainage	52,120,839	51,765,985
Advances from governmental agencies	37,346,255	27,233,495
Compensated absences	13,225,918	15,324,409
Contingencies	6,808,330	5,183,355
Due to Commonwealth	<u>3,687,388</u>	<u>3,742,388</u>
Total non-current liabilities	<u>2,980,238,726</u>	<u>2,945,225,316</u>
Total liabilities	<u>3,192,681,081</u>	<u>3,130,238,517</u>
<b>NET ASSETS:</b>		
Invested in capital assets, net of related debt	27,248,937	60,470,851
Restricted	7,743,319	13,928,666
Unrestricted	<u>152,298,776</u>	<u>112,598,444</u>
Total Net Assets	<u>\$ 187,291,032</u>	<u>\$ 186,997,961</u>

The accompanying notes are an integral part of these statements.

# PUBLIC BUILDINGS AUTHORITY

(A Blended Component Unit of the Commonwealth of Puerto Rico)

## STATEMENTS OF REVENUES, EXPENSES AND CHANGE IN NET ASSETS

For the years ended June 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
<b>OPERATING REVENUES:</b>		
Rent revenue	\$ 314,486,068	\$ 278,721,711
<b>OPERATING EXPENSES:</b>		
Salaries and employee benefits	89,664,527	93,344,166
Depreciation	56,814,681	46,987,366
Utilities	16,616,824	14,156,965
Repairs and maintenance	16,001,371	11,653,448
Security services	11,564,542	17,968,503
Rent and insurance	8,437,196	8,793,260
Other general and administrative	1,401,682	9,671,654
Total operating expenses	<u>200,500,823</u>	<u>202,575,362</u>
Less: Administrative expenses applied to construction in progress	<u>(9,503,225)</u>	<u>(12,177,120)</u>
Net operating expenses	<u>190,997,598</u>	<u>190,398,242</u>
<b>OPERATING INCOME</b>	<u>123,488,470</u>	<u>88,323,469</u>
<b>NON-OPERATING REVENUE (EXPENSES):</b>		
Gain on sale of real estate	11,913,675	-
Interest income	7,472,688	7,895,219
Other income	4,362,879	5,560,847
Interest on bonds and notes, net of capitalized interest of \$23 million and \$39.8 million, respectively	(133,219,037)	(92,377,581)
Amortization of deferred loss on bond defeasance	(5,541,882)	(5,541,882)
Amortization of bond issue costs	(456,573)	(456,573)
Settlement of legal claim and other contingencies	(3,926,030)	(3,000,000)
Cost of abandoned projects	(3,801,119)	265,342
Total non- operating expenses	<u>(123,195,399)</u>	<u>(87,654,628)</u>
<b>NET INCREASE IN NET ASSETS</b>	293,071	668,841
<b>NET ASSETS, beginning of year</b>	186,997,961	186,329,120
<b>NET ASSETS, end of year</b>	<u>\$ 187,291,032</u>	<u>\$ 186,997,961</u>

The accompanying notes are an integral part of these statements.

# PUBLIC BUILDINGS AUTHORITY

(A Blended Component Unit of the Commonwealth of Puerto Rico)

## STATEMENTS OF CASH FLOWS

For the years ended June 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Receipts from tenants covering debt service and operating rent	\$ 257,761,179	\$ 261,162,769
Payments to employees and related benefits	(91,973,011)	(93,809,902)
Payments to suppliers for goods and services	<u>(59,920,647)</u>	<u>(56,227,580)</u>
Net cash provided by operating activities	<u>105,867,521</u>	<u>111,125,287</u>
<b>CASH FLOWS PROVIDED BY NON-CAPITAL FINANCING ACTIVITIES:</b>		
Non-operating income	<u>4,362,879</u>	<u>1,897,780</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:</b>		
Capital expenditures, excluding capitalized interest of \$23 million and \$39.8 million in 2006 and 2005, respectively, and administrative expenses capitalized of \$9.5 million and \$12.2 million in 2006 and 2005, respectively	(139,641,815)	(224,752,073)
Proceeds from sale of land lot	3,192,853	-
Repayment of bonds	(46,150,000)	(35,910,000)
Borrowings under lines of credit	123,294,387	12,303,468
Interest paid	(144,695,931)	(97,949,572)
Net advances from governmental agencies	<u>(2,306,838)</u>	<u>11,176,129</u>
Net cash used in capital and related financing activities	<u>(206,307,344)</u>	<u>(335,132,048)</u>
<b>CASH FLOWS PROVIDED BY INVESTING ACTIVITIES:</b>		
Interest collected	<u>6,921,580</u>	<u>7,895,219</u>
Net cash provided by investing activities	<u>6,921,580</u>	<u>7,895,219</u>
<b>NET DECREASE IN CASH AND CASH EQUIVALENTS</b>	(89,155,364)	(214,213,762)
<b>CASH AND CASH EQUIVALENTS, beginning of year</b>	<u>378,086,750</u>	<u>592,300,512</u>
<b>CASH AND CASH EQUIVALENTS, end of year</b>	<u>\$ 288,931,386</u>	<u>\$ 378,086,750</u>
<b>RECONCILIATION OF CASH AND CASH EQUIVALENTS WITH THE STATEMENT OF NET ASSETS:</b>		
Unrestricted cash	\$ 88,538,796	\$ 49,047,610
Bonds sinking funds	143,712,323	117,970,044
Constructions funds	47,154,776	193,083,736
Funds available for construction to other governmental agencies	6,209,140	12,730,857
Proceeds from sales of assets	2,492,293	3,874,452
Restricted for the School Renovation Fund	807,943	1,371,845
Restricted for the payment of salaries under Act. No. 52	<u>16,115</u>	<u>8,206</u>
	<u>\$ 288,931,386</u>	<u>\$ 378,086,750</u>

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# PUBLIC BUILDINGS AUTHORITY

(A Blended Component Unit of the Commonwealth of Puerto Rico)

## STATEMENTS OF CASH FLOWS

For the years ended June 30, 2006 and 2005

	<u>2006</u>	<u>2005</u>
<b>RECONCILIATION OF OPERATING INCOME TO NET CASH PROVIDED BY OPERATING ACTIVITIES:</b>		
Operating income	\$ 123,488,470	\$ 88,323,469
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	56,814,681	46,987,366
Capitalized salaries and administrative expenses	(9,503,225)	(12,177,120)
Decrease (increase) in operating assets-		
Rent receivable	(56,724,889)	(18,488,633)
Other receivables	(87,765)	215,615
Other assets	32,765	714,225
Increase (decrease) in operating liabilities-		
Accounts payable	(5,844,032)	6,016,101
Accrued expenses and compensated absences	(2,308,484)	(465,736)
Net cash provided by operating activities	\$ <u>105,867,521</u>	\$ <u>111,125,287</u>

### SUMMARY OF NON-CASH TRANSACTIONS:

Exchange transaction-		
Reduction of line of credit	\$ 30,000,000	\$ -
Transfer of a building	(21,279,178)	-

The accompanying notes are an integral part of these statements.

**PUBLIC BUILDINGS AUTHORITY**  
**(A Blended Component Unit of the Commonwealth of Puerto Rico)**  
**NOTES TO FINANCIAL STATEMENTS**  
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**1) Reporting Entity**

The Public Buildings Authority (the “Authority”) is a blended component unit of the Commonwealth of Puerto Rico (the “Commonwealth”), created on June 19, 1958 by Act No. 56, as amended, of the Legislature of Puerto Rico (the “Enabling Act”). The Authority designs, constructs, administers, and provides maintenance to office buildings, courts, warehouses, schools, health care facilities, welfare facilities, shops and related facilities leased to the Commonwealth or any of its departments, agencies, instrumentalities or municipalities. The annual rent for each leased building is based on the amounts needed by the Authority to cover the payment of:

- a) principal, interest and other amortization requirements of the notes and bonds issued to finance the buildings;
- b) operating and maintenance expenses of the buildings, including a reasonable proportional share of administrative expenses, excluding depreciation;
- c) cost of equipment replacement and extraordinary repairs.

Components (b) and (c), described above, are subject to escalation to permit the Authority recover the investment incurred. Amount due from departments and governmental agencies of the Commonwealth may be subject to periodic revisions and/or adjustments based on the availability of funds at the Commonwealth level.

The Enabling Act provides that the full faith and credit of the Commonwealth is pledged for the payment of rent under any lease agreement executed pursuant to the Enabling Act with any department of the Commonwealth. The Enabling Act also provides that the Department of the Treasury of the Commonwealth of Puerto Rico (the “Treasury Department”) will make advances to the Authority for any unpaid portion of rent payable to the Authority by any agency or instrumentality of the Commonwealth that has entered into lease agreements with the Authority. Such advances are recorded as a reduction of accounts receivable since the responsibility of reimbursement belongs to the agency in accordance to the Enabling Act.

**2) Summary of Significant Accounting Policies**

- a. Basis of accounting – The financial statements are presented on the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America. Under this method, revenues are recognized when earned, regardless of when received, and expenses when incurred, regardless of when paid.
- b. Basis of presentation – The financial statements are presented as an enterprise fund and conform to the provisions of Governmental Accounting Standards Board Statement No. 34 (“GASB 34”) “Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments.” GASB 34, as amended, establishes standards for external financial reporting for all state and local governmental entities, which includes a statement of net assets, a statement of revenues, expenses and changes in net assets and a statement of cash flows. It requires the classification of net assets into three components: invested in capital assets, net of related debt; restricted; and unrestricted, described as follows:

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- *Invested in capital assets, net of related debt* – Consists of capital assets, net of accumulated depreciation reduced by the outstanding balance of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction or improvement of those assets. Significant unspent related debt proceeds at year-end, the portion of the debt attributable to the unspent proceeds is not included in the calculation of invested in capital assets, net of related debt. Rather, that portion of the debt is included in the same net assets component as the unspent proceeds.
- *Restricted* – This component of net assets consists of constraints placed on net assets use through external constraints imposed by creditors (such as through covenants), contributors, or law or regulations of other governments or constraints imposed by law through constitutional provision or enabling legislation.
- *Unrestricted* – This component of net assets consists of net assets that do not meet the definition of “restricted” or “invested in capital assets, net of related debt.”

As permitted by Governmental Accounting Standard Board (“GASB”) Statement No. 20, “Accounting and Financial Reporting for Proprietary Funds and other Governmental Entities that use Proprietary Fund Accounting,” the Authority has elected to apply all Financial Accounting Standards Board Statements and Interpretations, issued after November 30, 1989 that does not conflict with those issued by GASB.

- c. Use of estimates – The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results may differ from those estimates.
- d. Fair value of financial instruments – The carrying amounts reported in the statement of net assets for cash and cash equivalents and receivables, approximate fair value due to their short-term duration. Amounts deposited in bond sinking funds and construction funds are carried at fair value. The carrying amount of bonds payable approximates fair value since interest rates on such debt approximate the rates currently available in the market for other debt with similar terms and remaining maturities.
- e. Cash equivalents – Cash equivalents are defined as highly liquid investments with original maturities at the date of purchase of 90 days or less, excluding resources held in restricted accounts.
- f. Custodial credit risk – This is the risk, in the event of a bank failure, that the government’s deposits may not be returned to it.
- g. Allowance for doubtful accounts – The allowance for doubtful accounts is an amount that management believes will be adequate to absorb possible losses on existing receivables, excluding debt service rentals and maintenance charges that may become uncollectible based on evaluations of the collectibility of each balance. Because of uncertainties inherent in the estimation process, management’s estimate of losses in the receivables outstanding and the related allowance may change in the near term. As of June 30, 2006 and 2005, the allowance for doubtful accounts for other receivables amounted to \$13.7 million and \$14.9 million, respectively.

