

NEW ISSUE - BOOK-ENTRY ONLY

\$1,095,845,000
Puerto Rico Public Finance Corporation
2001 Series E Bonds
(Commonwealth Appropriation Bonds)

Puerto Rico Public Finance Corporation (the "Corporation") is issuing its 2001 Series E Bonds (the "2001 Series E Bonds") together with the Corporation's 2001 Series C Bonds and 2001 Series D Bonds in the principal amount of \$771,274,288.85 and \$40,750,000, respectively (collectively with the 2001 Series E Bonds, the "Series 2001 Bonds"), for the purpose of funding the purchase of certain promissory notes (the "Series 2001 Notes") issued in connection with the restructuring of certain outstanding loans made by Government Development Bank for Puerto Rico ("Government Development Bank") to certain departments, agencies, instrumentalities and public corporations of the Commonwealth of Puerto Rico (the "Commonwealth" or "Puerto Rico"). The 2001 Series C Bonds and the 2001 Series D Bonds are being offered in separate Official Statements solely in the Commonwealth and are expected to be delivered on or about December 27, 2001.

The Series 2001 Bonds are limited obligations of the Corporation payable solely from payments of principal of and interest on the Series 2001 Notes and any additional promissory notes (such additional notes, together with the Series 2001 Notes, the "Notes") purchased by the Corporation pursuant to the Act (as defined below). The Notes are payable solely from budgetary appropriations to be made pursuant to Act Number 164 of the Legislature of Puerto Rico, approved December 17, 2001 (the "Act"). The Act requires the Office of Management and Budget to include in the operating budget of the Commonwealth submitted annually to the Legislature of the Commonwealth an amount not to exceed \$225 million to be used to pay the principal of and interest on the Notes and any loans covered by the Act which are held by Government Development Bank, as they become due and payable. If the budgetary appropriations provided for under the Act are made on a timely basis each year and in the required amounts, payments required to be made under the Notes will at all times be sufficient to pay the principal of and interest on the Series 2001 Bonds as they become due and payable. The Legislature of Puerto Rico is not legally bound to appropriate funds for such payments.

The 2001 Series E Bonds will have the following characteristics:

- Interest on the 2001 Series E Bonds will be payable semiannually on the first day of August and February, commencing on August 1, 2002. Interest will accrue from the date of issuance of the 2001 Series E Bonds.
- The maturity schedules, interest rates and prices of the 2001 Series E Bonds are presented on the inside cover page.
- The 2001 Series E Bonds are subject to redemption as described in this Official Statement.
- In the opinion of Bond Counsel, under existing law and assuming compliance with the tax covenants described herein, interest on the 2001 Series E Bonds is excluded from gross income for Federal income tax purposes under Section 103 of the Internal Revenue Code of 1986, as amended. Additionally, under existing law, interest on the 2001 Series E Bonds will be exempt from state, Commonwealth and local income taxation. However, see "Tax Matters" herein for a description of alternative minimum tax consequences with respect to interest on the 2001 Series E Bonds and other tax considerations.

The 2001 Series E Bonds are expected to be delivered on or about January 16, 2002.

The 2001 Series E Bonds will not constitute an obligation of the Commonwealth or any of its political subdivisions or public instrumentalities (other than the Corporation), and neither the Commonwealth nor any of its political subdivisions or public instrumentalities (other than the Corporation) will be liable thereon. The Corporation has no taxing power.

MORGAN STANLEY

ABN AMRO FINANCIAL SERVICES, INC.

BEAR, STEARNS & CO. INC.

LEHMAN BROTHERS

GOLDMAN, SACHS & CO.

MERRILL LYNCH & CO.

SALOMON SMITH BARNEY

BANC OF AMERICA SECURITIES LLC

FIRST UNION NATIONAL BANK

UBS PAINEWEBBER INC.

December 19, 2001

\$1,095,845,000
Puerto Rico Public Finance Corporation
2001 Series E Bonds
(Commonwealth Appropriation Bonds)

\$115,110,000	5.70%	Term Bonds due August 1, 2025	— Yield 5.74%
\$174,780,000	6%	Term Bonds due August 1, 2026	— Yield 5.52%
\$50,000,000	5½%	Term Bonds due August 1, 2027*	— Yield 5.16%
\$537,345,000	5½%	Term Bonds due August 1, 2029	— Yield 5.72%
\$218,610,000	5¾%	Term Bonds due August 1, 2030	— Yield 5.80%

*Insured by Ambac Assurance Corporation.

No dealer, broker, sales representative or other person has been authorized by the Corporation 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 Corporation 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 2001 Series E Bonds by any person in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale. The delivery of this Official Statement at any time does not imply that the information contained herein is correct as of any time subsequent to its date. The information set forth herein has been obtained from the Corporation, the Commonwealth and other official sources that are believed to be reliable. The information and expressions of opinion herein are subject to change without notice, and neither the delivery of this Official Statement nor any sale made hereunder shall, under any circumstances, create any implication that there has been no change in the affairs of the Corporation or the Commonwealth since the date hereof. The Underwriters have provided the following three sentences for inclusion in this Official Statement. The Underwriters have reviewed the information in this Official Statement in accordance with, and as part of, their respective responsibilities to investors under the federal securities laws as applied to the facts and circumstances of this transaction, but the Underwriters do not guarantee the accuracy or completeness of such information.

IN CONNECTION WITH THIS OFFERING, THE UNDERWRITERS MAY EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICES OF THE 2001 SERIES E BONDS OFFERED HEREBY AT LEVELS ABOVE THOSE WHICH MIGHT OTHERWISE PREVAIL IN THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

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\$1,095,845,000
Puerto Rico Public Finance Corporation
2001 Series E Bonds
(Commonwealth Appropriation Bonds)

INTRODUCTORY STATEMENT AND PLAN OF FINANCE

This Official Statement of Puerto Rico Public Finance Corporation (the “Corporation”), a subsidiary of Government Development Bank for Puerto Rico (“Government Development Bank”), provides certain information in connection with the sale of Puerto Rico Public Finance Corporation 2001 Series E Bonds (the “2001 Series E Bonds”).

This Official Statement incorporates by reference (i) the Comprehensive Annual Financial Report of the Commonwealth of Puerto Rico (the “Commonwealth” or “Puerto Rico”) for the Fiscal Year ended June 30, 2000, prepared by the Department of the Treasury of Puerto Rico (the “Commonwealth’s Annual Financial Report”), which report includes the general purpose financial statements of the Commonwealth as of and for the Fiscal Year ended June 30, 2000, which have been audited by Deloitte & Touche LLP, independent auditors, as stated in their report accompanying the financial statements; and (ii) the Commonwealth’s Financial Information and Operating Data Report dated September 25, 2001 (the “Commonwealth Report”). The Commonwealth’s Annual Financial Report has been filed by the Commonwealth with each nationally recognized municipal securities information repository (“NRMSIR”). The Commonwealth Report is incorporated by reference from the Official Statement of the Commonwealth, dated October 11, 2001, relating to the issuance by the Commonwealth of its \$455,000,000 Public Improvement Bonds of 2002, Series A, and its \$837,960,000 Public Improvement Refunding Bonds, Series 2002 A, which has been filed by the Commonwealth with each NRMSIR and with the Municipal Securities Rulemaking Board (the “MSRB”). Any appendix of an official statement of the Commonwealth or of any instrumentality of the Commonwealth containing the Commonwealth’s Annual Financial Report or the Commonwealth Report filed with each NRMSIR and the MSRB or any other document containing the Commonwealth’s Annual Financial Report or the Commonwealth Report filed with each NRMSIR after the date hereof and prior to the termination of the offering of the 2001 Series E Bonds shall be deemed to be incorporated by reference into this Official Statement and to be part of this Official Statement from the date of filing of such document. Any statement contained in any of the above described documents incorporated by reference shall be deemed to be modified or superseded for purposes of this Official Statement to the extent that a statement contained herein or in any subsequently filed document modifies or supersedes such statement. Any statement contained herein shall also be deemed to be modified or superseded to the extent that a statement contained in any subsequently filed document modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Official Statement.

For information on how to obtain the Commonwealth’s Annual Financial Report and the Commonwealth’s Report, see “Miscellaneous.”

The Commonwealth expects to complete the preparation of its Comprehensive Annual Financial Report for the Fiscal Year ended June 30, 2001, which will include the Commonwealth’s general purpose financial statements as of and for the Fiscal Year ended June 30, 2001, together with the report thereon of the independent auditors, during the first calendar quarter of 2002. Upon completion thereof, the Commonwealth will file such Comprehensive Annual Financial Report with each NRMSIR and will make such report available to any person to whom this Official Statement is delivered upon request therefor in the manner specified below under “Miscellaneous.”

The 2001 Series E Bonds are being issued under a trust agreement to be dated the date of issuance of the Corporation’s 2001 Series C Bonds and 2001 Series D Bonds (the “Trust Agreement”), between the Corporation and The Bank of New York, as trustee (the “Trustee”).

Prior to the issuance of its 2001 Series E Bonds, the Corporation will issue under the Trust Agreement its 2001 Series C Bonds and 2001 Series D Bonds in the principal amount of \$771,274,288.85 and \$40,750,000, respectively. The 2001 Series C Bonds and 2001 Series D Bonds are expected to be delivered on or about December 27, 2001. The 2001 Series C Bonds, 2001 Series D Bonds and 2001 Series E Bonds (collectively, the “Series 2001 Bonds”) are being issued for the purpose of providing the Corporation with the necessary funds to purchase from Government Development Bank several promissory notes (the “Series 2001 Notes”) issued in connection with the restructuring and

refinancing of certain loans made by Government Development Bank to certain departments, agencies, instrumentalities and public corporations of the Commonwealth (the “Authorized Debtors”) pursuant to the terms of Act Number 164 of the Legislature of Puerto Rico, approved December 17, 2001 (the “Act”). All loans made by Government Development Bank to Authorized Debtors which are covered by the Act are referred to herein as the “Loans.” See “Source of Payment and Security for the Bonds - The Act, the Notes and the Loans.” The 2001 Series C Bonds and 2001 Series D Bonds are being offered in separate Official Statements solely in the Commonwealth.

The Series 2001 Notes will evidence the indebtedness of those Authorized Debtors that, pursuant to the Act, will have restructured and refinanced their Loans with Government Development Bank as of the dates of delivery of the Series 2001 Bonds. Those Loans that are not restructured and refinanced with the Series 2001 Notes will continue to be held by Government Development Bank until additional bonds are issued by the Corporation under the Trust Agreement to fund the purchase of notes issued in connection with the restructuring of such Loans. As of November 30, 2001, the aggregate amount of principal and interest due on all Loans, plus amounts committed thereunder not yet disbursed, was approximately \$2.5 billion. The approved budget for Fiscal Year 2001-02 included an appropriation in respect of the Loans in the amount of approximately \$218 million. Government Development Bank applied this appropriation on November 30, 2001 to the payment of principal and interest on the Loans, thereby reducing the aggregate principal due on all Loans, plus amounts committed thereunder not yet disbursed, to approximately \$2.4 billion. Of this amount, approximately \$1.85 billion principal amount, which includes approximately \$90 million of loan commitments not yet disbursed, is being refinanced with proceeds of the Series 2001 Bonds and the balance of approximately \$557 million will continue to be held by Government Development Bank.

The Series 2001 Bonds and any additional bonds issued in the future under the Trust Agreement are herein collectively referred to as the “Bonds.” Additional Bonds may be issued under the Trust Agreement only to (i) fund the purchase of additional notes covered by the Act representing additional Loans that have been restructured and refinanced (such notes, together with the Series 2001 Notes, being referred to collectively as the “Notes”), (ii) refund any Bonds Outstanding under the Trust Agreement, (iii) fund a Reserve Account, if applicable, (iv) pay capitalized interest with respect to any such additional Bonds, and (v) pay the cost of issuance of such additional Bonds. See “Source of Payment and Security for the Bonds — Limitation on Additional Bonds.”

The Series 2001 Bonds are limited obligations of the Corporation payable solely from Pledged Revenues (as defined in the Trust Agreement), consisting of payments of principal of and interest on the Notes and other amounts deposited to the credit of the Puerto Rico Public Finance Corporation Act 164 Sinking Fund (the “Sinking Fund”) established under the Trust Agreement, including the investment earnings thereon. Payments of principal and interest under the Notes will be made solely from Legislative Appropriations to be made pursuant to the Act. The Act requires the Office of Management and Budget to include in the operating budget of the Commonwealth submitted annually to the Legislature of the Commonwealth the amounts necessary, up to a maximum of \$225 million per Fiscal Year, to pay the principal of and interest on the Notes and the Loans as they become due. If the Legislative Appropriations provided for under the Act are made on a timely basis each year and in the required amounts, payments of principal and interest required to be made under the Series 2001 Notes will at all times be sufficient to pay the principal of and interest on the Series 2001 Bonds as they become due and payable. The Legislature of Puerto Rico is not legally bound to appropriate funds for such payments. See “Source of Payment and Security for the Bonds.”

Payment of the principal of and interest on the 2001 Series E Bonds maturing on August 1, 2027 (the “Ambac Insured Bonds”) when due will be insured by a financial guaranty insurance policy (the “Ambac Financial Guaranty Insurance Policy”) to be issued by Ambac Assurance Corporation (“Ambac”) simultaneously with the delivery of the 2001 Series E Bonds.

This Official Statement, including information incorporated in this Official Statement by reference, contains certain “forward-looking statements” concerning the Commonwealth’s operations and financial condition. These statements are based upon a number of assumptions and estimates which are subject to significant uncertainties, many of which are beyond the control of the Commonwealth. The words “may,” “would,” “could,” “will,” “expect,” “anticipate,” “believe,” “intend,” “plan,” “estimate” and similar expressions are meant to identify these forward-looking statements. Actual results may differ materially from those expressed or implied by these forward-looking statements.

Descriptions of the Corporation, the Commonwealth, the 2001 Series E Bonds, the Trust Agreement and certain other documents are included in this Official Statement. Such descriptions do not purport to be comprehensive or definitive. All references herein to the Trust Agreement and other documents are qualified in their entirety by reference to each such document. References herein to the 2001 Series E Bonds are qualified in their entirety by reference to the form thereof. The resolution of the Corporation authorizing the issuance of the 2001 Series E Bonds (the “Resolution”) and each of the aforesaid documents are available for inspection at the offices of the Corporation, located at Minillas Government Center, De Diego Avenue, San Juan, Puerto Rico 00940.

Capitalized terms not otherwise defined herein are defined in the Trust Agreement. See Appendix I - “Summary of the Trust Agreement.”

USE OF PROCEEDS

The net proceeds of the Series 2001 Bonds (after payment of the costs of issuance hereinafter described) will be used to purchase the Series 2001 Notes at a price equal to the principal amount thereof plus accrued interest. A portion of the proceeds of the Series 2001 Bonds will be applied to the payment of expenses incident to the issuance thereof. The sources and uses of bond proceeds are set forth below.

Sources:

Proceeds of the 2001 Series C Bonds	\$ 771,274,288.85
Proceeds of the 2001 Series D Bonds	40,750,000.00
Proceeds of the 2001 Series E Bonds*	<u>1,091,006,530.00</u>
 Total Sources	 <u>\$1,903,030,818.85</u>

Uses:

Purchase of the Series 2001 Notes (principal and accrued interest)	\$1,851,535,717.45
Capitalized interest on the Series 2001 Bonds	29,025,717.92
Underwriting discount, bond insurance premium, legal, printing and other costs of issuance of the Series 2001 Bonds	<u>22,469,383.48</u>
 Total Uses	 <u>\$1,903,030,818.85</u>

* After deducting \$4,838,470 of net original issue discount.

PUERTO RICO PUBLIC FINANCE CORPORATION

The Corporation is a subsidiary corporation of Government Development Bank created pursuant to Resolution No. 5044 of the Board of Directors of Government Development Bank, as amended (“Resolution No. 5044”), adopted pursuant to the authority granted under Act No. 17 of the Legislature of Puerto Rico, approved September 23, 1948, as amended. The Corporation is exempt from the payment of any Commonwealth taxes on its revenues and properties and constitutes an independent governmental instrumentality of the Commonwealth separate and apart from Government Development Bank. The obligations of the Corporation are not obligations of Government Development Bank. For additional information regarding the Corporation and Government Development Bank, see “Public Corporations - Government Development Bank for Puerto Rico” in the Commonwealth Report.

The Board of Directors of the Corporation consists of the same members of the Board of Directors of Government Development Bank, who are the following:

<u>Member</u>	<u>Occupation</u>	<u>Expiration Date</u>
Juan Agosto Alicea, Chairman	President, Government Development Bank for Puerto Rico	September 22, 2004
Melba Acosta Febo	Director, Office of Management and Budget	September 22, 2002
Ramón Cantero-Frau	Secretary of Economic Development and Commerce	September 22, 2002
Juan A. Flores Galarza	Secretary of the Treasury	September 22, 2002
Samuel H. Jové Fontán	President, BMJ Foods of Puerto Rico, Inc.	September 22, 2003
Fermín Contreras Bordallo	Private investor	September 22, 2003
Carmen Conde Torres	Attorney at law	September 22, 2004

The following individuals are currently officers of the Corporation:

Juan Agosto Alicea, President, is also President of Government Development Bank, a position he assumed in January of 2001. Prior to joining Government Development Bank this year, Mr. Agosto Alicea held various positions in government and in the private sector. From 1985 to 1988, he served as Secretary of the Treasury of Puerto Rico, and was Chairman of the Board of Directors of Government Development Bank. From 1995 to 1996 he was Administrator of the Municipality of San Juan. He worked for many years at two major accounting firms, and was the managing partner of one of these firms. He also worked at the Puerto Rico Industrial Development Company and the Federal Department of Housing and Urban Development. He obtained a bachelor's degree in accounting from the University of Puerto Rico and is licensed as a certified public accountant since 1966. He is a former president of the Puerto Rico College of Certified Public Accountants and the Board of Directors of United Way of Puerto Rico.

José V. Pagán, Executive Vice President, is also Executive Vice President of Government Development Bank, a position he assumed in January of 2001. Prior to joining Government Development Bank this year, Mr. Pagán held various positions in investment banking and accounting firms during a 17 year period. Mr. Pagán also held the position of Executive Vice President of the Government Development Bank during 1992. Mr. Pagán received a bachelor's degree in engineering and applied science from Yale University, and a master's degree in finance from the New York University Graduate School of Business Administration.

Miriam Figueroa, Executive Vice President and General Counsel, is also Executive Vice President and General Counsel of Government Development Bank, a position she assumed in January of 2001. Prior to joining Government Development Bank, Ms. Figueroa worked as an attorney in private practice in New York and Tokyo, and in the United States Congress. Ms. Figueroa received a bachelor's degree from Macalester College, a law degree from the Pontifical Catholic University of Puerto Rico, and a master of law degree from Harvard Law School.

Olga Ortiz, Secretary of the Board of Directors, is also Secretary of the Board of Directors of Government Development Bank.

Pursuant to Resolution No. 5044, the Corporation has the authority, among other things, to issue bonds and other obligations for borrowed money payable out of all or any part of funds received in payment of the principal of and interest on securities of governmental instrumentalities of Puerto Rico purchased by the Corporation or any other funds or assets of the Corporation as provided by the resolution or trust agreement authorizing the issuance of its bonds.