**PUBLIC BUILDINGS AUTHORITY**  
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- h. Investments – The Authority is authorized to invest in Puerto Rico and U.S. government obligations or in obligations guaranteed by the Puerto Rico or U.S. governments or its agencies or instrumentalities. The Authority invests in certificates of deposit with financial institutions rated AA or AAA by Moody’s. Pursuant to the Investment Guidelines for the Commonwealth, adopted by GDB, the Authority may invest in obligations of the Commonwealth, obligations of the United States, certificates of deposit, commercial paper, banker’s acceptances, or in pools of obligations of the municipalities of Puerto Rico, among others. Monies in the sinking funds can only be invested in direct obligations of the United States government, or obligations unconditionally guaranteed by the United States government, and/or interest-bearing time deposits, or other similar arrangements, as provided by the Bond Resolutions.
- i. Restricted assets and liabilities payable from restricted assets – Restricted assets represent the amounts deposited by the Authority to provide for the amortization of bonds payable and related interest costs and cash available in the related construction fund.
- j. Capital assets – Capital assets are recorded at cost. The construction costs include indirect administrative costs and interest costs allocated during the construction period. Capital assets are assets with an individual cost of more than \$100 and a useful life in excess of five (5) years. As of June 30, 2006 and 2005, property (excluding cost of land, equipment and construction in progress) with a total cost of \$2,791 million and \$2,631 million, respectively, is leased to other governmental agencies.

Expenditures for major renewals and betterments that extend the useful live of the assets are capitalized, and normal repairs and maintenance are expensed when incurred. Depreciation determined using the straight-line method over the estimated useful live of the assets is as follow:

Buildings	50 years
Equipment and automobiles	5-10 years

During the year ended June 30, 2006, the Authority evaluated its capital assets for impairment and did not determine any material impairment amount.

- k. Real estate held for sale – Represents the estimated net realizable amount from the sale of certain real estate properties. Capital assets that have been identified to be for sale are presented net of accumulated depreciation and net of the incidental cost to dispose or sell such assets.
- l. Amortization of discount, premium and bond issuance costs on bonds payable – Discount, premiums and bond issuance costs on bonds payable are amortized over the term of the bond, based on the straight line method, which approximates the effective interest method.
- m. Operating revenues and expenses – Operating revenues and expenses are those that result from the Authority’s operations. All leases are deemed to be operating leases. Accordingly, rent revenue is recognized as operating revenue over the term of the lease. Rent revenue is pledged as collateral for the repayment of the Authority’s revenue bonds.
- n. Risk financing – The Authority carries commercial insurance to cover casualty, theft, claims and other losses. The current insurance policies have not been cancelled or terminated. The Authority has not settled any claims in excess of its insurance coverage during the past three years. The Authority also pays premiums for workers compensation insurance to another component unit of the Commonwealth.



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- o. Compensated absences – Compensated absences are accrued when earned by the employees. Employees may carry forward their vacation and sick leave as permitted by statute and may receive a cash payment from the Authority upon termination of employment.
  
- p. Adoption of future accounting pronouncements – The Governmental Accounting Standards Board has issued the following accounting standards that have effective dates after June 30, 2006:
  - Statement No. 45, *Accounting and Financial Reporting by Employers for Post employment Benefits Other than Pensions*, which for the Authority is effective for fiscal years beginning after December 15, 2006.
  - Statement No. 47, *Accounting for Termination Benefits*, which is effective for periods beginning after June 15, 2006
  - Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, which is effective for periods beginning after December 15, 2006.

The Authority has not evaluated the effects of the adoption of the statements on the Authority's financial statements.

### **3) Management Plans**

As presented in the accompanying financial statements, during the years ended June 30, 2006 and 2005, the Authority has faced certain cash flow difficulties arising from the budgetary constraints established by the Commonwealth, in the collection of the accumulated rent receivable. The Authority is dependent upon the timely payment of the rent revenue when due, mainly due from agencies and instrumentalities of the Commonwealth. The appropriated budget by the Commonwealth for fiscal years ended June 30, 2006 and 2005 for the payment of rent to the Authority has fallen short, allowing for the continued accumulation of the rent receivable (\$157 million in 2006 and \$100 million in 2005).

The Authority has established a reorganization plan in order to reduce its operating and administrative costs, including certain employee retirement incentives, among other measures. In addition, the Authority has identified several properties that may be sold to provide additional funds, and is currently negotiating with the Commonwealth the acceleration of the collection of rent in arrears. In the opinion of the management of the Authority, these plans, should they be successful, will allow the Authority to continue operating without major cash flow difficulties. However, since the implementation of these plans will also depend on the Commonwealth's executive decision, as well as possible legislation requirements, the actual success of these plans cannot be assured.

### **4) Cash, Restricted Cash and Deposits**

The Government does not have a deposit policy for custodial credit risk. As of June 30, 2006 and 2005, \$66 million and \$23 million, respectively, of the Authority's bank balance was exposed to custodial credit risk. However, since these amounts represent deposits at the GDB and the Economic Development Bank for Puerto Rico, component units of the Commonwealth, the collateralization requirement does not apply.

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Restricted cash consist of the following:

- A) Bond sinking funds
- B) Construction funds
- C) Funds for construction of facilities for other governmental entities
- D) Proceeds from sales of assets
- E) School renovation funds
- F) Payment of salaries under Act No. 82

**A) Bond sinking funds**

The bond sinking funds under Bond Resolutions No. 77, 158 and 468 as of June 30, 2006 and 2005, consist of cash, US Treasury Bills and money market funds carried at fair value, as follows:

Description	June 30, 2006		
	Bond Service Account	Reserve and Redemption Accounts	Total
Resolution No. 77 - Office Buildings - Cash	\$ 7,824,729	\$ -	\$ 7,824,729
Resolution No. 158 - Public Education and Health Facilities - US Treasury Bills	40,051,319	3,524,059	43,575,378
Resolution No. 468 - Governmental Facilities - Money Market Funds	92,312,216	-	92,312,216
<b>Totals</b>	<b>\$ 140,188,264</b>	<b>\$ 3,524,059</b>	<b>\$ 143,712,323</b>

Description	June 30, 2005		
	Bond Service Account	Reserve and Redemption Accounts	Total
Resolution No. 77 - Office Buildings - Cash	\$ 10,172,428	\$ -	\$ 10,172,428
Resolution No. 158 - Public Education and Health Facilities - US Treasury Bills	39,440,422	3,401,512	42,841,934
Resolution No. 468 - Governmental Facilities - Money Market Funds	64,955,682	-	64,955,682
<b>Totals</b>	<b>\$ 114,568,532</b>	<b>\$ 3,401,512</b>	<b>\$ 117,970,044</b>

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Each bond sinking fund consists of three (3) separate accounts designated as a “Bond Service Account,” a “Reserve Account” and a “Redemption Account,” except under Resolution No. 468, which has no Reserve Account in its Sinking Fund. Revenues received from debt service rentals with respect to the facilities financed under Bond Resolutions No. 77, No. 158 and No. 468 are deposited with their respective Fiscal Agents for the credit of such accounts in the following order:

- to the Bond Service Account, in such amount as may be required to make the amount equal to the amount of interest then due and payable and the interest which will become due and payable within the next ensuing six months on all bonds of each series then outstanding and the principal of all serial bonds, if any, which will become payable within the next ensuing twelve months;
- to the Redemption Account, in such amount as may be required to make the amounts so deposited in the current fiscal year equal to the amortization requirement, if any, for such fiscal year for the term bonds of each series then outstanding, plus the premium, if any, which would be payable on a like principal amount of bonds if such principal amount of bonds should be redeemed on the next redemption date from monies in their respective Bond Sinking Funds; and
- the remaining balance, if any, is deposited to the credit of the Reserve Account, except under Resolution No. 468, where such balance is deposited to the credit of the Bond Service Account.

Bond Resolution No. 77 requires that monies held in the various accounts be, as nearly as practicable, invested and reinvested in direct obligations of, or obligations on which the principal of and the interest are unconditionally guaranteed by, the United States government. In lieu of such investments, monies in any or all of such accounts may be placed in interest-bearing time deposits.

Bond Resolution No. 158 requires that monies be invested and reinvested in investment obligations, repurchase agreements or time deposits fully secured by investment obligations, as those terms are defined therein.

Bond Resolution No. 468 requires that monies be invested and reinvested in government obligations, bankers’ acceptances, certificates or time deposits of any Commonwealth’s approval bank or national banking association, repurchase or reverse repurchase agreements or any other investment which are rated in one of the three highest rating categories.

Investments will mature or will be subject to redemption by the holder thereof at the option of such holder:

- as to investment of monies in the Bond Service Account and the Redemption Account not later than the dates when the monies held for credit thereof will be required for the purposes intended.
- as to investment of monies in the Reserve Account under Bond Resolution No. 77, (i) 25% of the principal amount not later than the next interest payment date of bonds issued there under, (ii) 25% not later than the second interest payment date after such investment, and (iii) 50% not later than three years after the date of such investment, and

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- as to investment of monies in the Reserve Account under Bond Resolution No. 158, (i) 50% of such monies not later than five years from the date of investment, and (ii) the balance of such monies as directed by an order signed by the Executive Director of the Authority.

The Authority has caused to be deposited to the credit of the respective reserve accounts under the 1970 Bond Resolution and the 1978 Bond Resolution reserve account letters of credit issued by The Bank of Nova Scotia acting through its San Juan Branch ("BNS") (each, a "BNS Reserve Account Letter of Credit" and, collectively, the "BNS Reserve Account Letters of Credit") in the respective amounts required by said resolutions to be held to the credit of such reserve accounts. The scheduled expiration date of the BNS Reserve Account Letters of Credit is July 15, 2008. Among other things, the BNS Reserve Account Letters of Credit authorize drawings for the payment of any amount required to be paid out of moneys in the reserve account to which such BNS Reserve Account Letter of Credit relates after the withdrawal from the applicable reserve account of all cash and securities therein.

The obligations of the Authority under the reimbursement agreements with BNS are payable from the portion of the rentals received by the Authority in respect of the facilities financed or refinanced with the proceeds of the bonds issued under the 1970 Bond Resolution or the 1978 Bond Resolution, as appropriate, and not from any rentals received by the Authority in respect of the government facilities financed or refinanced with the proceeds of any Government Facilities Bonds issued under the 1995 Bond Resolution and allocable to such Government Facilities Bonds.

No reserve account is established or required under the 1995 Bond Resolution.

**B) Construction funds**

Construction Funds are created for the purpose of providing resources for the payment of all or any part of the remaining cost of the Initial Facilities, as defined, or for payment of all or any part of the cost to the Authority of any Additional Facilities or Improvements, as defined, in accordance with the Bond Resolutions. As of June 30, 2006 and 2005 construction funds aggregate \$47,154,776 and \$193,083,736, respectively.

**C) Funds for the construction of facilities for other governmental entities**

Funds for the construction of facilities for other governmental entities represent the balance of the funds received less the amounts invested in the construction of said facilities. The properties constructed through this arrangement belong to the individual agencies and not to the Authority. Upon completion of each project, the Authority settles with the agency either by returning remaining funds or billing for the excess costs over the funds received. Funds available at June 30, 2006 and 2005 amounted to \$6.2 and \$12.7 million, respectively.

**D) Proceeds from sale of assets**

Funds received from the sale of assets are restricted for certain purposes, depending upon the types of assets sold. At June 30, 2006 and 2005, the balance of these funds amounted to \$2.4 and \$3.9 million, respectively.