As of November 2, 2001, the Corporation had bonds or notes outstanding in the aggregate principal amount of \$1.9 billion. All such bonds and notes, other than the Bonds, are payable from revenues other than the Pledged Revenues. Except for Bonds which may be issued in the future to refund the Bonds, to purchase additional Notes covered by the Act, to fund a Reserve Account for one or more series of Bonds, to pay capitalized interest with respect to any such additional Bonds or to fund the costs of issuance of Bonds, the Corporation may not issue additional bonds payable from Pledged Revenues. The Corporation may from time to time issue additional bonds and notes, which would

be authorized and issued pursuant to trust indentures or authorizing resolutions separate from and unrelated to the Resolution and the Trust Agreement and would be secured with revenues other than the Pledged Revenues. See Appendix I - “Summary of the Trust Agreement—Additional Bonds—Refunding Bonds.”

THE 2001 SERIES E BONDS

General

The 2001 Series E Bonds are being issued as registered bonds without coupons and 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 2001 Series E Bonds. The 2001 Series E Bonds will be available to purchasers in denominations of \$5,000 and any integral multiple thereof only under the book-entry system maintained by DTC through brokers and dealers who are, or act through, DTC Participants (as defined herein). Purchasers will not receive physical delivery of the 2001 Series E Bonds. So long as any purchaser is the Beneficial Owner (as defined herein) of a 2001 Series E 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 2001 Series E Bonds. See “Book-Entry Only System” below.

The 2001 Series E Bonds are being issued pursuant to the Resolution and the Trust Agreement. The 2001 Series E Bonds will be issued in such aggregate principal amounts and will be stated to mature as set forth on the inside cover page of this Official Statement.

Interest on the 2001 Series E Bonds will accrue from their date of issue at the rates set forth on the inside cover page of this Official Statement, and will be payable semiannually on the first day of August and February, commencing on August 1, 2002.

Interest will be calculated on the basis of a 360-day year of twelve 30-day months.

Optional Redemption

At the option of the Corporation, and upon at least 30 days’ notice, the 2001 Series E Bonds maturing on August 1, 2025 are subject to redemption, from any moneys available for that purpose (other than from moneys set aside with respect to an Amortization Requirement), prior to maturity, in whole or in part, on any date not earlier than February 1, 2010, as directed by the Corporation, at a price equal to the principal amount thereof, without premium, together with accrued interest to the date fixed for redemption.

At the option of the Corporation, and upon at least 30 days’ notice, the 2001 Series E Bonds maturing on August 1, 2029 are subject to redemption, from any moneys available for that purpose (other than from moneys set aside with respect to an Amortization Requirement), prior to maturity, in whole or in part, on any date not earlier than February 1, 2012, as directed by the Corporation, at a price equal to the principal amount thereof, without premium, together with accrued interest to the date fixed for redemption.

At the option of the Corporation, and upon at least 30 days’ notice, the 2001 Series E Bonds maturing on August 1, 2030 are subject to redemption, from any moneys available for that purpose (other than from moneys set aside with respect to an Amortization Requirement), prior to maturity, in whole or in part, on any date not earlier than February 1, 2007, as directed by the Corporation, at a price equal to the principal amount thereof, without premium, together with accrued interest to the date fixed for redemption.

Mandatory Redemption

The 2001 Series E Bonds maturing on August 1, 2029 (the “2029 Term Bonds”) are subject to redemption upon at least 30 days’ notice, to the extent of their Amortization Requirement set forth below, commencing on August 1, 2027, and on August 1 of each year thereafter, at a redemption price of par plus accrued interest to the dates fixed for redemption.

Amortization Requirement for the 2029 Term Bonds means the principal amount fixed for the retirement by purchase or redemption of the 2029 Term Bonds in any Bond Year (the period from August 1 to July 31 of the following year), as provided for in the Trust Agreement. The Amortization Requirement shall be the respective principal amount for each Bond Year fixed in the Resolution (as set forth below) and the aggregate amount of the Amortization Requirement for the 2029 Term Bonds shall be equal to the aggregate principal amount of such 2029 Term Bonds.

<u>August 1,</u>	<u>Amortization Requirement</u>
2027	\$135,115,000
2028	195,585,000
2029	206,645,000*
Average life (in years)	26.675

*Maturity.

If at the close of any Bond Year the total principal amount of the 2029 Term Bonds retired by purchase or redemption, or called for redemption under the provisions of the Trust Agreement during such Bond Year, shall be in excess of the amount of the Amortization Requirement for such Bond Year, then the amount of the Amortization Requirement shall be reduced for such subsequent Bond Years in such amounts aggregating the amount of such excess as shall be determined by the President of the Corporation in an order filed with the Trustee on or before the 15th day of August following the close of such Bond Year.

Notice and Effect of Redemption

Any redemption of the 2001 Series E Bonds, either in whole or in part, shall be made upon at least 30 days' notice by mail to DTC or, if the book-entry only system as described below has been discontinued, by first class mail, postage prepaid, to all registered owners in the manner and under the terms and conditions provided in the Trust Agreement. On the date designated for redemption, notice having been given as provided in the Trust Agreement and moneys for payment of the principal of and redemption premium, if any, and the interest on the 2001 Series E Bonds or portions thereof so called for redemption being held by the Trustee, interest on the 2001 Series E Bonds or portions thereof so called for redemption shall cease to accrue. Subject to certain provisions of the Trust Agreement, 2001 Series E Bonds and portions thereof which have been duly called for redemption under the provisions of the Trust Agreement, or with respect to which irrevocable instructions to call for redemption or to pay at maturity have been given, and for which sufficient moneys or investments permitted by the Trust Agreement are held in a separate account for the payment of the principal of and redemption premium, if any, and the interest on the 2001 Series E Bonds or portions thereof to be paid or redeemed, such 2001 Series E Bonds shall not be deemed to be Outstanding under the Trust Agreement, and the registered owners thereof shall have no rights with respect thereto, except to receive payment of the principal thereof and redemption premium, if any, and the interest thereon from such separate account.

Each notice of redemption shall contain, among other things, the CUSIP identification number of the 2001 Series E Bonds (or portions thereof) being called for redemption, the redemption date and price and the address at which such 2001 Series E Bonds are to be surrendered for payment of the redemption price. Any defect in such notice or the failure to mail any such notice to DTC will not affect the validity of the proceedings for the redemption of any other 2001 Series E Bond.

If less than all the 2001 Series E Bonds of any maturity are called for redemption, the particular 2001 Series E Bonds so called for redemption shall be selected by the Trustee by such method as it deems fair and appropriate, except that so long as the book-entry only system remains in effect, in the event of any such partial redemption, DTC shall reduce the credit balances of the applicable DTC Participants with respect to the 2001 Series E Bonds and such DTC Participants shall in turn select those Beneficial Owners (as defined herein) whose ownership interests are to be

extinguished by such partial redemption, each by such method as DTC or such DTC Participant, as the case may be, in its sole discretion, deems fair and appropriate.

Book-Entry Only System

The following information concerning DTC and DTC's book-entry system has been obtained from DTC. The Corporation, the Trustee and the Underwriters assume no responsibility for the accuracy thereof.

DTC will act as securities depository for the 2001 Series E Bonds. The 2001 Series E Bonds will be issued as fully registered bonds registered in the name of Cede & Co. (DTC's partnership nominee) or such other nominee as may be requested by an authorized representative of DTC. One fully registered bond will be issued for each maturity of the 2001 Series E Bonds, each in the aggregate principal amount of such maturity, and will be deposited with DTC.

DTC is a limited-purpose trust company organized under the New York Banking Law, a "banking organization" within the meaning of the New York Banking Law, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the New York Uniform Commercial Code, and a "clearing agency" registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds securities that its participants (the "Direct Participants") deposit with DTC. DTC also facilitates the settlement among Direct Participants of securities transactions, such as transfers and pledges, in deposited securities through electronic computerized book-entry changes in Direct Participants' accounts, thereby eliminating the need for physical movement of securities certificates. Direct Participants include securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is owned by a number of its Direct Participants and by the New York Stock Exchange, Inc., the American Stock Exchange LLC and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others, such as securities brokers and dealers, banks and trust companies, that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (the "Indirect Participants" and, together with the Direct Participants, the "Participants"). The rules applicable to DTC and its Participants are on file with the Securities and Exchange Commission.

Purchases of the 2001 Series E Bonds under the DTC system must be made by or through Direct Participants, which will receive a credit for the 2001 Series E Bonds in DTC's records. The ownership interest of each actual purchaser of a 2001 Series E Bond (a "Beneficial Owner") will in turn be recorded in the Direct or Indirect Participants' records. Beneficial Owners will not receive written confirmations from DTC of their purchases, but Beneficial Owners are expected to receive written confirmation providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the 2001 Series E Bonds will be accomplished by entries made in the books of Participants acting on behalf of the Beneficial Owners. Beneficial Owners will not receive definitive bonds representing their ownership interests in the 2001 Series E Bonds except in the event that use of the book-entry system for the 2001 Series E Bonds is discontinued.

To facilitate subsequent transfers, all 2001 Series E Bonds deposited by Direct Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co. or such other nominee as may be requested by an authorized representative of DTC. The deposit of 2001 Series E Bonds with DTC and their registration in the name of Cede & Co. effect no change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the 2001 Series E Bonds; DTC's records reflect only the identity of the Direct Participants to whose accounts such 2001 Series E Bonds are credited, which may or may not be the Beneficial Owners. The Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Redemption notices will be sent to DTC. If less than all of the 2001 Series E 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 the 2001 Series E Bonds to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the 2001 Series E Bonds. Under its usual procedures, DTC mails an Omnibus Proxy to the Corporation 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 2001 Series E Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal, redemption premium, if any, and interest payments on the 2001 Series E Bonds will be made to DTC or such other nominee as may be requested by an authorized representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detailed information from the Corporation or the Trustee on the payable date in accordance with their respective holdings shown on DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name," and will be the responsibility of such Participant and not of DTC, the Corporation or the Trustee, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of the principal, redemption premium, if any, and interest to DTC (or such nominee as may be requested by an authorized representative of DTC) is the responsibility of the Corporation and the Trustee. Disbursement of such payments to Direct Participants shall be the responsibility of DTC, and disbursement of such payments to the Beneficial Owners shall be the responsibility of Direct and Indirect Participants.