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**E) School renovation funds**

These funds represent the balance received under federal financial assistance programs, as a sub-recipient of the Commonwealth of Puerto Rico Department of Education. These funds are restricted to be used for projects related to school renovation and are subject to compliance requirements applicable to this federal program. At June 30, 2006 and 2005, the balance of these funds amounted to approximately \$808 thousand and \$1.4 million, respectively.

**F) Payment of salaries under Act No. 52**

These funds represent the amount transferred by the Department of Labor as an incentive to promote employment opportunities. At June 30, 2006 and 2005, the balance of these funds amounted to approximately \$16 and \$8 thousand, respectively.

**5) Rent Receivable**

This balance represents the amount due from Commonwealth agencies and instrumentalities determined in accordance with the corresponding rent contracts. In accordance with the provisions of the Enabling Act, the Secretary of the Treasury of the Commonwealth may make advances on behalf of certain agencies and instrumentalities lessees and make payments on behalf of certain department lessees. Minimum lease rentals for the year ending June 30, 2007 aggregate approximately \$370.5 million. Minimum lease rentals for the following four years and thereafter are not readily available; as they are revised every July 1st based on, among other things, debt service requirements for the particular year. During the year ended June 30, 2006 the Authority reclassified approximately \$69.2 million of the rent receivables as a non current asset because there is an uncertainty of when the collection will be achieved.

**6) Notes and Other Receivables**

On July 23, 2004, the Authority entered into a note receivable agreement with the Department of Education (Institute of Technology in Ponce), for the payment of construction costs aggregating \$12,256,704 to be collected into a thirty two (32) years period plus interest at 2.81%. Subsequent to the signing of the agreement, the Authority credited to the balance due \$4,522,137 as agreed with the Puerto Rico Office of Management and Budget. Future minimum collections, during the remaining term of the note, after the application of the credit of \$4,532,137 are as follows:

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Year ending June 30,	Principal	Interest	Total
2007	\$ 453,565	\$ 616,067	\$ 1,069,632
2008	164,254	202,477	366,731
2009	168,929	197,802	366,731
2010	173,737	192,994	366,731
2011	178,682	188,049	366,731
2012-2016	972,657	860,998	1,833,655
2017-2021	1,119,186	714,469	1,833,655
2022-2026	1,287,790	545,865	1,833,655
2027-2031	1,481,793	351,862	1,833,655
2032-2036	1,733,974	130,316	1,864,290
Total	\$ <u>7,734,567</u>	\$ <u>4,000,899</u>	\$ <u>11,735,466</u>

On July 28, 2004, the Authority entered into a note receivable agreement with the Puerto Rico Courts Administration, for the payment of rent due aggregating \$18,356,379, to be collected into a five (5) years period plus interest at 2.5%. Future minimum collections during the remaining term of the note are as follows:

Year ending June 30,	Principal	Interest	Total
2007	\$ 2,756,588	\$ 410,079	\$ 3,166,667
2008	4,713,457	286,543	5,000,000
2009	8,898,852	120,951	9,019,803
	\$ <u>16,368,897</u>	\$ <u>817,573</u>	\$ <u>17,186,470</u>

Other receivables represents amount due for services not guaranteed by the Commonwealth, net of allowance for doubtful accounts.

**7) Due from Commonwealth of Puerto Rico**

The amount due from the Commonwealth of Puerto Rico represents the approximate costs of certain construction projects that have been either suspended or cancelled unilaterally by the Commonwealth during planning stages and, therefore, the funds must be returned and deposited in the corresponding bond sinking, construction, or reserve accounts, as deemed appropriate by the bond indentures. The Puerto Rico Office of Management and Budget of the Commonwealth (OMB), on a letter dated February 3, 2004, committed to reimburse the total amount due at June 30, 2005 of \$57.4 million.

During the fiscal year ended June 30, 2006, the Authority received the notification to cancel additional projects for which the Authority had already incurred \$6.2 million. On a letter dated December 18, 2006, the OMB recognized that, subject to certain audit requirements by the OMB, this amount shall be recognized as a liability by the Commonwealth. Accordingly the Authority has recognized this amount as an additional amount due from the Commonwealth as, in the opinion of the Authority's management, these costs are similar to those recognized in previous years and will be recovered from future appropriations from the Commonwealth.

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Nevertheless, OMB has not appropriated any funds to reimburse the Authority and, since the timing of the collection cannot be readily determined, this amount is presented as a non-current asset.

**8) Capital Assets**

Capital assets activity for the years ended June 30, 2006 and 2005 were as follows:

	Year Ended June 30, 2006			
	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Capital assets not being depreciated:				
Land	\$ 125,045,535	\$ 2,425,873	\$ (15,048,521)	\$ 112,422,887
Construction in progress	543,036,790	170,567,683	(198,063,570)	515,540,903
	<u>668,082,325</u>	<u>172,993,556</u>	<u>(213,112,091)</u>	<u>627,963,790</u>
Capital assets being depreciated:				
Buildings	2,630,594,993	187,088,543	(26,798,610)	2,790,884,926
Equipment and automobiles	15,380,234	-	(92,466)	15,287,768
	<u>2,645,975,227</u>	<u>187,088,543</u>	<u>(26,891,076)</u>	<u>2,806,172,694</u>
Less accumulated depreciation for:				
Buildings	(600,395,453)	(55,492,502)	1,347,690	(654,540,265)
Equipment and automobiles	(10,294,202)	(1,322,179)	322,944	(11,293,437)
	<u>(610,689,655)</u>	<u>(56,814,681)</u>	<u>1,670,634</u>	<u>(665,833,702)</u>
Capital assets being depreciated, net	<u>2,035,285,572</u>	<u>130,273,862</u>	<u>(25,220,442)</u>	<u>2,140,338,992</u>
Capital assets, net	<u>\$ 2,703,367,897</u>	<u>\$ 303,267,418</u>	<u>\$ (238,332,533)</u>	<u>\$ 2,768,302,782</u>

	Year Ended June 30, 2005			
	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>
Capital assets not being depreciated:				
Land	\$ 116,663,163	8,788,023	(405,651)	125,045,535
Construction in progress	588,368,131	241,521,218	(286,852,559)	543,036,790
	<u>705,031,294</u>	<u>250,309,241</u>	<u>(287,258,210)</u>	<u>668,082,325</u>
Capital assets being depreciated:				
Buildings	2,349,404,287	281,190,706	-	2,630,594,993
Equipment and automobiles	14,452,221	1,814,064	(886,051)	15,380,234
	<u>2,363,856,508</u>	<u>283,004,770</u>	<u>(886,051)</u>	<u>2,645,975,227</u>
Less accumulated depreciation for:				
Buildings	(553,637,743)	(46,757,710)	-	(600,395,453)
Equipment and automobiles	(10,950,612)	(229,656)	886,066	(10,294,202)
	<u>(564,588,355)</u>	<u>(46,987,366)</u>	<u>886,066</u>	<u>(610,689,655)</u>
Capital assets being depreciated, net	<u>1,799,268,153</u>	<u>236,017,404</u>	<u>15</u>	<u>2,035,285,572</u>
Capital assets, net	<u>\$ 2,504,299,447</u>	<u>\$ 486,326,645</u>	<u>(287,258,195)</u>	<u>2,703,367,897</u>

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Total interest costs capitalized during the years ended June 30, 2006 and 2005, aggregate to approximately \$23 million and \$39.8 million, respectively. Total general and administrative expenses capitalized during the years ended June 30, 2006 and 2005, aggregates approximately \$9.5 million and \$12.2 million, respectively.

At June 30, 2006, construction in progress includes approximately \$73 million in projects that have been postponed because they do not have financing sources identified in order to be completed. However, the Authority believes that these projects will continue in the near future, and no impairment loss has been deemed necessary to be recognized.

At June 30, 2006, the carrying amount of capital assets that are idle that the Authority expects to continue to use, amounted to approximately \$452,000.

**9) Property Held for Sale**

During the year ended June 30, 2006, the Authority identified certain properties for sale, as part of its efforts to increase liquidity. The amount shown of \$14.4 million was reclassified from capital assets as property held for sale and is recorded at cost. No cost to disposal has been estimated as these properties consist of real estate and the Authority believes that the net realizable amount will exceed the current book value of the property held for sale.

**10) Land and Buildings Under Construction and Advances from Other Governmental**

Land and buildings under construction for other governmental agencies as of June 30, 2006 and 2005 were as follows:

	June 30, 2006			
	2005	Increase	Decrease	2006
Construction in progress	\$ 17,466,507	\$ 12,419,598	\$ -	\$ 29,886,105

  

	June 30, 2005			
	2004	Increase	Decrease	2005
Construction in progress	\$ 9,320,236	\$ 9,130,406	\$ (984,135)	\$ 17,466,507

Advances from other governmental entities at June 30, 2006 and 2005 amounted to \$37.3 million and \$27.2 million, respectively. These amounts represent funds received from several agencies and municipalities for the construction of projects.



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**11) Bonds Payable**

Bonds payable as of June 30, 2006 and 2005 were as follow:

<u>Description</u>	<u>2006</u>	<u>2005</u>
<b>Office Buildings Bonds -</b>		
Serial Bonds, maturing through 2010, with interest rates ranging from 4 1/2% to 6 9/10% \$	14,300,000	\$ 16,675,000
Term Bonds, maturing through 2021, with interest rates ranging from 5 1/2% to 6%	37,315,000	37,315,000
Capital Appreciation Bonds, maturing through 2006, with interest rates ranging from 6 3/5% to 7 3/20%	3,600,000	6,962,360
Tax-exempt components maturing through 2008, with interest rates ranging from 5 1/2% to 5 3/5%	10,520,000	10,520,000
	<u>65,735,000</u>	<u>71,472,360</u>
<b>Public Education and Health Facilities Bonds -</b>		
Serial Bonds, maturing through 2010, with interest rates ranging from 4 1/2% to 6 3/5%	90,045,000	112,825,000
Capital Appreciation Bonds, maturing through 2006, with interest rates ranging from 5% to 6 7/10%	11,760,000	22,747,376
Tax-exempt components maturing through 2007, with interest rates ranging from 5 1/2% to 5 3/5%	61,640,000	61,640,000
	<u>163,445,000</u>	<u>197,212,376</u>
<b>Government Facilities Revenue Bonds -</b>		
Serial Bonds maturing through 2025, with interest rates ranging from 3% to 6.75%	996,230,000	999,240,000
Term Bonds Maturing through 2036, with interest rates ranging from 3% to 5.75%	1,551,340,000	1,551,340,000
Capital Appreciation Bonds, maturing through 2031, with interest rates ranging from 5 1/10% to 5 1/2%	145,558,639	141,492,802
	<u>2,693,128,639</u>	<u>2,692,072,802</u>
Total bonds outstanding	2,922,308,639	2,960,757,538
Less: Bonds discounts	(28,485,421)	(29,961,956)
Deferred loss on bonds defeased	(106,051,866)	(111,593,747)
Deferred bond issuance costs	(12,026,321)	(12,482,894)
Plus: Bonds premiums	63,349,615	68,944,683
Net bonds payable	<u>2,839,094,646</u>	<u>2,875,663,624</u>
Less: Current portion	(69,925,000)	(46,150,000)
Total bonds payable	<u>\$ 2,769,169,646</u>	<u>\$ 2,829,513,624</u>

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Aggregate maturities of sinking funds' amortization requirements on bonds, (excluding discounts and premiums), accreted value on bonds and related interest payments in future years are as follows:

Year ending June 30,	Principal	Interest
2007	\$ 56,854,982	\$ 152,464,217
2008	73,056,893	138,933,672
2009	80,684,097	134,992,062
2010	86,740,000	128,119,365
2011	89,455,000	123,273,447
2011-2015	318,442,418	484,228,739
2016-2020	397,340,000	488,677,816
2021-2025	396,700,000	392,901,090
2026-2030	494,190,000	288,260,503
2031-2035	593,623,797	188,197,050
2036-2040	<u>297,400,000</u>	<u>14,263,441</u>
Principal outstanding and interest	2,884,487,187	2,534,311,402
Add (deduct): Accreted value on bonds outstanding	<u>37,821,452</u>	<u>(37,821,453)</u>
	<u>\$ 2,922,308,639</u>	<u>\$ 2,496,489,949</u>

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Activity of bonds payable during the year ended June 30, 2006 is as follows:

	June 30, 2006				
	2005	Issuances/ Accretion	Payments/ Current	2006	Current Portion
<b>Office Building Bonds -</b>					
Serial Bonds	\$ 16,675,000	\$ -	\$ (2,375,000)	\$ 14,300,000	\$ 2,500,000
Terms Bonds	37,315,000	-	-	37,315,000	-
Capital Appreciation Bonds	6,962,360	242,640	(3,605,000)	3,600,000	3,600,000
Tax-Exempt Bonds	10,520,000	-	-	10,520,000	-
	<u>71,472,360</u>	<u>242,640</u>	<u>(5,980,000)</u>	<u>65,735,000</u>	<u>6,100,000</u>
<b>Public Education and Health Facilities Bonds -</b>					
Serial Bonds	112,825,000	-	(22,780,000)	90,045,000	24,030,000
Capital Appreciation Bonds	22,747,376	792,624	(11,780,000)	11,760,000	11,760,000
Tax-Exempt Bonds	61,640,000	-	-	61,640,000	-
	<u>197,212,376</u>	<u>792,624</u>	<u>(34,560,000)</u>	<u>163,445,000</u>	<u>35,790,000</u>
<b>Government Facilities Revenue Bonds -</b>					
Serial Bonds	999,240,000	-	(5,610,000)	993,630,000	25,600,094
Terms Bonds	1,551,340,000	-	-	1,551,340,000	-
Capital Appreciation Bonds	141,492,802	6,665,836	-	148,158,638	2,434,906
	<u>2,692,072,802</u>	<u>6,665,836</u>	<u>(5,610,000)</u>	<u>2,693,128,638</u>	<u>28,035,000</u>
Total bonds outstanding	2,960,757,538	7,701,100	(46,150,000)	2,922,308,638	69,925,000
Less: Bonds discount	(29,961,956)	-	1,476,535	(28,485,421)	-
Deferred loss on bond defeased	(111,593,747)	-	5,541,882	(106,051,865)	-
Deferred bond issuance cost	(12,482,894)	-	456,573	(12,026,321)	-
Plus: Bonds premiums	68,944,683	-	(5,595,068)	63,349,615	-
Total bonds payable, net	<u>\$ 2,875,663,624</u>	<u>\$ 7,701,100</u>	<u>\$ (44,270,078)</u>	<u>\$ 2,839,094,646</u>	<u>\$ 69,925,000</u>

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Activity of bonds payable during the year ended June 30, 2005 is as follow:

	June 30, 2005				
	2004	Issuances/ Accretion	Payments/ Current	2005	Current Portion
Office Building Bonds -					
Serial Bonds	\$ 18,925,000	\$ -	\$ (2,250,000)	\$ 16,675,000	\$ 2,375,000
Terms Bonds	37,315,000	-	-	37,315,000	-
Capital Appreciation Bonds	10,103,159	469,201	(3,610,000)	6,962,360	3,605,000
Tax-Exempt Bonds	<u>10,520,000</u>	<u>-</u>	<u>-</u>	<u>10,520,000</u>	<u>-</u>
	<u>76,863,159</u>	<u>469,201</u>	<u>(5,860,000)</u>	<u>71,472,360</u>	<u>5,980,000</u>
Public Education and Health Facilities Bonds -					
Serial Bonds	130,785,000	-	(17,960,000)	112,825,000	22,780,000
Capital Appreciation Bonds	33,009,406	1,532,970	(11,795,000)	22,747,376	11,780,000
Tax-Exempt Bonds	<u>61,640,000</u>	<u>-</u>	<u>-</u>	<u>61,640,000</u>	<u>-</u>
	<u>225,434,406</u>	<u>1,532,970</u>	<u>(29,755,000)</u>	<u>197,212,376</u>	<u>34,560,000</u>
Government Facilities Revenue Bonds -					
Serial Bonds	999,535,000	-	(295,000)	999,240,000	-
Terms Bonds	1,551,340,000	-	-	1,551,340,000	-
Capital Appreciation Bonds	<u>135,120,126</u>	<u>6,372,676</u>	<u>-</u>	<u>141,492,802</u>	<u>5,610,000</u>
	<u>2,685,995,126</u>	<u>6,372,676</u>	<u>(295,000)</u>	<u>2,692,072,802</u>	<u>5,610,000</u>
Total bonds outstanding	2,988,292,691	8,374,847	(35,910,000)	2,960,757,538	46,150,000
Less: Bonds discount	(31,639,934)	-	1,677,978	(29,961,956)	-
Deferred loss on bond defeased	(117,135,629)	-	5,541,882	(111,593,747)	-
Deferred bond issuance cost	(12,939,467)	-	456,573	(12,482,894)	-
Plus: Bonds premiums	<u>74,645,481</u>	<u>-</u>	<u>(5,700,798)</u>	<u>68,944,683</u>	<u>-</u>
Total bonds payable, net	<u>\$ 2,901,223,142</u>	<u>\$ 8,374,847</u>	<u>\$ (33,934,365)</u>	<u>\$ 2,875,663,624</u>	<u>\$ 46,150,000</u>

The maturities of bonds payable are funded by debt service rental revenue collected from the lessees. The bonds are secured by a pledge of the rentals of government facilities financed or refinanced by such bonds and leased by the Authority to departments, agencies, and instrumentalities of the Commonwealth.

The good faith and credit of the Commonwealth are pledged for the payment or advance of such rentals. The payment of principal and interest on the bonds is further secured by the guaranty of the Commonwealth under which the Commonwealth, pledges to draw from any funds available in the Treasury of Puerto Rico such sums as may be necessary to cover any deficiency in the amount required for the payment of principal and interest on the bonds, in an aggregate principal amount not exceeding \$3,325 million.

The Authority's bonds payable are subject to the arbitrage rebate regulations issued by the Internal Revenue Service of the United States of America that require rebate to the federal government of excess investment earnings on tax-exempt debt proceeds if the yield on those earnings exceeds the effective yield on the related tax-exempt debt issued. Excess earnings must be rebated every five years or upon maturity of the debt, whichever is earlier.

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During fiscal year ended June 30, 2006, bond rating agencies, Standard and Poors and Moodys Investors Services, lowered the Authority's bond rating on several of its bonds.

**Advance refunding and defeased bonds**

In prior years, the Authority defeased certain revenue bonds by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old debts. Accordingly, the trust's account assets and liabilities for the defeased bonds are not included in the statements of net assets. As of June 30, 2006 and 2005, approximately \$656 million and \$765 million of bonds outstanding are considered defeased.

**12) Other Long-Term Liabilities**

Other long term liabilities are composed of the following:

	Year Ended June 30, 2006				
	<u>Beginning Balance</u>	<u>Increases</u>	<u>Payments/ Current</u>	<u>Ending Balances</u>	<u>Current Portion</u>
Borrowings under lines of credit	\$ 12,462,060	125,418,290	(30,000,000)	107,880,350	10,000,000
Due to contractors, including retainage	91,877,817	-	(3,187,571)	88,690,246	36,569,407
Advances from governmental agencies	27,233,495	12,330,224	(2,217,464)	37,346,255	-
Compensated absences	15,324,409	-	(2,098,491)	13,225,918	-
Contingencies	5,183,355	1,624,975	-	6,808,330	-
Due to commonwealth	3,742,388	-	(55,000)	3,687,388	-
Total other long term liabilities	<u>\$ 155,823,524</u>	<u>139,373,489</u>	<u>(37,558,526)</u>	<u>257,638,487</u>	<u>46,569,407</u>

  

	Year Ended June 30, 2005				
	<u>Beginning Balance</u>	<u>Increases</u>	<u>Payments/ Current</u>	<u>Ending Balances</u>	<u>Current Portion</u>
Borrowings under lines of credit	\$ -	12,462,060	-	12,462,060	-
Due to contractors, including retainage	126,157,811	-	(34,279,994)	91,877,817	40,111,833
Advances from governmental agencies	16,971,586	10,261,909	-	27,233,495	-
Compensated absences	1,396,000	13,928,409	-	15,324,409	-
Contingencies	1,500,000	3,683,355	-	5,183,355	-
Due to commonwealth	3,742,388	-	-	3,742,388	-
Total other long term liabilities	<u>\$ 149,767,785</u>	<u>40,335,733</u>	<u>(34,279,994)</u>	<u>155,823,524</u>	<u>40,111,833</u>

**Borrowings under line of credit –**

On July 28, 2004, the Authority executed a credit facility not to exceed \$256 million, bearing interest at 1.50% over the cost of Tax-Exempt Commercial Paper with the Government Development Bank of Puerto Rico (GDB), for the interim financing of its Capital Improvements Program. At June 30, 2006 and 2005 the funds used amounted to \$30.6 million and \$12.3 million, respectively. This amount will be payable from the proceeds of future bond issues by the Authority pursuant to the provision of Section 208 of Resolution No. 468 of June 22, 1995.

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On April 6, 2006, the Authority executed a Loan Agreement with GDB for \$75 million, bearing interest at a variable rate based on 1.25% over the three months LIBOR rate, with a minimum of 5% interest rate. The loan is due on June 30, 2010 and is collateralized with two of the Authority's properties. The loan proceeds were for the Authority's operational needs. Debt service requirements will come from the Authority's rent receivables, as a financing source. Payments of principal and interest will be appropriated from the Commonwealth of Puerto Rico's general budget pursuant to the provisions of the Resolution Num. 387 of December 21, 2005. Principal portion of the loan will be due in future years as follows:

<u>Fiscal year</u>	<u>Amount</u>
2006-07	\$ 10,000,000
2007-08	15,000,000
2008-09	25,000,000
2009-10	25,000,000
	<u>\$ 75,000,000</u>

On June 30, 2006, the Authority executed an Amendment to the Loan Agreement and Cession Contract with GDB, in which the Authority gave up one of its properties as a partial payment to the loan for \$30 million. This transaction resulted in a gain of \$8.7 million recorded as gain on sale of real estate in the Statement of Revenues, Expenses and Change in Net Assets. At this moment that loan was changed to a line of credit and the Authority borrowed \$30 million. For the fiscal year ended June 30, 2006, \$75 million of the line of credit were used.

**Due to contractors, including retainage** – This amount represent the remaining balance due to contractors for projects under construction. Normally, the contractors submit progress billings for projects in progress and the Authority pay these invoices, except for the retainage portion. This withholding is used as a guarantee that the contractor will complete the project in accordance with contract requirements. Normally the retainage will be paid upon completion and acceptable receipt of the projects, as determined by the Authority's engineers.

**Advances from governmental entities** – This amount represent the balance of the amounts advanced by other governmental entities, mainly for the construction of facilities that will be owned by these entities. These projects include appropriations from the Commonwealth to finance the construction of facilities, by these agencies, which in turn request from the Authority to carryout the construction project and the administration of the construction process. Upon acceptable completion, the project is completed and is taken over by the corresponding agency. The assets are not owned by the Authority.