Each person for which a DTC Participant acquires an interest in the 2001 Series E Bonds, as nominee, may desire to make arrangements with such DTC Participant to receive a credit balance in the records of such DTC Participant, to have all communications to DTC which may affect such persons forwarded in writing by such DTC Participant, and to have notification made of all interest payments.

The Corporation, the Trustee, and the Underwriters will have no responsibility or obligation to DTC Participants, Beneficial Owners or other nominees of such Beneficial Owners for: (i) sending transaction statements; (ii) maintaining, supervising or reviewing the accuracy of any records maintained by DTC or any DTC Participant or other nominees of such Beneficial Owners; (iii) payment or the timeliness of payment by DTC to any DTC Participant, or by any DTC Participant or other nominees of Beneficial Owners to any Beneficial Owner, of any amount due with respect to the principal of or interest on 2001 Series E Bonds; (iv) delivery or timely delivery by DTC to any DTC Participant, or by any DTC Participant or other nominees of Beneficial Owners to any Beneficial Owners, of any notice or other communication which is required or permitted under the terms of the Trust Agreement to be given to the registered owners of 2001 Series E Bonds; or (v) any consent given or any action taken by DTC or its nominee as the registered owner of the 2001 Series E Bonds.

Discontinuance of the Book-Entry Only System

DTC may discontinue providing its services as securities depository with respect to the 2001 Series E Bonds at any time by giving reasonable notice to the Corporation or the Trustee. Under such circumstances, in the event that a successor securities depository is not obtained, definitive 2001 Series E Bonds will be printed and delivered.

The Corporation, in its sole discretion and without the consent of any other person, may terminate the services of DTC as securities depository with respect to the 2001 Series E Bonds. In such event, definitive 2001 Series E Bonds will be printed and delivered.

In the event that such book-entry only system is discontinued or the Corporation terminates the services of DTC as securities depository, the following provisions will apply: (i) payments of the principal of and the interest on the 2001 Series E Bonds will be made in lawful money of the United States of America; (ii) payments of principal will be made at the principal corporate trust office of the Trustee in New York, New York; (iii) interest on the 2001 Series E Bonds will be paid by check mailed to the respective addresses of the registered owners thereof as of the fifteenth day of the month immediately preceding the interest payment date as shown on the registration books of the Corporation maintained by the Trustee; (iv) the 2001 Series E Bonds will be issued only as registered bonds without coupons in denominations of \$5,000 or any multiple thereof; and (v) the transfer of the 2001 Series E Bonds will be registrable and the 2001 Series E Bonds may be exchanged at the principal corporate trust office of the Trustee 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.

Bond Insurance

The principal of and interest on the Ambac Insured Bonds will be insured by the Ambac Financial Guaranty Insurance Policy. Ambac shall be deemed to be the owner of the Ambac Insured Bonds in lieu of the registered owners thereof for purposes of (1) directing remedies and making requests to the Trustee to take remedial actions under the Trust Agreement, and waiving or directing the Trustee to waive any defaults, and (2) so long as Ambac shall not then be in default on its obligations under the policy, the giving of consents to the execution of any supplemental agreement to the Trust Agreement.

The following information has been furnished by Ambac for use in this Official Statement. No representation is made by the Corporation as to the accuracy or completeness of the information. Reference is made to Appendix IV for a specimen of the Ambac Financial Guaranty Insurance Policy.

Payment Pursuant to the Ambac Financial Guaranty Insurance Policy. Ambac has made a commitment to issue the Ambac Financial Guaranty Insurance Policy relating to the Ambac Insured Bonds effective as of the date of issuance of the Ambac Insured Bonds. Under the terms of the Ambac Financial Guaranty Insurance Policy, Ambac 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 which shall become Due for Payment but shall be unpaid by reason of Nonpayment by the Obligor (as such terms are defined in the Ambac Financial Guaranty Insurance Policy). Ambac will make such payments to the Insurance Trustee on the later of the date on which such principal and interest becomes Due for Payment or within one business day following the date on which Ambac shall have received notice of Nonpayment from the Trustee. The insurance will extend for the term of the Ambac Insured Bonds and, once issued, cannot be canceled by Ambac.

The Ambac Financial Guaranty Insurance Policy will insure payment only on stated maturity dates and on mandatory sinking fund installments 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 will remain obligated to pay 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.

In the event the Trustee has notice that any payment of principal of or interest on an Ambac Insured Bond 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 its registered owner pursuant to the United States Bankruptcy Code in accordance with a final, nonappealable order of a court of competent jurisdiction, such registered owner will be entitled to payment from Ambac to the extent of such recovery if sufficient funds are not otherwise available.

The Ambac Financial Guaranty Insurance Policy does not insure any risk other than Nonpayment, as defined in the Policy. Specifically, the Ambac 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.
- (3) nonpayment of principal or interest caused by the insolvency or negligence of the Trustee.

If it becomes necessary to call upon the Ambac Financial Guaranty Insurance Policy, payment of principal requires surrender of 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 to the extent of the payment under the Ambac Financial Guaranty Insurance Policy. Payment of interest pursuant to the Ambac 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.

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

Ambac Assurance Corporation. Ambac is a Wisconsin-domiciled stock insurance corporation regulated by the Office of the Commissioner of Insurance of the State of Wisconsin and licensed to do business in 50 states, the District of Columbia, the Territory of Guam and the Commonwealth, with admitted assets of approximately \$4,988,000,000 (unaudited) and statutory capital of approximately \$2,963,000,000 (unaudited) as of September 30, 2001. Statutory capital consists of Ambac's policyholders' surplus and statutory contingency reserve. Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc. ("Standard & Poor's"), Moody's Investors Service, Inc. ("Moody's") and Fitch, Inc. have each assigned a triple-A financial strength rating to Ambac.

Ambac has obtained a ruling from the Internal Revenue Service to the effect that the insuring of an obligation by Ambac 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 under policy provisions substantially identical to those contained in its financial guaranty insurance policy shall be treated for federal income tax purposes in the same manner as if such payments were made by the Corporation.

Ambac 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, the Official Statement other than the information supplied by Ambac and presented under "Bond Insurance."

Available Information. The parent company of Ambac, Ambac Financial Group, Inc. ("Ambac Financial"), is subject to the informational requirements of the Securities Exchange Act of 1934, as amended, and in accordance therewith files reports, proxy statements and other information with the Securities and Exchange Commission (the "SEC"). Such reports, proxy statements and other information may be inspected and copied at the public reference facilities maintained by the SEC at 450 Fifth Street, N.W., Washington, D.C. 20549 and Northwestern Atrium Center, 500 West Madison Street, Suite 1400, Chicago, Illinois 60661. Copies of such material can be obtained from the public reference section of the SEC at 450 Fifth Street, N.W., Washington, D.C. 20549 at prescribed rates. In addition, the aforementioned material may also be inspected at the offices of the New York Stock Exchange, Inc. (the "NYSE") at 20 Broad Street, New York, New York 10005. Ambac Financial's Common Stock is listed on the NYSE.

Copies of Ambac's financial statements prepared in accordance with statutory accounting standards are available from Ambac. The address of Ambac's administrative offices and its telephone number are One State Street Plaza, 17th Floor, New York, New York 10004 and (212) 668-0340.

Incorporation of Certain Documents by Reference. The following documents filed by Ambac Financial with the SEC (File No. 1-10777) are incorporated by reference in this Official Statement:

- (1) Ambac Financial's Current Report on Form 8-K dated January 24, 2001 and filed on January 24, 2001;
- (2) Ambac Financial's Current Report on Form 8-K dated March 19, 2001 and filed on March 19, 2001;
- (3) Ambac Financial's Annual Report on Form 10-K for the fiscal year ended December 31, 2000 and filed on March 28, 2001;
- (4) Ambac Financial's Quarterly Report on Form 10-Q for the fiscal quarterly period ended March 31, 2001 and filed on May 15, 2001;
- (5) Ambac Financial's Current Report on Form 8-K dated July 18, 2001 and filed on July 23, 2001;
- (6) Ambac Financial's Quarterly Report on Form 10-Q for the fiscal quarterly period ended June 30, 2001 and filed on August 10, 2001;

- (7) Ambac Financial's Current Report on Form 8-K dated and filed on September 17, 2001;
- (8) Ambac Financial's Current Report on Form 8-K dated and filed on September 19, 2001;
- (9) Ambac Financial's Current Report on Form 8-K dated and filed on October 22, 2001; and
- (10) Ambac Financial's Quarterly Report on Form 10-Q for the fiscal quarterly period ended September 30, 2001 and filed on November 14, 2001.

All documents subsequently filed by Ambac Financial 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".

SOURCE OF PAYMENT AND SECURITY FOR THE BONDS

General

Under the Trust Agreement, the Corporation will pledge the Notes to the Trustee and create a first lien on the Pledged Revenues (as defined in the Trust Agreement) for the benefit of the holders of the Bonds.

The Bonds are payable solely from and are secured by the Pledged Revenues, consisting of payments of principal of and interest on the Notes required to be deposited to the credit of the Bond Service Account and Redemption Account established under the Trust Agreement, any other moneys deposited to the credit of those Accounts, including investment earnings thereon, and the moneys on deposit in the Surplus Account established under the Trust Agreement, including investment earnings thereon. See Appendix I - "Summary of the Trust Agreement—Sinking Fund and Accounts."

The Bonds do not constitute an obligation of the Commonwealth or any of its political subdivisions or public instrumentalities (other than the Corporation), and neither the Commonwealth nor any of its political subdivisions or public instrumentalities (other than the Corporation) shall be liable thereon. The Corporation has no taxing power.