**Compensated absences** – This amount represent the long term portion of the accrued compensated absences, as estimated by the Authority.

**Contingencies** – This amount represent the Authority's estimated of possible legal and contractual settlement arising from normal litigation procedures. The estimated amount was based on the corresponding number of legal cases currently underway, and based upon the advice and consent of the Authority's legal division and its external legal advisors. Actual amount to be settled may be materially different from the amount accrued.

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**Due to Commonwealth** – During the fiscal year ended June 30, 2004, the Authority received a land lot with an appraised value of approximately \$22 million in settlement of amounts due from the Commonwealth of approximately \$18.3 million. The balance represents the excess of the fair value of the exchange real property over the receivable.

**13) Employee Retirement Plan**

The Employees’ Retirement System of the Government of Puerto Rico and its Instrumentalities (the “System”) is a cost sharing multiple-employer defined-benefit pension plan sponsored by, and reported as a component unit of, the Commonwealth. The System was created under Act No. 447 (the “Act”), approved on May 15, 1951, as amended, and became effective on January 1, 1952. All regular appointed and temporary employees of the Authority under age fifty-five (55) at the date of employment become plan participants of the System.

The System provides retirement, death, and disability benefits. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits generally vest after ten (10) years of plan participation. Retirement benefits are determined by the application of stipulated benefit ratios to the member’s average compensation. Average compensation is computed based on the highest thirty-six (36) months of compensation recognized by the System. The annuity, for which a plan member is eligible, is limited to a minimum of \$200 per month and a maximum of 75 percent of the average compensation.

Contribution requirements, which are established by Law and are not actuarially determined, are as follows:

Commonwealth	9.275% of applicable payroll
Employees:	
Hired on or before March 31, 1990	5.775% of monthly gross salary up to \$550 and 8.275% of monthly gross salary over \$550
Hired on or after April 1, 1990	8.275% of monthly gross salary

On September 24, 1999, an amendment to Act, which created the System, was enacted with the purpose of establishing a defined contribution plan effective January 1, 2000. Employees participating in the defined-benefit plan (the “traditional plan”) at December 31, 1999, had the option to either stay in the traditional plan or transfer to System 2000. Persons employed on or after January 1, 2000 are only allowed to become members of System 2000.

System 2000 is a hybrid defined-contribution plan, also known as a cash balance plan. Under this new plan there is a pool of pension assets, which are invested by the System, together with those of System 2000 benefit plan. The Commonwealth does not guarantee benefits at retirement age. The annuity is based on a formula which assumes that each year the participants’ contribution (with a minimum of 8.275 percent of the participants’ salary up to a maximum of 10%) will be invested in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Notes, (2) earn a rate equal to 75% of the return of the System’s investment portfolio (net of management fees), or (3) earn a combination of both alternatives. Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions are not granted under System 2000. The employers’ contributions (9.275% of the employee’s salary) are used to fund the traditional plan. System 2000 reduces the retirement age from sixty-five (65) years to sixty

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(60) years for those employees who joined the current plan on or after January 1, 2000. Total employee and employer contributions for the years ended June 30, 2006 and 2005 are as follows:

	<u>2006</u>	<u>2005</u>
Traditional Plan -		
Employer	\$ 3,642,564	\$ 3,522,575
Employee	<u>\$ 3,207,189</u>	<u>\$ 3,146,538</u>
System 2000 -		
Employer	\$ 1,029,127	\$ 780,236
Employee	<u>\$ 921,677</u>	<u>\$ 698,784</u>

The System issued financial reports that include their basic financial statements and required supplementary information. Those reports may be obtained by writing to the System's administrator at 437 Ponce de León Avenue, Hato Rey, Puerto Rico 00918. Activity of accrued pension costs, included within accrued expenses, during the years ended June 30, 2006 and 2005 is as follows.

<u>Description</u>	<u>2006</u>	<u>2005</u>
Beginning balance	\$ 872,806	\$ 868,328
Increase	4,899,916	4,574,448
Decrease	(4,903,025)	(4,569,970)
Ending balance	<u>\$ 869,697</u>	<u>\$ 872,806</u>

**14) Commitments**

The Authority has entered into various contracts with outside contractors for the construction of buildings and other facilities. The Authority records the liability for these contracts as progress billings are received, based on completed work. The uncompleted portion of these contracts approximated \$239 million and \$274 million as of June 30, 2006 and 2005, respectively.

**15) Contingent Liabilities**

The Authority is a defendant and/or co-defendant in various lawsuits for alleged breach of contracts and other actions arising in the ordinary course of business. Management, based on the advice of the legal counsel, has recorded reserves to cover for possible liabilities related to these claims. These reserves are recorded as part of the contingencies in the accompanying statements of net assets.

**16) Subsequent Events**

The Board of Directors decided to enter into the following two Swap Transactions in order to fix the interest rates on the bonds Series J and K to eliminate the risk of increase in interest rates. On August 8, 2006, the Public Building Authority entered into a Swap Transaction with the Bank of New York. The notional amounts of the transaction are \$50 million and \$39 million. The transaction's effective date is on July 1, 2007 and the termination date is July 1, 2027. The interest rate is a fixed rate of 3.77310%. On September 8, 2006, the Public Building Authority entered into another Swap Transaction with the Royal Bank of Canada. The notional amount of the transaction is \$150 million.



**PUBLIC BUILDINGS AUTHORITY**  
**(A Blended Component Unit of the Commonwealth of Puerto Rico)**  
**NOTES TO FINANCIAL STATEMENTS**  
For the years ended June 30, 2006 and 2005

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The transaction's effective date is on July 1, 2007 and the termination date is July 1, 2026. The interest rate is a fixed rate of 3.65907%.

On September 8, 2006, the Authority executed a Loan Agreement with GDB the interim financing of its Capital Improvement Program in an amount not to exceed \$223.6 million, bearing interest at 1.50% over the cost of Tax-Exempt Commercial Paper issued by GDB. The loan and the accrued interest are due on August 31, 2008 and will be payable from the proceeds of the next bond issue of the Authority.

On October 5, 2006, the Board of Directors approved a Plan of Voluntary Termination benefits. The plan has been communicated to the employees and will be available from October 31, 2006 until December 15, 2006. The actual number of employees that will participate cannot be presently determined. Therefore, the effects of the plan will be reflected in future years.

**17) Reclassifications:**

Certain reclassifications have been made to the 2005 financial statements in order to conform to the 2006 financial statements presentation.



## **Section IV**

## **Other Supplementary Information**

**PUERTO RICO BUILDINGS AUTHORITY**

**SCHEDULE 1**

(A Blended Component Unit Of The Commonwealth of Puerto Rico)

**SCHEDULE OF BOND SINKING FUNDS ACCOUNTS**

**YEAR ENDED JUNE 30, 2006**

	<b>2006 TOTAL</b>	<b>BOND SERVICE ACCOUNT</b>	<b>RESERVE &amp; REDEMPTION ACCOUNT</b>
<b>OFFICE BUILDING BONDS:</b>			
Balance at June 30, 2005	\$ 10,172,428	\$ 10,172,428.00	\$ -
Receipts:			
Debt Service Rentals	9,549,458	9,549,458	-
Disbursements:			
Payment of Bonds interest	(3,513,583)	(3,513,583)	-
Payment of Bonds principal	(5,980,000)	(5,980,000)	-
Other	(2,403,575)	(2,403,575)	-
	<u>(11,897,158)</u>	<u>(11,897,158)</u>	<u>-</u>
<b>Balance at June 30, 2006</b>	<b><u>7,824,728</u></b>	<b><u>7,824,728</u></b>	<b><u>-</u></b>
<b>PUBLIC EDUCATION &amp; HEALTH FACILITIES BONDS:</b>			
Balance at June 30, 2005	42,841,934	39,440,422	3,401,512
Receipts:			
Debt Service Rentals	72,603,956	72,603,956	-
Investments Income	122,547	-	122,547
	<u>72,726,503</u>	<u>72,603,956</u>	<u>122,547</u>
Disbursements:			
Payment of Bonds interest	(13,399,016)	(13,399,016)	-
Payment of Bonds principal	(58,590,000)	(58,590,000)	-
Other	(4,044)	(4,044)	-
	<u>(71,993,060)</u>	<u>(71,993,060)</u>	<u>-</u>
<b>Balance at June 30, 2006</b>	<b><u>43,575,377</u></b>	<b><u>40,051,318</u></b>	<b><u>3,524,059</u></b>
<b>GOVERNMENTAL FACILITIES BONDS:</b>			
Balance at June 30, 2005	64,955,682	64,955,682	-
Receipts:			
Debt Service Rentals	154,887,722	154,887,722	-
Investments Income	1,216,493	1,216,493	-
Other	1,593,972	1,593,972	-
	<u>157,698,187</u>	<u>157,698,187</u>	<u>-</u>
Disbursements:			
Payment of Bonds interest	(124,680,252)	(124,680,252)	-
Payment of Bonds principal	(5,661,399)	(5,661,399)	-
	<u>(130,341,651)</u>	<u>(130,341,651)</u>	<u>-</u>
<b>Balance at June 30, 2006</b>	<b><u>\$ 92,312,218</u></b>	<b><u>\$ 92,312,218</u></b>	<b><u>\$ -</u></b>

**PUERTO RICO BUILDINGS AUTHORITY**

(A Blended Component Unit Of The Commonwealth of Puerto Rico)

**SCHEDULE OF OPERATING CASH ACCOUNT**

**YEAR ENDED JUNE 30, 2006**

**SCHEDULE 2**

<u>DESCRIPTION</u>	<u>BANCO POPULAR</u>	<u>BANCO BILBAO VIZCAYA</u>	<u>BANCO GUBERNAMENTAL DE FOMENTO</u>
BALANCE AT JUNE 30, 2005	\$ 120,602	\$ 10,743	\$ -
Deposits:			
Rent collected	22,738,407	-	223,415,935
Interest	913	-	1,684,102
Other deposits, mainly legislative appropriations	6,205,521	-	-
Transfer from (to) other accounts	(27,973,005)	(10,743)	(23,107,335)
Disbursements:			
For current expenses, transfers to bond service accounts and others	-	-	(201,992,702)
BALANCE AT JUNE 30, 2006	\$ <u>1,092,438</u>	\$ <u>-</u>	\$ <u>-</u>
	(A)	(A)	(A)

A) Balance included in cash and cash equivalents in the accompanying Statements of Net Assets.