The Act, the Notes and the Loans

As of June 30, 2001, the aggregate amount of principal and interest due on all Loans to Authorized Debtors held by Government Development Bank totaled approximately \$2.4 billion. These Loans had been made by Government Development Bank for the purpose of funding, among other things, capital expenditures and operating deficits of the Authorized Debtors. Prior to the enactment of the Act, the Loans did not have an established source of repayment. The Legislature of Puerto Rico approved the Act in order to provide a source of repayment for these Loans and enable Government Development Bank to sell the Loans in the capital markets through bond issues of the Corporation.

The Act requires Authorized Debtors to negotiate and execute with Government Development Bank the agreements necessary to recognize, formalize, restructure and/or refinance the Loans and to finance all expenses incurred in connection therewith. The Act provides that the Commonwealth, through budgetary appropriations during the next thirty Fiscal Years, commencing with Fiscal Year 2001-2002, will pay the principal of and interest on the Loans as the same may be restructured and/or refinanced under the Act. The Act provides, however, that such budgetary appropriations shall not exceed \$225 million per Fiscal Year.

On each date of delivery of the Series 2001 Bonds, Government Development Bank and the Corporation will enter into Debt Restructuring and Assignment Agreements with certain Authorized Debtors whereby the Authorized Debtors will agree to restructure and refinance all or a portion of their corresponding Loans. Pursuant to such Debt Restructuring and Assignment Agreements, such Authorized Debtors will execute the Series 2001 Notes and the Corporation will issue the Series 2001 Bonds and apply the net proceeds therefrom to purchase the Series 2001 Notes from Government Development Bank, without recourse to Government Development Bank.

The initial aggregate principal amount of the Series 2001 Notes will be equal to the initial aggregate principal amount of the Series 2001 Bonds and the interest payable on such Series 2001 Notes will be the same as the interest payable on the Series 2001 Bonds.

After the sale of the Series 2001 Notes to the Corporation, Government Development Bank will continue to hold certain Loans in the aggregate principal amount of approximately \$557 million. It is expected that such Loans will be restructured in the future and that the Corporation will issue additional Bonds to purchase additional Notes issued by the Authorized Debtors in connection with the restructuring of such Loans. Such additional Notes will be in a principal amount equal to the initial principal amount of the additional Bonds issued to purchase such Notes and will bear interest sufficient to cover the interest on the additional Bonds. After all the Loans have been restructured and sold to the Corporation as contemplated by the Act, the aggregate initial principal amount of the Notes will equal the aggregate initial principal amount of the Bonds and the aggregate interest payable under the Notes will equal the aggregate interest payable under the Bonds. Such additional Bonds issued to purchase additional Notes may be privately placed with and held by Government Development Bank or sold in public offerings.

Under the Debt Restructuring and Assignment Agreements, Government Development Bank has agreed that it will not restructure and refinance any Loan if as a result thereof the annual interest, principal and other payments required to be made by the Authorized Debtors under the Notes and Loans would exceed \$225 million per Fiscal Year.

Under the Notes, the Authorized Debtors are required to make on or before July 15 of each Fiscal Year, commencing July 15, 2002, payments thereunder equal to the sum of the following amounts, without duplication: (i) the interest on, principal of, redemption premium, if any, and Accreted Value of the Bonds which is due and payable in the Bond Year which begins during such Fiscal Year (whether at maturity, in connection with an Amortization Requirement, upon redemption or otherwise) less any amounts available in the Sinking Fund for the payment of such amounts in such Bond Year; (ii) any fees, expenses or other amounts becoming due and payable in such Bond Year to the provider (a "Facility Provider"), if applicable, of a credit facility or a liquidity facility (each a "Facility") under the agreement relating to such Facility or any amounts required to reimburse a Facility Provider for payments made under any such Facility in respect of the Bonds and not theretofore reimbursed; (iii) if applicable, all payments required to be made by the Corporation under any Swap Agreement (as defined in the Trust Agreement) (such payments being called the "Corporation Swap Payments") expected to be due and payable for such Bond Year (to the extent not already included in the portion corresponding to interest on the Bonds); (iv) any fees or reimbursement for expenses payable to the Trustee under the Trust Agreement; (v) if applicable, any amount then due by the Corporation to the Hedge Counterparty (as defined in the Trust Agreement) for breakage cost or other termination payment under the terms of any Swap Agreement; and (vi) any other amount becoming due and payable in such Bond Year in respect of the Bonds or becoming due and payable under the provisions of the Trust Agreement. See Appendix I - "Summary of the Trust Agreement." The aggregate principal and interest installments required to be paid under the Notes will be sufficient to cover the aggregate principal amount of and the aggregate annual amount of interest payable on the Bonds, together with fees, expenses and other amounts payable by the Corporation or the Trustee with respect to the Bonds.

The Notes are payable solely from Legislative Appropriations to be made pursuant to the Act. The Act provides that (i) the Commonwealth shall honor, by means of budgetary appropriations, the payment of principal of and interest on the Notes and Loans, (ii) the Office of Management and Budget shall include in the operating budget of the Commonwealth submitted annually to the Legislature of Puerto Rico in each of the succeeding thirty Fiscal Years, commencing with Fiscal Year 2001-02, the amounts necessary to pay the principal of and interest on the Notes and Loans, up to a maximum annual amount of \$225 million per Fiscal Year, and (iii) the budgetary appropriations made thereunder may be used only for the payment of principal of and interest on the Notes and Loans and related costs, and are not subject to third party claims. The approved budget for Fiscal Year 2001-02 included an appropriation in respect of the Loans in the amount of approximately \$218 million. This amount was applied by Government Development Bank to pay accrued interest on the Loans and to reduce the outstanding principal balance thereof.

The funds to be provided by the Commonwealth to make the payments required under the Notes and Loans are subject to and conditioned upon the appropriation of such funds by the Legislature of Puerto Rico in the annual budget of the Commonwealth. If all required annual Legislative Appropriations are made in full and all payments of principal and interest due under the Notes are timely paid, such payments will be sufficient to pay the principal of and interest on the Bonds as the same become due and payable, together with all amounts payable under the Trust

Agreement. **The failure to make annual Legislative Appropriations in the amounts required would cause a shortfall in the moneys available under the Notes to pay principal and interest due on the Bonds.**

Special Considerations - Bonds are Limited Obligations; Legislature Not Legally Bound to Appropriate; Investment of Funds

The principal of and redemption premium, if any, and interest on the Bonds will be payable solely from the Legislative Appropriations made pursuant to the Act and other sources described above. **The Legislature of Puerto Rico is not legally bound to appropriate sufficient amounts to timely pay the principal of and redemption premium, if any, and interest due on the Bonds. There is no assurance that sufficient funds will be appropriated or otherwise made available to make such payments on the Bonds.** For a discussion of Puerto Rico's budgetary process, see "Budgetary Process and Payment of Commonwealth Obligations" below and the Commonwealth Report, which is incorporated herein by reference.

Bondholders have no legal recourse to require the Legislature of Puerto Rico to appropriate the funds necessary to timely pay the principal of and redemption premium, if any, and interest due on the Bonds.

Neither the Corporation nor the Commonwealth has ever defaulted on the payment of principal of or interest on any of its debt.

Pending their application for the payment of principal of and interest on the Bonds on the dates required, funds on deposit in the Sinking Fund (including funds representing the Legislative Appropriation) shall be invested by the Trustee as required by the Trust Agreement. Pursuant to the Trust Agreement, such funds may be invested, among other investments, in an investment agreement with a financial institution which has a long term debt rating in one of the three highest rating categories by Moody's and Standard & Poor's (without regards to any gradations within such categories). Losses incurred in connection with such investments may result in a shortfall in the moneys available to pay principal and interest due on the Bonds. See Appendix I - "Summary of the Trust Agreement—Investment of Moneys."

Letter of Credit

Under the Commonwealth's Constitution, if the annual budget of capital expenditures and operating expenses of the Commonwealth for a Fiscal Year has not been adopted by June 30 of the preceding Fiscal Year, the budget for such preceding Fiscal Year is automatically renewed for the ensuing Fiscal Year, until a new budget for such succeeding Fiscal Year is approved by the Legislature of Puerto Rico and the Governor. This means that if the debt service on the Notes and the Loans held by Government Development Bank (if at such time not all Loans have been restructured and transferred to the Corporation as Notes in connection with the issuance of additional Bonds) for any Fiscal Year and, therefore, the annual budgetary appropriation for such Fiscal Year is less than the debt service on the Notes and such Loans in the immediately succeeding Fiscal Year, then in the case of a delay in the approval of the budget for such succeeding Fiscal Year, pending approval of the new budget, the budgetary appropriation that would carry over and be available to meet debt service on the Notes and such Loans for such succeeding Fiscal Year would be insufficient to meet the debt service on the Notes and such Loans. See "Budgetary Process and Payment of Commonwealth Obligations" below.

The maximum increase from one Fiscal Year to the next in the aggregate debt service on the Notes and any Loans remaining with Government Development Bank (the "Maximum Difference"), and, thus, the maximum difference in the annual budgetary appropriation under the Act from one Fiscal Year to the next with respect to the payment of debt service on the Notes and such Loans, as estimated by Government Development Bank based on its projected schedule of amortization of principal of such Loans, is approximately \$50,000,000.

To cover the risk that in any year during the term of the Bonds the budget is not adopted prior to June 30 and the budgetary appropriation that automatically carries over from the prior Fiscal Year may be insufficient to cover fully the debt service payments on the Bonds during the ensuing Bond Year, on the date of delivery of the 2001 Series C Bonds and 2001 Series D Bonds, Government Development Bank (in such capacity, the "Letter of Credit Bank"), will issue an irrevocable, transferable standby letter of credit (the "Letter of Credit") in favor of the Trustee solely for the benefit of the owners of the Bonds. The Letter of Credit will be in the stated amount of \$50,000,000, which amount represents the estimated Maximum Difference throughout the term of the Bonds, as discussed above. The Letter of

Credit enables the Trustee to draw up to the full amount thereunder unless: (i) on or prior to the third Business Day immediately preceding August 1 of each Fiscal Year during the term of the Bonds it receives written notice from the Corporation to the effect that the operating budget of the Commonwealth for such Fiscal Year has been adopted, or (ii) the Trustee has otherwise received funds representing the full amount of the principal and interest due with respect to the Bonds for the Bond Year commencing within such Fiscal Year. In connection with the issuance of additional Bonds, the Trustee may be required to consent to amendments to the Letter of Credit or release the Letter of Credit in exchange for a new letter of credit from Government Development Bank or another financial institution meeting the requirements of the Trust Agreement. Such amended Letter of Credit or successor letter of credit would be in a stated amount higher or lower than the stated amount of the Letter of Credit to the extent the Maximum Difference increases or decreases as a result of the issuance of additional Bonds. See “Source of Payment and Security for the Bonds—Limitation on Additional Bonds.”

The Letter of Credit will expire on August 15, 2030. The stated amount of the Letter of Credit will be reduced by the amount of any drawing thereunder. The Letter of Credit will be reinstated in the amount of any drawing upon receipt by Government Development Bank of reimbursement of the full amount due to it with respect to such drawing. The Letter of Credit will not cover the risk that no appropriation is made by the Legislature of Puerto Rico under the Act for any particular Fiscal Year (or that an appropriation is made pursuant to the Act in an amount lower than the amount of debt service on the Notes due with respect to any particular Fiscal Year). If the budget for any particular Fiscal Year is adopted but no appropriation for the payment of the Notes is included in such budget, the Trustee may not make a draw under the Letter of Credit. The Letter of Credit will be issued pursuant to a Letter of Credit and Reimbursement Agreement, dated the date of issuance of the 2001 Series C Bonds and 2001 Series D Bonds, by and between the Corporation and the Letter of Credit Bank. Appendix III sets forth certain information with respect to Government Development Bank.

The Trust Agreement permits the Corporation to substitute the Letter of Credit or any successor letter of credit for a letter of credit in the same stated amount, for a term at least as long as the remaining term of the Letter of Credit or the successor letter of credit being replaced, containing administrative provisions substantially similar to those of the Letter of Credit and reasonably acceptable to the Trustee and issued by a bank, banking association or trust company whose long-term debt obligations are rated at the time of issuance of such letter of credit in one of the three highest rating categories (without regard to any gradations within any such category) by Standard & Poor’s and Moody’s.

Flow of Funds

Under the Trust Agreement the Corporation agrees to cause the Secretary of the Treasury to transfer to the Trustee, no later than July 15 of each Fiscal Year while the Bonds are Outstanding, funds representing the entire Legislative Appropriation needed for the payment of all amounts due in respect of the Notes (including principal of and interest on the Bonds) for the immediately succeeding Bond Year, for deposit in the Sinking Fund as described below.

Any Legislative Appropriation (or funds received in substitution therefor or with respect to the Notes, including any moneys received pursuant to a draw under the Letter of Credit) and other funds received by the Trustee, including any Hedge Counterparty Swap Payments (other than moneys received from draws made under any Credit Facility or Liquidity Facility, other than the Letter of Credit, which moneys will be deposited in special subaccounts as provided in the Trust Agreement) for the payment of principal of and interest on the Bonds shall be deposited in the Sinking Fund in the following order:

first, to the credit of the Bond Service Account, such amount as may be required to make the total amount then to the credit of the Bond Service Account equal to the sum of (i) the amount of interest then or to become due and payable on the Bonds of each Series then Outstanding during the Bond Year commencing within the Fiscal Year with respect to which such Legislative Appropriation is made or such funds are received; and (ii) the amount of principal then or to become due and payable not later than July 31 of such Bond Year on the Serial Bonds of each Series then Outstanding;

second, to the credit of the Redemption Account, such amount as may be required to make the total amount then to the credit of the Redemption Account in the Bond Year commencing within the Fiscal Year

with respect to which such Legislative Appropriation is made or such funds are received equal to the Amortization Requirement for such Bond Year for the Term Bonds of each Series then Outstanding; and

third, to the credit of the Surplus Account, any remaining amount.

Under the Trust Agreement, the Trustee is required to make a draw under the Letter of Credit on the second Business Day immediately preceding August 1 of any Bond Year unless it receives written notice from the Corporation prior to such date to the effect that a budget for the Fiscal Year commencing on the preceding July 1 has been adopted or it has otherwise received funds representing the full amount of principal and interest due with respect to the Bonds for such Bond Year.

Upon the delivery of the 2001 Series E Bonds, the Trustee will deposit to the credit of the Bond Service Account approximately \$1,000,000, which sum will be applied by the Trustee to the payment of interest on the 2001 Series E Bonds becoming due on August 1, 2002. Such sum will not be available to pay any other debt service on the Series 2001 Bonds.

No Acceleration of the Bonds

The Bonds are not subject to acceleration upon the occurrence of an event of default or otherwise.

Limitation on Additional Bonds

No additional bonds may be issued under the Trust Agreement except to (i) fund the purchase by the Corporation of additional Notes covered by the Act, (ii) refund any Bonds issued under the Trust Agreement, (iii) fund a Reserve Account, if applicable, (iv) pay capitalized interest with respect to such additional Bonds, or (v) to pay the costs of issuance of such additional Bonds. All such additional Bonds will be issued on a parity with the Series 2001 Bonds and will be entitled to the same benefit and security under the Trust Agreement.

No additional Bonds may be issued unless the amounts of principal and interest payable under the Notes (assuming timely payments under the Notes) after the issuance of such additional Bonds are sufficient to pay the principal of and interest on all Bonds Outstanding after the issuance of such additional Bonds as the same become due, together with other amounts required to be paid by the Corporation with respect to the Bonds, any outstanding Credit or Liquidity Facility, if applicable, or under the Trust Agreement. In addition, no additional Bonds may be issued unless the Letter of Credit is amended to change the stated amount thereof or a successor letter of credit is issued in favor of the Trustee, if necessary, so that in either case the stated amount of the Letter of Credit or such successor letter of credit is not less than the estimated Maximum Difference after the issuance of such additional Bonds as certified by the Corporation. Any successor letter of credit must be issued by a bank, banking association or trust company whose long-term debt obligations are rated at the time of issuance of such letter of credit in any of the three highest rating categories (without regard to any gradations within any such category) by Standard & Poor's and Moody's.

Budgetary Process and Payment of Commonwealth Obligations

The Fiscal Year of the Commonwealth begins on July 1 and ends on June 30 (references herein to a particular Fiscal Year are based on the year in which such Fiscal Year ends). The Governor is constitutionally required to submit to the Legislature of Puerto Rico an annual budget of capital improvements and operating expenses of the Commonwealth for the ensuing Fiscal Year. The annual budget is prepared by the Office of Management and Budget, working with the Planning Board, the Treasury Department, Government Development Bank and other government offices and agencies. Section 7 of Article VI of the Constitution of Puerto Rico provides: "The appropriations made for any Fiscal Year shall not exceed the total revenues, including available surplus, estimated for said Fiscal Year unless the imposition of taxes sufficient to cover said appropriations is provided by law."

The annual budget, which is developed utilizing elements of program budgeting and zero-base budgeting, includes an estimate of revenues and other resources for the ensuing Fiscal Year under (i) laws existing at the time the budget is submitted and (ii) legislative measures proposed by the Governor and submitted with the proposed budget,

as well as the Governor's recommendations as to appropriations that in his/her judgment are necessary, convenient, and in conformity with the four-year investment plan prepared by the Planning Board.

The Legislature of Puerto Rico may amend the budget submitted by the Governor, but may not increase any items so as to cause a deficit without imposing taxes to cover such deficit. Upon passage by the Legislature of Puerto Rico, the budget is referred to the Governor, who may decrease or eliminate any item, but may not increase or insert any new item in the budget. The Governor may also veto the budget in its entirety and return it to the Legislature of Puerto Rico with objections. The Legislature of Puerto Rico, by a two-thirds majority in each house, may override the Governor's veto. If a budget is not adopted prior to the end of the Fiscal Year, the annual budget for the preceding Fiscal Year as originally approved by the Legislature of Puerto Rico and the Governor is automatically renewed for the ensuing Fiscal Year until a new budget is approved by the Legislature of Puerto Rico and the Governor. This permits the Commonwealth to continue to make payments of its operating and other expenses until a new budget is approved.

During any Fiscal Year in which the resources available to the Commonwealth are insufficient to cover the appropriations approved for such year, the Governor may take administrative measures necessary to balance the budget, or make recommendations to the Legislature of Puerto Rico for new taxes, or take any other necessary action to meet the estimated deficiency, or authorize borrowings under provisions of existing legislation, or take action which involves a combination of such steps. Any such proposed adjustments shall give effect to the "priority norms" established by law for the disbursement of public funds in the following order of priority: first, the payment of the interest on, and amortization requirements for, public debt (Commonwealth general obligation and guaranteed debt); second, the fulfillment of obligations arising out of legally binding contracts, court decisions on eminent domain and certain commitments to protect the name, credit and good faith of the Commonwealth government; third, current expenditures in the areas of health, protection of persons and property, education, welfare and retirement systems; and fourth, all other purposes.

The Constitution of Puerto Rico provides that the public debt of the Commonwealth will constitute a first claim on available Commonwealth revenues. Public debt of the Commonwealth includes general obligation bonds and notes of the Commonwealth to which the full faith, credit and taxing power of the Commonwealth are pledged and, according to opinions rendered by the Attorney General of the Commonwealth, also any payments required to be made by the Commonwealth under its guarantees of bonds and notes issued by its public instrumentalities. **The Bonds do not constitute public debt of the Commonwealth for purposes of the constitutional provision described above.**

For a description of the public debt of the Commonwealth and a more detailed discussion of the Commonwealth Budget, see the Commonwealth Report, which is incorporated herein by reference.