**PUERTO RICO BUILDINGS AUTHORITY**  
 (A Blended Component Unit Of The Commonwealth of Puerto Rico)  
**SCHEDULE OF RENT REVENUES AND RECEIVABLES**  
**YEAR ENDED JUNE 30, 2006**

**SCHEDULE 3**

	<b>Revenues</b> <b>Year Ended</b> <b>June 30, 2006</b>	<b>Receivables</b> <b>As of</b> <b>June 30, 2006</b>
<b>OFFICE BUILDINGS:</b>		
Debt service rentals - bonds	\$ 44,181,325	\$ -
Operating, Administrative and equipment replacement reserve rentals	43,103,518	38,862,469
Debt service rentals - notes	<u>104,812</u>	<u>-</u>
Total	<u>87,389,655</u>	<u>38,862,469</u>
<b>PUBLIC EDUCATION BUILDINGS:</b>		
Debt service rentals - bonds	97,323,991	-
Operating, administrative and equipment replacement reserve rentals	91,694,077	76,478,725
Debt service rentals - notes	<u>-</u>	<u>-</u>
***	<u>189,018,068</u>	<u>76,478,725</u>
<b>HEALTH FACILITIES:</b>		
Debt service rentals - bonds	30,747,008	-
Operating, administrative and equipment replacement reserve rentals	7,331,337	42,602,643
Debt service rentals - notes	<u>-</u>	<u>-</u>
Total	<u>38,078,345</u>	<u>42,602,643</u>
<b>TOTAL</b>	<u><u>\$ 314,486,068</u></u>	<u><u>\$ 157,943,837</u></u>

**PUERTO RICO BUILDINGS AUTHORITY**  
(A Blended Component Unit Of The Commonwealth of Puerto Rico)  
**SCHEDULE OF CAPITAL IMPROVEMENT PROGRAM**  
**YEAR ENDED JUNE 30, 2006**

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**SCHEDULE 4**

	<u>ACTUAL</u>	<u>BUDGET</u>
EDUCATIONAL FACILITIES	\$ 147,207,711	\$ 235,592,748
POLICE FACILITIES	9,554,557	26,069,797
OFFICE BUILDINGS	13,130,131	12,115,000
CORRECTIONAL FACILITIES	1,102,640	737,680
COURTHOUSES	1,309,906	1,134,584
FIREHOUSES	4,409,125	3,545,292
AUTHORITY'S EQUIPMENT	349,298	1,194,727
TOTAL	<u>\$ 177,063,368</u>	<u>\$ 280,389,828</u>

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PROPOSED FORMS OF OPINIONS

*Upon delivery of the Series M Bonds, Squire, Sanders & Dempsey L.L.P. is prepared to render its final opinion with respect to the Series M Bonds in substantially the following form:*

December \_\_, 2007

Puerto Rico Public Buildings Authority  
San Juan, Puerto Rico

Re: \$562,850,000 Puerto Rico Public Buildings Authority Government Facilities Revenue Refunding Bonds, Series M, Guaranteed by the Commonwealth of Puerto Rico

Gentlemen:

We have served as bond counsel in connection with the issuance by the Puerto Rico Public Buildings Authority (the "Authority") of its \$562,850,000 aggregate principal amount of Government Facilities Revenue Refunding Bonds, Series M, Guaranteed by the Commonwealth of Puerto Rico (the "Bonds"). The Bonds are dated, mature on July 1 of the years and in such principal amounts and bear interest at the rates, all as set forth in the Resolution referred to hereinbelow. The Bonds are issuable as fully registered Bonds without coupons, in authorized denominations and are subject to redemption prior to maturity, in the manner and in accordance with the terms and conditions of the Resolution.

In our capacity as bond counsel, we have examined the transcript of the proceedings (the "Transcript") of the Authority relating to the issuance of the Bonds, including, without limitation, (i) Act No. 56 of the Legislature of Puerto Rico, approved June 19, 1958, as amended (hereinafter the "Enabling Act"), creating the Authority as a body corporate and politic constituting an instrumentality of the Commonwealth of Puerto Rico (the "Commonwealth"), exercising public and essential governmental functions; (ii) Act No. 17 of the Legislature of Puerto Rico, approved April 11, 1968, as amended (hereinafter called the "Guaranty Act"), providing for the guaranty by the Commonwealth of the payment of the principal of and interest on a principal amount of bonds outstanding at any one time of the Authority, not exceeding \$3,325,000,000, specified by the Authority to be covered by such guaranty, to the extent that the revenues and other moneys of the Authority pledged to the payment of such principal and interest are not sufficient for that purpose; (iii) Resolution No. 468, duly adopted by the Authority on June 22, 1995, as supplemented by Resolution No. 1280, duly adopted by the Authority on December 6, 2007 (said Resolution No. 468, as supplemented by Resolution No. 1280, being hereinafter called the "Resolution"); and (iv) such other documents as we have deemed necessary to render this opinion.

We have also examined a copy of one of the Bonds as executed and authenticated. We assume that all other Bonds have been similarly executed and authenticated.

From such examination, we are of the opinion that:

1. The Enabling Act is valid.
2. The Guaranty Act is valid.
3. Said proceedings have been validly and legally taken.
4. The Bonds have been duly authorized and issued to provide funds to refund certain of the Authority's outstanding bonds as more specifically set forth in the Resolution. The Bonds are valid and binding obligations of the Authority payable solely from the special fund created by the Resolution and designated "Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds Sinking Fund" (the "Sinking Fund") or from moneys provided by the Commonwealth under its guaranty of payment of the principal of and interest on the Bonds. The Authority has



covenanted to deposit to the credit of the Sinking Fund a sufficient amount of the rentals received by the Authority from the leasing of government facilities financed or refinanced by the Authority under the provisions of the Resolution to pay the principal of and the interest on all bonds issued under the provisions of the Resolution (including the Bonds) as the same shall become due and payable, which Sinking Fund is pledged to and charged with the payment of such principal and interest.

5. The Authority has properly specified the Bonds to be covered by the guaranty of the Commonwealth under the Guaranty Act.

6. The good faith and credit of the Commonwealth are pledged for the payment of any amounts required to be paid by the Commonwealth pursuant to said guaranty.

7. The Resolution provides for the issuance, from time to time, under the conditions, limitations and restrictions therein set forth, of additional bonds for the purpose of paying all or part of the cost of government facilities and improvements of such facilities and refunding any bonds issued by the Authority under the provisions of the Resolution or under Resolution No. 77, adopted by the Authority on November 16, 1970, as amended, or under Resolution No. 158, adopted by the Authority on February 14, 1978, as amended.

8. The interest on the Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), and is not an item of tax preference under Section 57 of the Code for purposes of the federal alternative minimum tax imposed on individuals and corporations. The Bonds and the interest thereon are exempt from state, Commonwealth of Puerto Rico and local income taxation. We express no opinion as to any other tax consequences regarding the Bonds.

In giving the opinion set forth in numbered paragraph 8. hereof, we have assumed and relied upon compliance with the Authority's covenants and the accuracy, which we have not independently verified, of the Authority's representations and certifications, all as contained in the Transcript. The accuracy of those representations and certifications, and compliance by the Authority with those covenants, may be necessary for the interest on the Bonds to be and to remain excluded from gross income for federal income tax purposes. Failure to comply with certain of those covenants subsequent to issuance of the Bonds could cause interest on the Bonds to be included in gross income for federal income tax purposes retroactively to the date of issuance of the Bonds. The Authority has covenanted to comply with the requirements of the Code to the extent permitted by the Constitution and laws of the Commonwealth. We are not aware of any provisions of the Constitution or laws of the Commonwealth that would prevent the Authority from complying with the requirements of the Code.

Under the Code, portions of the interest on the Bonds earned by certain corporations may be subject to a corporate alternative minimum tax, and interest on the Bonds may be subject to a branch profits tax imposed on certain foreign corporations doing business in the United States and to a tax imposed on excess net passive income of certain S corporations.

In rendering the opinions set forth herein, we have assumed the accuracy and truthfulness of all public records and of all certifications, documents and other proceedings examined by us that have been executed or certified by public officials acting within the scope of their official capacities and have not verified the accuracy or truthfulness thereof. We have also assumed the genuineness of the signatures appearing upon such public records, certifications, documents and proceedings. As to questions of fact material to our opinion, we have relied on representations of the Authority furnished to us, without undertaking to verify such representations by independent investigation.

It is to be understood that the rights of the holders of the Bonds and the enforceability of the Resolution and the Bonds may be subject to judicial discretion and valid bankruptcy, insolvency, reorganization, moratorium and other laws affecting creditors' rights generally, and subject to general principles of equity (regardless of whether considered in a proceeding in equity or at law).

Respectfully submitted,

[To be signed "Squire, Sanders & Dempsey L.L.P."]

*Upon delivery of the Series N Bonds, Squire, Sanders & Dempsey L.L.P. is prepared to render its final opinion with respect to the Series N Bonds in substantially the following form:*

December \_\_, 2007

Puerto Rico Public Buildings Authority  
San Juan, Puerto Rico

Re: \$329,415,000 Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds, Series N, Guaranteed by the Commonwealth of Puerto Rico

Gentlemen:

We have served as bond counsel in connection with the issuance by the Puerto Rico Public Buildings Authority (the "Authority") of its \$329,415,000 aggregate principal amount of Government Facilities Revenue Bonds, Series N, Guaranteed by the Commonwealth of Puerto Rico (the "Bonds"). The Bonds are dated, mature on July 1 of the years and in such principal amounts and bear interest at the rates, all as set forth in the Resolution referred to hereinbelow. The Bonds are issuable as fully registered Bonds without coupons, in authorized denominations of \$5,000 and integral multiples thereof and are subject to redemption prior to maturity, in the manner and in accordance with the terms and conditions of the Resolution.

In our capacity as bond counsel, we have examined the transcript of the proceedings (the "Transcript") of the Authority relating to the issuance of the Bonds, including, without limitation, (i) Act No. 56 of the Legislature of Puerto Rico, approved June 19, 1958, as amended (hereinafter called the "Enabling Act"), creating the Authority as a body corporate and politic constituting an instrumentality of the Commonwealth of Puerto Rico (the "Commonwealth"), exercising public and essential governmental functions; (ii) Act No. 17 of the Legislature of Puerto Rico, approved April 11, 1968, as amended (hereinafter called the "Guaranty Act"), providing for the guaranty by the Commonwealth of the payment of the principal of and interest on a principal amount of bonds outstanding at any one time of the Authority, not exceeding \$3,325,000,000, specified by the Authority to be covered by such guaranty, to the extent that the revenues and other moneys of the Authority pledged to the payment of such principal and interest are not sufficient for that purpose; (iii) Resolution No. 468, duly adopted by the Authority on June 22, 1995, as supplemented by Resolution No. 1280, duly adopted by the Authority on December 6, 2007 (said Resolution No. 468, as supplemented by Resolution No. 1280, being hereinafter called the "Resolution"); and (iv) such other documents as we have deemed necessary to render this opinion.

We have also examined a copy of one of the Bonds as executed and authenticated. We assume that all other Bonds have been similarly executed and authenticated.

From such examination we are of the opinion that:

1. The Enabling Act is valid.
2. The Guaranty Act is valid.
3. Said proceedings have been validly and legally taken.
4. The Bonds have been duly authorized and issued to pay a portion of the cost of constructing certain buildings and other facilities to be leased to various departments, agencies and instrumentalities of the Commonwealth, including the repayment of certain outstanding notes of the Authority held by Government Development Bank for Puerto Rico, and for paying capitalized interest on the Bonds. The Bonds are valid and binding obligations of the Authority payable solely from the special fund created by the Resolution and designated "Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds Sinking Fund" (the "Sinking Fund") or from moneys provided by the Commonwealth under its guaranty of payment of the principal of and interest on the Bonds. The Authority has covenanted to deposit to the credit of the Sinking Fund a sufficient amount of the

rentals received by the Authority from the leasing of government facilities financed or refinanced by the Authority under the provisions of the Resolution to pay the principal of and the interest on all bonds issued under the provisions of the Resolution (including the Bonds) as the same shall become due and payable, which Sinking Fund is pledged to and charged with the payment of such principal and interest.

5. The Authority has properly specified the Bonds to be covered by the guaranty of the Commonwealth under the Guaranty Act.

6. The good faith and credit of the Commonwealth are pledged for the payment of any amounts required to be paid by the Commonwealth pursuant to said guaranty.

7. The Resolution provides for the issuance, from time to time, under the conditions, limitations and restrictions therein set forth, of additional bonds for the purpose of paying all or a part of the cost of government facilities and improvements of such facilities and refunding any bonds issued by the Authority under the provisions of the Resolution or under Resolution No. 77, adopted by the Authority on November 16, 1970, as amended, or under Resolution No. 158, adopted by the Authority on February 14, 1978, as amended.