PRO FORMA PUBLIC SECTOR DEBT OF THE COMMONWEALTH

The following table presents a summary of the public sector debt of the Commonwealth (1) as of June 30, 2001, as adjusted for the issuance on August 2, 2001 of the Corporation's 2001 Series A and Series B Bonds in the aggregate principal amount of \$390,000,000 (the "Prior 2001 Bonds") and for the issuance on October 25, 2001 of the Commonwealth's Public Improvement Bonds of 2002, Series A and Series B and its Public Improvement Refunding Bonds, Series 2002A in the aggregate principal amount of \$1,312,960,000 (collectively, the "2002 Bonds") and the refunding of the bonds refunded thereby, (2) as further adjusted for the issuance of the Corporation's Series 2001 Bonds, and (3) as further adjusted for the issuance of the Commonwealth's Public Improvement Refunding Bonds, Series 2002 in the principal amount of \$501,565,000 (the "Forward Delivery Bonds") and the refunding of the bonds referred thereby. The Forward Delivery Bonds have been sold and are expected to be delivered in April 2002. The table should be read in conjunction with the information set forth in "Debt" in the Commonwealth Report.

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

	June 30, 2001 As Adjusted by the Issuance of the Prior 2001 Bonds and the 2002 Bonds ⁽¹⁾	As Adjusted by the Issuance of the Prior 2001 Bonds, the 2002 Bonds and the Series 2001 Bonds ⁽¹⁾	As Adjusted by the Issuance of the Prior 2001 Bonds, the Series 2001 Bonds and the Forward Delivery Bonds ⁽¹⁾
Puerto Rico direct debt	\$ 5,936,380 ⁽²⁾	\$ 5,936,380 ⁽²⁾	\$ 5,933,185 ⁽²⁾
Municipal debt	1,632,170	1,632,170	1,632,170
Public corporations debt			
Puerto Rico guaranteed debt . . .	603,334	603,334	603,334
Debt supported by Puerto Rico appropriations or taxes	12,142,612	14,050,481	14,050,481
Other non-guaranteed debt	<u>6,539,423</u>	<u>6,539,423</u>	<u>6,539,423</u>
Total public corporations debt . .	<u>\$19,285,369</u>	<u>\$21,193,238</u>	<u>\$21,193,238</u>
Total public sector debt	<u>\$26,853,919</u>	<u>\$28,761,788</u>	<u>\$28,758,593</u>

* For a complete recital of all notes to this table, see "Public Sector Debt" under "Debt" in the Commonwealth Report.
(1) Adjusted to exclude the bonds refunded thereby, including bonds refunded with proceeds that are or will be invested in guaranteed investment contracts and that will be considered to be outstanding under their authorizing resolutions and for purposes of calculating the Commonwealth's debt limitation.
(2) Adjusted to exclude payments of principal made on July 1, 2001.

Source: Government Development Bank

TAX MATTERS

Federal Income Taxes

The Internal Revenue Code of 1986, as amended (the "Code"), imposes certain requirements that must be met subsequent to the issuance and delivery of the 2001 Series E Bonds for interest thereon to be and remain excluded from gross income for Federal income tax purposes. Noncompliance with such requirements could cause the interest on the 2001 Series E Bonds to be included in gross income for Federal income tax purposes retroactive to the date of issue of the 2001 Series E Bonds. The Corporation, Government Development Bank and the Authorized Debtors have each covenanted to comply with the applicable requirements of the Code in order to maintain the exclusion of the interest on the 2001 Series E Bonds from gross income for Federal income tax purposes pursuant to Section 103 of the Code.

In the opinion of Nixon Peabody LLP, Bond Counsel, under existing law and assuming compliance with the aforementioned covenant, interest on the 2001 Series E Bonds is excluded from gross income for Federal income tax purposes under Section 103 of the Code. Bond Counsel is also of the opinion that such interest is not treated as a preference item in calculating the alternative minimum tax imposed under the Code with respect to individuals and corporations. Interest on the 2001 Series E Bonds is, however, included in the adjusted current earnings of certain corporations for purposes of computing the alternative minimum tax imposed on such corporations.

Commonwealth Taxes

Bond Counsel is also of the opinion that the 2001 Series E Bonds and the interest thereon are exempt from state, Commonwealth and local income taxation.

Original Issue Discount

Bond Counsel is further of the opinion that the difference between the principal amount of the 2001 Series E Bonds maturing on August 1, 2025, 2029 and 2030 (the “Discount Bonds”) and the initial offering price to the public (excluding bond houses, brokers or similar persons or organizations acting in the capacity of underwriters or wholesalers) at which price a substantial amount of such Discount Bonds of the same maturity was sold constitutes original issue discount which is excluded from gross income for Federal income tax purposes to the same extent as interest on the 2001 Series E Bonds. Further, such original issue discount accrues actuarially on a constant interest rate basis over the term of each Discount Bond and the basis of each Discount Bond acquired at such initial offering price by an initial purchaser thereof will be increased by the amount of such accrued original issue discount. The accrual of original issue discount may be taken into account as an increase in the amount of tax-exempt income for purposes of determining various other tax consequences of owning the Discount Bonds, even though there will not be a corresponding cash payment. Owners of the Discount Bonds are advised that they should consult with their own advisors with respect to the state and local tax consequences of owning such Discount Bonds.

Original Issue Premium

The 2001 Series E Bonds maturing on August 1, 2026 and 2027 (the “Premium Bonds”) are being offered at prices in excess of their principal amounts. Bond Counsel is of the opinion that an initial purchaser with an initial adjusted basis in a Premium Bond in excess of its principal amount will have amortizable bond premium which is not deductible from gross income for Federal income tax purposes. The amount of amortizable bond premium for a taxable year is determined actuarially on a constant interest rate basis over the term of each Premium Bond based on the purchaser’s yield to maturity (or, in the case of Premium Bonds callable prior to their maturity, over the period to the call date, based on the purchaser’s yield to the call date and giving effect to any call premium). For purposes of determining gain or loss on the sale or other disposition of a Premium Bond, an initial purchaser who acquires such obligation with an amortizable bond premium is required to decrease such purchaser’s adjusted basis in such Premium Bond annually by the amount of amortizable bond premium for the taxable year. The amortization of bond premium may be taken into account as a reduction in the amount of tax-exempt income for purposes of determining various other tax consequences of owning such 2001 Series E Bonds. Owners of the Premium Bonds are advised that they should consult with their own advisors with respect to the state and local tax consequences of owning such Premium Bonds.

Certain Federal Tax Information

General. The following is a discussion of certain additional tax matters under existing statutes. It does not purport to deal with all aspects of Federal taxation that may be relevant to particular investors. Prospective investors, particularly those who may be subject to special rules, are advised to consult their own tax advisors regarding the Federal tax consequences of owning and disposing of the 2001 Series E Bonds, as well as any tax consequences arising under the laws of any state or other taxing jurisdiction.

Social Security and Railroad Retirement Payments. The Code provides that interest on tax-exempt obligations is included in the calculation of modified adjusted gross income in determining whether a portion of Social Security or railroad retirement benefits received are to be included in taxable income.

Branch Profits Tax. The Code provides that interest on tax-exempt obligations is included in effectively connected earnings and profits for purposes of computing the branch profits tax on certain foreign corporations doing business in the United States.

Borrowed Funds. The Code provides that interest paid (or deemed paid) on borrowed funds used during a tax year to purchase or carry tax-exempt obligations is not deductible. In addition, under rules used by the Internal Revenue Service for determining when borrowed funds are considered used for the purpose of purchasing or carrying particular assets, the purchase of obligations may be considered to have been made with borrowed funds even though the borrowed funds are not directly traceable to the purchase of such obligations.

Property and Casualty Insurance Companies. The Code contains provisions relating to property and casualty insurance companies whereunder the amount of certain loss deductions otherwise allowed is reduced (in certain cases

below zero) by a specified percentage of, among other things, interest on tax-exempt obligations acquired after August 7, 1986.

Financial Institutions. The Code provides that commercial banks, thrift institutions and other financial institutions may not deduct the portion of their interest expense allocable to tax-exempt obligations acquired after August 7, 1986, other than certain “qualified” obligations. The 2001 Series E Bonds are not “qualified” obligations for this purpose.

S Corporations. The Code imposes a tax on excess net passive income of certain S corporations that have subchapter C earnings and profits. Interest on tax-exempt obligations must be included in passive investment income for purposes of this tax.

Earned Income Credit. For any taxable year beginning after December 31, 1995, the Code denies the earned income credit to persons otherwise eligible for it if the aggregate amount of disqualified income of the taxpayer for the taxable year exceeds \$2,200, subject to adjustment for inflation for taxable years beginning after December 31, 1996. Interest on the 2001 Series E Bonds will constitute disqualified income for this purpose.

Changes in Federal Tax Law and Post Issuance Events. From time to time proposals are introduced in Congress that, if enacted into law, could have an adverse impact on the potential benefits of the exclusion from gross income for Federal income tax purposes of the interest on the 2001 Series E Bonds, and thus on the economic value of the 2001 Series E Bonds. This could result from reductions in Federal income tax rates, changes in the structure of the Federal income tax rates, changes in the structure of the Federal income tax or its replacement with another type of tax, repeal of the exclusion of the interest on the 2001 Series E Bonds from gross income for such purposes, or otherwise. It is not possible to predict whether any legislation having an adverse impact on the tax treatment of holders of the 2001 Series E Bonds may be proposed or enacted. Bond Counsel has not undertaken to advise in the future whether any events after the date of issuance and delivery of the 2001 Series E Bonds may affect the tax status of interest on the 2001 Series E Bonds. Bond Counsel expresses no opinion as to any Federal, State or local tax law consequences with respect to the 2001 Series E Bonds, or the interest thereon, if any action is taken with respect to the 2001 Series E Bonds or the proceeds thereof upon the advice or approval of other counsel.