8. The interest on the Bonds is excluded from gross income for federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, as amended (the "Code"), and is not an item of tax preference under Section 57 of the Code for purposes of the federal alternative minimum tax imposed on individuals and corporations. The Bonds and the interest thereon are exempt from state, Commonwealth of Puerto Rico and local income taxation. We express no opinion as to any other tax consequences regarding the Bonds.

In giving the opinion set forth in numbered paragraph 8. hereof, we have assumed and relied upon compliance with the Authority's covenants and the accuracy, which we have not independently verified, of the Authority's representations and certifications, all as contained in the Transcript. The accuracy of those representations and certifications, and compliance by the Authority with those covenants, may be necessary for the interest on the Bonds to be and to remain excluded from gross income for federal income tax purposes. Failure to comply with certain of those covenants subsequent to issuance of the Bonds could cause interest on the Bonds to be included in gross income for federal income tax purposes retroactively to the date of issuance of the Bonds. The Authority has covenanted to comply with the requirements of the Code to the extent permitted by the Constitution and laws of the Commonwealth. We are not aware of any provisions of the Constitution or laws of the Commonwealth that would prevent the Authority from complying with the requirements of the Code.

Under the Code, portions of the interest on the Bonds earned by certain corporations may be subject to a corporate alternative minimum tax, and interest on the Bonds may be subject to a branch profits tax imposed on certain foreign corporations doing business in the United States and to a tax imposed on excess net passive income of certain S corporations.

In rendering the opinions set forth herein, we have assumed the accuracy and truthfulness of all public records and of all certifications, documents and other proceedings examined by us that have been executed or certified by public officials acting within the scope of their official capacities and have not verified the accuracy or truthfulness thereof. We have also assumed the genuineness of the signatures appearing upon such public records, certifications, documents and proceedings. As to questions of fact material to our opinion, we have relied on representations of the Authority furnished to us, without undertaking to verify such representations by independent investigation.

It is to be understood that the rights of the holders of the Bonds and the enforceability of the Resolution and the Bonds may be subject to judicial discretion and valid bankruptcy, insolvency, reorganization, moratorium and other laws affecting creditors' rights generally, and subject to general principles of equity (regardless of whether considered in a proceeding in equity or at law).

Respectfully submitted,

[To be signed "Squire, Sanders & Dempsey L.L.P."]

*Upon delivery of the Series O Bonds, Squire, Sanders & Dempsey L.L.P. is prepared to render its final opinion with respect to the Series O Bonds in substantially the following form:*

December \_\_, 2007

Puerto Rico Public Buildings Authority  
San Juan, Puerto Rico

Re: \$3,025,000 Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds, Series O,  
Guaranteed by the Commonwealth of Puerto Rico

Gentlemen:

We have served as bond counsel in connection with the issuance by the Puerto Rico Public Buildings Authority (the "Authority") of its \$3,025,000 aggregate principal amount of Government Facilities Revenue Bonds, Series O, Guaranteed by the Commonwealth of Puerto Rico (the "Bonds"). The Bonds are dated, mature on July 1 of the years and in such principal amounts and bear interest at the rates, all as set forth in the Resolution referred to hereinbelow. The Bonds are issuable as fully registered Bonds without coupons, in authorized denominations of \$5,000 and integral multiples thereof and are subject to redemption prior to maturity, in the manner and in accordance with the terms and conditions of the Resolution.

In our capacity as bond counsel, we have examined the transcript of the proceedings (the "Transcript") of the Authority relating to the issuance of the Bonds, including, without limitation, (i) Act No. 56 of the Legislature of Puerto Rico, approved June 19, 1958, as amended (hereinafter the "Enabling Act"), creating the Authority as a body corporate and politic constituting an instrumentality of the Commonwealth of Puerto Rico (the "Commonwealth"), exercising public and essential governmental functions; (ii) Act No. 17 of the Legislature of Puerto Rico, approved April 11, 1968, as amended (hereinafter called the "Guaranty Act"), providing for the guaranty by the Commonwealth of the payment of the principal of and interest on a principal amount of bonds outstanding at any one time of the Authority, not exceeding \$3,325,000,000, specified by the Authority to be covered by such guaranty, to the extent that the revenues and other moneys of the Authority pledged to the payment of such principal and interest are not sufficient for that purpose; (iii) Resolution No. 468, duly adopted by the Authority on June 22, 1995, as supplemented by Resolution No. 1280, duly adopted by the Authority on December 6, 2007 (said Resolution No. 468, as supplemented by Resolution No. 1280, being hereinafter called the "Resolution"); and (iv) such other documents as we have deemed necessary to render this opinion.

We have also examined a copy of one of the Bonds as executed and authenticated. We assume that all other Bonds have been similarly executed and authenticated.

From such examination, we are of the opinion that:

1. The Enabling Act is valid.
2. The Guaranty Act is valid.
3. Said proceedings have been validly and legally taken.
4. The Bonds have been duly authorized and issued to provide funds to refund certain of the Authority's outstanding bonds as more specifically set forth in the Resolution. The Bonds are valid and binding obligations of the Authority payable solely from the special fund created by the Resolution and designated "Puerto Rico Public Buildings Authority Government Facilities Revenue Bonds Sinking Fund" (the "Sinking Fund") or from moneys provided by the Commonwealth under its guaranty of payment of the principal of and interest on the Bonds. The Authority has covenanted to deposit to the credit of the Sinking Fund a sufficient amount of the rentals received by the Authority from

the leasing of government facilities financed or refinanced by the Authority under the provisions of the Resolution to pay the principal of and the interest on all bonds issued under the provisions of the Resolution (including the Bonds) as the same shall become due and payable, which Sinking Fund is pledged to and charged with the payment of such principal and interest.

5. The Authority has properly specified the Bonds to be covered by the guaranty of the Commonwealth under the Guaranty Act.

6. The good faith and credit of the Commonwealth are pledged for the payment of any amounts required to be paid by the Commonwealth pursuant to said guaranty.

7. The Resolution provides for the issuance, from time to time, under the conditions, limitations and restrictions therein set forth, of additional bonds for the purpose of paying all or part of the cost of government facilities and improvements of such facilities and refunding any bonds issued by the Authority under the provisions of the Resolution or under Resolution No. 77, adopted by the Authority on November 16, 1970, as amended, or under Resolution No. 158, adopted by the Authority on February 14, 1978, as amended.

As bond counsel, we express no opinion as to any federal, state, Commonwealth of Puerto Rico or local tax consequences regarding the Bonds. We understand that you are relying on the opinion of Quiñones & Sánchez PSC, special tax counsel, as to certain tax consequences regarding the Bonds.

In rendering the opinions set forth herein, we have assumed the accuracy and truthfulness of all public records and of all certifications, documents and other proceedings examined by us that have been executed or certified by public officials acting within the scope of their official capacities and have not verified the accuracy or truthfulness thereof. We have also assumed the genuineness of the signatures appearing upon such public records, certifications, documents and proceedings. As to questions of fact material to our opinion, we have relied on representations of the Authority furnished to us, without undertaking to verify such representations by independent investigation.

It is to be understood that the rights of the holders of the Bonds and the enforceability of the Resolution and the Bonds may be subject to judicial discretion and valid bankruptcy, insolvency, reorganization, moratorium and other laws affecting creditors' rights generally, and subject to general principles of equity (regardless of whether considered in a proceeding in equity or at law).

Respectfully submitted,

[To be signed "Squire, Sanders & Dempsey L.L.P."]

*Upon delivery of the Series O Bonds, Quiñones & Sánchez PSC, Special Tax Counsel, is prepared to render its final opinion with respect to the Series O Bonds in substantially the following form:*

December \_\_, 2007

Puerto Rico Public Buildings Authority  
San Juan, Puerto Rico

Re: \$3,025,000 Puerto Rico Public Buildings Authority Government Facilities Revenue Refunding Bonds, Series O, Guaranteed by the Commonwealth of Puerto Rico

Ladies and Gentlemen:

We have acted as Special Tax Counsel in connection with the issuance by the Puerto Rico Public Buildings Authority (the "Authority") of its \$3,025,000 principal amount Government Facilities Revenue Refunding Bonds, Series O, guaranteed by the Commonwealth of Puerto Rico (the "Bonds").

As such counsel we have examined we have examined the transcript of the proceedings (the "Transcript") of the Authority relating to the issuance of the Bonds, including, without limitation, (i) Act No. 56 of the Legislature of Puerto Rico, approved June 19, 1958, as amended (hereinafter the "Enabling Act"), creating the Authority as a body corporate and politic constituting an instrumentality of the Commonwealth of Puerto Rico (the "Commonwealth"), exercising public and essential governmental functions; (ii) Act No. 17 of the Legislature of Puerto Rico, approved April 11, 1968, as amended (hereinafter called the "Guaranty Act"), providing for the guaranty by the Commonwealth of the payment of the principal of and interest on a principal amount of bonds outstanding at any one time of the Authority, not exceeding \$3,325,000,000, specified by the Authority to be covered by such guaranty, to the extent that the revenues and other moneys of the Authority pledged to the payment of such principal and interest are not sufficient for that purpose; (iii) Resolution No. 468, duly adopted by the Authority on June 22, 1995, as supplemented by Resolution No. 1280, duly adopted by the Authority on December 6, 2007 (said Resolution No. 468, as supplemented by Resolution No. 1280, being hereinafter called the "Resolution"); and (iv) such other documents as we have deemed necessary to render this opinion.

We have also examined the United States Internal Revenue Code of 1986, as amended, and regulations promulgated thereunder (the "Code"), the Puerto Rico Internal Revenue Code of 1994, as amended, and regulations promulgated thereunder (the "P.R. Code"), and such other laws as we have deemed relevant for the purpose of rendering this opinion.

In connection with matters opined herein under the Code, please be advised that in accordance with the requirements of IRS Circular 230: (i) such opinions are not intended or written to be used and cannot be used by any person for purposes of avoiding penalties that may be imposed on such person, (ii) such opinions are issued to support the promotion or marketing of the Bonds, and (iii) any person investing in the Bonds should seek advice based on such person's particular circumstances from an independent tax advisor.

From such examination, we are of the opinion that, based on the provisions of Commonwealth law now in force:

1. Interest of the Bonds is exempt from Puerto Rico income and withholding taxes, including the alternative minimum tax imposed by Section 1017 of the P.R. Code.
2. The Bonds are exempt from property taxes imposed by the Municipal Property Tax Act of 1991, as amended, and interest thereon is exempt from the municipal license tax imposed by the Municipal License Tax Act of 1974, as amended.
3. The transfer of the Bonds by (i) gift will not be subject to gift tax under the P.R. Code in the case of donors who are residents of the Commonwealth at the time the gift is made and (ii) death will not be subject to

estate tax under the P.R. Code in the case of a decedent who at the time of death was (x) a resident of Puerto Rico and (y) a United States citizen who acquired such citizenship solely by reason of birth or residence in Puerto Rico.

4. Gain realized from the sale, exchange or redemption of a Bond by an individual that is a resident of the Commonwealth (as determined under the P.R. Code) or a corporation or partnership organized under the laws of the Commonwealth will be subject to income tax under the P.R. Code.

Gain realized from the sale, exchange or redemption of the Bonds by an individual that is a citizen of the United States and not a resident of Puerto Rico during the taxable year in which such gain is realized will not be subject to income tax under the P.R. Code, provided such gain does not constitute income from sources within Puerto Rico.

Gain realized from the sale, exchange or redemption of the Bonds by an individual that is an alien and not a resident of the Commonwealth or by a foreign corporation or partnership will not be subject to income tax under the P.R. Code, provided such gain does not constitute income from sources within the Commonwealth and is not effectively connected with the conduct of a trade or business within the United States.

5. The Bonds will be considered an obligation qualifying for (i) the non-recognition of gain rules of Section 1112(f)(2)(A) of the P.R. Code applicable to certain involuntary conversions and (ii) the exemption from the surtax imposed by Section 1102 of the P.R. Code available in obligations of the Commonwealth and certain other investments.

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

The P.R. Code does not provide rules with respect to the treatment of the excess of the amount due at maturity of a Bond with an initial offering price to the public lower than the amount due at maturity over such initial offering price (the "Discount Amount"). Under the current administrative practice followed by the Department of the Treasury of the Commonwealth, the Discount Amount is treated as interest.

Prospective owners of the Bonds, including but not limited to financial institutions, should be aware that ownership of the Bonds may result in having a portion of their interest and other expenses attributable to interest on the Bonds disallowed as deductions for purposes of computing the regular tax and the alternative minimum tax for Puerto Rico income tax purposes.

From such examination, we are further of the opinion that, based on the provisions of the Code now in force:

1. Interest on the Bonds received by, or "original issue discount" (within the meaning of Sections 1272 and 1273 of the Code) accrued to, a corporation (i) organized under the laws of the Commonwealth and subject to income tax under the Code as a corporation, or (ii) otherwise constituting a foreign corporation that is subject to income tax under the Code as a corporation, is not, in the hands of such corporation, subject to income taxation under the Code provided such interest or "original issue discount" is not effectively connected, or treated as effectively connected, with or attributable to the conduct of a trade or business within the United States by such corporation;

2. Interest on the Bonds received by, or "original issue discount" (within the meaning of Sections 1272 and 1273 of the Code) accrued to, an individual who is a *bona fide* resident of the Commonwealth (within the meaning of Sections 933 and 937(a) of the Code and the regulations issued thereunder) during the entire taxable year in which such interest is received or "original issue discount" is accrued will constitute gross income from sources within the Commonwealth and, therefore, excludable from gross income pursuant to Section 933(1) of the Code, provided such interest and original issue discount are not effectively connected with the conduct of a trade or business within the United States by such individual.

3. Interest on the Bonds and any original issue discount accrued or received thereon is not excludable from the gross income of the recipient thereof for United States federal income tax purposes under Section 103(a) of the Code.

4. Pursuant to Notice 89-40 issued by the United States Internal Revenue Services on March 27, 1989, gain on the sale, exchange or redemption of the Bonds by an individual who is a *bona fide* resident of the Commonwealth (within the meaning of Sections 933 and 937(a) of the Code and the regulations issued thereunder) during the entire taxable year will constitute income from sources within the Commonwealth and, therefore, qualify for the exclusion from gross income provided in Section 933(1) of the Code, provided such Bonds do not constitute inventory in the hands of such individual and at the time that the Bonds were acquired by such individual, such individual was a *bona fide* resident of the Commonwealth (within the meaning of Sections 933 and 937(a) of the Code and the regulations issued thereunder).

5. The transfer of the Bonds by death or gift will not be subject to estate or gift tax under the Code in the case of decedents or donors who, at the time of death or gift, are (i) residents of the Commonwealth and (ii) United States citizens that acquired such citizenship solely by reason of birth or residence in the Commonwealth.

Prospective owners of the Bonds should also be aware that the Code provides special rules for the taxation of shareholders of foreign corporations that qualify as "controlled foreign corporations," "personal holding companies," or "passive foreign investment companies," as such terms are defined by the Code.

Other than as described herein, we have not addressed, and we are not opining upon, the federal or Commonwealth tax consequences to any investor arising from the ownership of, receipt or accrual of interest on, or disposition of the Bonds. We understand that you are relying on the opinion of Squire, Sanders & Dempsey L.L.P., bond counsel, as to the legality of the Bonds and certain other conditions, upon which matters we express no opinion.

Very truly yours,

Quiñones & Sánchez PSC



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MBIA Insurance Corporation
Armonk, New York 10504

Policy No. [NUMBER]

MBIA Insurance Corporation (the "Insurer"), in consideration of the payment of the premium and subject to the terms of this policy, hereby unconditionally and irrevocably guarantees to any owner, as hereinafter defined, of the following described obligations, the full and complete payment required to be made by or on behalf of the Issuer to [PAYING AGENT/TRUSTEE] or its successor (the "Paying Agent") of an amount equal to (i) the principal of (either at the stated maturity or by any advancement of maturity pursuant to a mandatory sinking fund payment) and interest on, the Obligations (as that term is defined below) as such payments shall become due but shall not be so paid (except that in the event of any acceleration of the due date of such principal by reason of mandatory or optional redemption or acceleration resulting from default or otherwise, other than any advancement of maturity pursuant to a mandatory sinking fund payment, the payments guaranteed hereby shall be made in such amounts and at such times as such payments of principal would have been due had there not been any such acceleration, unless the Insurer elects, in its sole discretion, to pay in whole or in part any principal due by reason of such acceleration); and (ii) the reimbursement of any such payment which is subsequently recovered from any owner pursuant to a final judgment by a court of competent jurisdiction that such payment constitutes an avoidable preference to such owner within the meaning of any applicable bankruptcy law. The amounts referred to in clauses (i) and (ii) of the preceding sentence shall be referred to herein collectively as the "Insured Amounts." "Obligations" shall mean:

[PAR]
[LEGAL NAME OF ISSUE]

Upon receipt of telephonic or telegraphic notice, such notice subsequently confirmed in writing by registered or certified mail, or upon receipt of written notice by registered or certified mail, by the Insurer from the Paying Agent or any owner of an Obligation the payment of an Insured Amount for which is then due, that such required payment has not been made, the Insurer on the due date of such payment or within one business day after receipt of notice of such nonpayment, whichever is later, will make a deposit of funds, in an account with U.S. Bank Trust National Association, in New York, New York, or its successor, sufficient for the payment of any such Insured Amounts which are then due. Upon presentment and surrender of such Obligations or presentment of such other proof of ownership of the Obligations, together with any appropriate instruments of assignment to evidence the assignment of the Insured Amounts due on the Obligations as are paid by the Insurer, and appropriate instruments to effect the appointment of the Insurer as agent for such owners of the Obligations in any legal proceeding related to payment of Insured Amounts on the Obligations, such instruments being in a form satisfactory to U.S. Bank Trust National Association, U.S. Bank Trust National Association shall disburse to such owners, or the Paying Agent payment of the Insured Amounts due on such Obligations, less any amount held by the Paying Agent for the payment of such Insured Amounts and legally available therefor. This policy does not insure against loss of any prepayment premium which may at any time be payable with respect to any Obligation.

As used herein, the term "owner" shall mean the registered owner of any Obligation as indicated in the books maintained by the Paying Agent, the Issuer, or any designee of the Issuer for such purpose. The term owner shall not include the Issuer or any party whose agreement with the Issuer constitutes the underlying security for the Obligations.

Any service of process on the Insurer may be made to the Insurer at its offices located at 113 King Street, Armonk, New York 10504 and such service of process shall be valid and binding.

This policy is non-cancellable for any reason. The premium on this policy is not refundable for any reason including the payment prior to maturity of the Obligations.

IN WITNESS WHEREOF, the Insurer has caused this policy to be executed in facsimile on its behalf by its duly authorized officers, this [DAY] day of [MONTH, YEAR].

COUNTERSIGNED:

MBIA Insurance Corporation

Resident Licensed Agent

resident

City, State

Attest:

Assistant Secretary

STD-RCS-7
01/05

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Obligor:

Policy Number:

Obligations:

Premium:

Ambac Assurance Corporation (Ambac), a Wisconsin stock insurance corporation, in consideration of the payment of the premium and subject to the terms of this Policy, hereby agrees to pay to The Bank of New York, as trustee, or its successor (the "Insurance Trustee"), for the benefit of the Holders, that portion of the principal of and interest on the above-described obligations (the "Obligations") which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Obligor.

Ambac will make such payments to the Insurance Trustee within one (1) business day following written notification to Ambac of Nonpayment. Upon a Holder's presentation and surrender to the Insurance Trustee of such unpaid Obligations or related coupons, uncanceled and in bearer form and free of any adverse claim, the Insurance Trustee will disburse to the Holder the amount of principal and interest which is then Due for Payment but is unpaid. Upon such disbursement, Ambac shall become the owner of the surrendered Obligations and/or coupons and shall be fully subrogated to all of the Holder's rights to payment thereon.

In cases where the Obligations are issued in registered form, the Insurance Trustee shall disburse principal to a Holder only upon presentation and surrender to the Insurance Trustee of the unpaid Obligation, uncanceled and free of any adverse claim, together with an instrument of assignment, in form satisfactory to Ambac and the Insurance Trustee duly executed by the Holder or such Holder's duly authorized representative, so as to permit ownership of such Obligation to be registered in the name of Ambac or its nominee. The Insurance Trustee shall disburse interest to a Holder of a registered Obligation only upon presentation to the Insurance Trustee of proof that the claimant is the person entitled to the payment of interest on the Obligation and delivery to the Insurance Trustee of an instrument of assignment, in form satisfactory to Ambac and the Insurance Trustee, duly executed by the Holder or such Holder's duly authorized representative, transferring to Ambac all rights under such Obligation to receive the interest in respect of which the insurance disbursement was made. Ambac shall be subrogated to all of the Holders' rights to payment on registered Obligations to the extent of any insurance disbursements so made.

In the event that a trustee or paying agent for the Obligations has notice that any payment of principal of or interest on an Obligation which has become Due for Payment and which is made to a Holder by or on behalf of the Obligor has been deemed a preferential transfer and theretofore recovered from the Holder pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court of competent jurisdiction, such Holder will be entitled to payment from Ambac to the extent of such recovery if sufficient funds are not otherwise available.

As used herein, the term "Holder" means any person other than (i) the Obligor or (ii) any person whose obligations constitute the underlying security or source of payment for the Obligations who, at the time of Nonpayment, is the owner of an Obligation or of a coupon relating to an Obligation. As used herein, "Due for Payment", when referring to the principal of Obligations, is when the scheduled maturity date or mandatory redemption date for the application of a required sinking fund installment has been reached and does not refer to any earlier date on which payment is due by reason of call for redemption (other than by application of required sinking fund installments), acceleration or other advancement of maturity; and, when referring to interest on the Obligations, is when the scheduled date for payment of interest has been reached. As used herein, "Nonpayment" means the failure of the Obligor to have provided sufficient funds to the trustee or paying agent for payment in full of all principal of and interest on the Obligations which are Due for Payment.

This Policy is noncancelable. The premium on this Policy is not refundable for any reason, including payment of the Obligations prior to maturity. This Policy does not insure against loss of any prepayment or other acceleration payment which at any time may become due in respect of any Obligation, other than at the sole option of Ambac, nor against any risk other than Nonpayment.

In witness whereof, Ambac has caused this Policy to be affixed with a facsimile of its corporate seal and to be signed by its duly authorized officers in facsimile to become effective as its original seal and signatures and binding upon Ambac by virtue of the countersignature of its duly authorized representative.



President



Secretary

Effective Date:

Authorized Representative

THE BANK OF NEW YORK acknowledges that it has agreed to perform the duties of Insurance Trustee under this Policy.



Form No.: 2B-0012 (1/01)

Authorized Officer of Insurance Trustee

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