CONTINUING DISCLOSURE UNDERTAKING

In accordance with the requirements of Rule 15c2-12, as amended (the “Rule”), promulgated by the Securities and Exchange Commission, the Corporation and the Commonwealth, as specifically stated below, have agreed in a continuing disclosure agreement for the benefit of the Beneficial Owners to provide or cause to provide the following:

1. The Commonwealth will file with each NRMSIR and with any Commonwealth state information depository (“SID”) core financial information and operating data for each Fiscal Year, including (i) its audited financial statements prepared in accordance with generally accepted accounting principles in effect from time to time and (ii) material historical quantitative data (including financial information and operating data) on the Commonwealth, and information as to revenues, expenditures, financial operations and indebtedness of the Commonwealth, generally consistent with the information contained in the Commonwealth Report. Such information is expected to be filed within 305 days after the end of each Fiscal Year.

2. The Corporation will file, in a timely manner, with each NRMSIR or with the MSRB and with any SID, notice of the failure by the Commonwealth to comply with paragraph 1 above and notice of the occurrence of any of the following events with respect to the 2001 Series E Bonds if, in the judgment of the Corporation or its agent, such event is 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-exempt status of the 2001 Series E Bonds;
- g. modifications to rights of the holders (including beneficial owners) of the 2001 Series E Bonds;
- h. bond calls;
- i. defeasances;
- j. release, substitution, or sale of property securing repayment of the 2001 Series E Bonds; and
- k. rating changes.

The Corporation 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 Corporation, such other event is material with respect to the 2001 Series E Bonds, but the Corporation does not undertake to provide any such notice of the occurrence of any material event except those events listed above.

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 2001 Series E Bonds do not provide for “debt service reserves.” In addition, with respect to the following events:

Events (d) and (e). The Corporation does not undertake to provide any notice with respect to credit enhancement added after the primary offering of the 2001 Series E Bonds, unless the Corporation applies for or participates in obtaining the enhancement.

Event (f). For information on the tax status of the 2001 Series E Bonds, see “Tax Matters.”

Event (h). The Corporation does not undertake to provide the above-described event notice of a mandatory scheduled redemption, not otherwise contingent upon the occurrence of an event, if (i) the terms, dates and amounts of redemption are set forth in detail in this Official Statement under “The 2001 Series E Bonds — Mandatory Redemption,” (ii) the only open issue is which 2001 Series E Bonds will be redeemed in the case of a partial redemption, (iii) notice of redemption is given to the Bondholders as required under the terms of the 2001 Series E Bonds, and (iv) public notice of the redemption is given pursuant to Securities Exchange Act of 1934 Release No. 34-23856 of the SEC, even if the originally scheduled amounts are reduced by prior optional redemptions or 2001 Series E Bond purchases.

The Commonwealth expects to provide the information described in paragraph 1(ii) above by filing its first bond official statement that includes such information for the preceding Fiscal Year or, if no such official statement is issued by the 305-day deadline, by filing its Financial Information and Operating Data Report containing the information described in paragraph 1(ii) above by such deadline.

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 J.J. Kenny Repository, 55 Water Street, 45th Floor, New York, New York 10041; FT Interactive Data, Attn.: NRMSIR, 100 William Street, New York, New York 10038; and DPC Data Inc., One Executive Drive, Fort Lee, New Jersey 07024.

The Commonwealth and the Corporation acknowledge that their undertaking pursuant to the Rule described under this heading is intended to be for the benefit of the holders of the 2001 Series E Bonds, including Beneficial Owners, and shall be enforceable by any such holders or Beneficial Owners; provided that the right to enforce the provisions of this undertaking shall be limited to a right to obtain specific enforcement of the Corporation's or the Commonwealth's obligations hereunder, and any failure by the Corporation or the Commonwealth to comply with the provisions of this undertaking shall not be an event of default with respect to the 2001 Series E Bonds under the Trust Agreement. The Corporation further acknowledges that it has not failed to comply with any similar undertaking under the Rule for the last five years.

No bondholder or Beneficial Owner may institute any suit, action or proceeding at law or in equity (“Proceeding”) for the enforcement of the foregoing covenants (the “Covenants”) or for any remedy for breach thereof, unless such bondholder or Beneficial Owner shall have filed with the Corporation and the Commonwealth written notice of any request to cure such breach, and the Corporation 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 for the equal benefit of all bondholders or Beneficial Owners of the Outstanding 2001 Series E

Bonds benefitted by the Covenants, and no remedy shall be sought or granted other than specific performance of any of the Covenants at issue. Notwithstanding the foregoing, no challenge to the adequacy of the information provided in accordance with the filings mentioned above may be prosecuted by any bondholder or Beneficial Owner except in compliance with the remedial and enforcement provisions contained in the Trust Agreement. Moreover, Proceedings filed by bondholders or Beneficial Owners against the Commonwealth may be subject to the sovereign immunity provisions of Article 2 of Law No. 104 of the Legislature of Puerto Rico, approved June 29, 1955, as amended (32 L.P.R.A. §3077), which governs the scope of legal actions against the Commonwealth and substantially limits the amount of monetary damages that may be granted against the Commonwealth.

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 Corporation or the Commonwealth, or type of business conducted; the Covenants, as amended, would have complied with the requirements of the Rule at the time of award of the 2001 Series E Bonds, after taking into account any amendments or change in circumstances; and the amendment does not materially impair the interests of bondholders or Beneficial Owners, as determined by parties unaffiliated with the Corporation or the Commonwealth; or

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

The Commonwealth has further agreed that the annual financial information containing any amended operating data or financial information will explain, in narrative form, the reasons for the amendment and the impact of the change in the type of operating data or financial information being provided.

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

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

UNDERWRITING

The Underwriters have jointly and severally agreed, subject to certain conditions, to purchase the 2001 Series E Bonds from the Corporation at an aggregate discount of \$7,795,805.74 from the initial public offering prices of the 2001 Series E Bonds set forth or derived from information set forth on the inside cover page hereof. The obligations of the Underwriters are subject to certain conditions precedent, and the Underwriters will be obligated to purchase all the 2001 Series E Bonds, if any 2001 Series E Bonds are purchased. The Underwriters may offer to sell the 2001 Series E Bonds to certain dealers and others at prices lower than the initial public offering prices, and such offering prices may be changed, from time to time, by the Underwriters.

Morgan Stanley & Co. Incorporated (“Morgan Stanley”) has entered into a written agreement with Popular Securities Inc. (“Popular Securities”) pursuant to which Popular Securities has agreed to act as a consultant to Morgan Stanley in connection with Morgan Stanley’s provision of underwriting and investment banking services to the Corporation with respect to the 2001 Series E Bonds. Pursuant to this agreement, the existence of which has been disclosed to the Corporation and Government Development Bank, Popular Securities will be entitled to receive a portion of Morgan Stanley’s actual net profits, if any, in connection with the underwriting of the 2001 Series E Bonds. Other similar agreements with respect to the sharing of underwriting net profits have been entered into and disclosed to the Corporation and Government Development Bank by the following Underwriters: ABN Amro Financial Services, Inc. and Prudential Securities Corporation; Banc of America Securities LLC and Oriental Financial Services Corporation; Goldman, Sachs & Co. and FirstBank Puerto Rico; Lehman Brothers Inc. and BBVA Capital Markets of Puerto Rico, Inc.; Merrill Lynch & Co. and Santander Securities Corporation; and Wachovia Securities and Doral Securities Inc.

LEGAL MATTERS

The proposed form of opinion of Nixon Peabody LLP, Bond Counsel, is attached as Appendix II to this Official Statement. Certain legal matters will be passed upon for the Underwriters by Pietrantoni Méndez & Alvarez LLP, San Juan, Puerto Rico.

LEGAL INVESTMENT

The 2001 Series E Bonds will be eligible for deposit by banks in Puerto Rico to secure public funds and will be approved investments for domestic insurance companies.

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO

As required by Act No. 272 of the Legislature of Puerto Rico, approved May 15, 1945, as amended, Government Development Bank has acted as financial advisor to the Corporation in connection with the 2001 Series E Bonds offered hereby. As financial advisor, Government Development Bank participated in the selection of the Underwriters of the 2001 Series E Bonds. Certain of the Underwriters have been selected by Government Development Bank to serve from time to time as underwriters of its obligations and the obligations of the Commonwealth, its instrumentalities and public corporations. Certain of the Underwriters or their affiliates participate in other financial transactions with Government Development Bank.

RATINGS

Moody's and Standard & Poor's have assigned the 2001 Series E Bonds ratings of Baa3 and A-, respectively, and are expected to give the Ambac Insured Bonds ratings of Aaa and AAA, respectively, based on the expected issuance by Ambac of the Ambac Financial Guaranty Insurance Policy. These 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. There is no assurance that such ratings will remain in effect for any given period of time or that they will not be revised downward or withdrawn entirely by either or both of such rating agencies, if in the judgment of either or both, circumstances so warrant. Any such downward revision or withdrawal of either of such ratings may have an adverse effect on the market prices of the 2001 Series E Bonds.

Such rating agencies were provided with materials relating to the Commonwealth and the 2001 Series E Bonds and other relevant information, and no application has been made to any other rating agency for the purpose of obtaining a rating on the 2001 Series E Bonds.

MISCELLANEOUS

The foregoing summaries of or references to the various acts, the 2001 Series E Bonds, the Trust Agreement, the Resolution, the Notes, the Debt Restructuring and Assignment Agreements, the Letter of Credit, the Act and the summaries of or references to the various acts contained in the Commonwealth Report incorporated by reference herein 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 (i) a summary of the provisions of the Trust Agreement (Appendix I), (ii) the proposed form of opinion of Bond Counsel (Appendix II), (iii) information relating to Government Development Bank (Appendix III) and (iv) a specimen of the Ambac Financial Guaranty Insurance Policy (Appendix IV).

This Official Statement incorporates by reference (i) the Commonwealth's Annual Financial Report, and (ii) the Commonwealth Report.

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 the Commonwealth Annual Financial Report and the Commonwealth Report incorporated herein by reference. Requests for such document should be directed to Director-General Obligations Division, Government Development Bank for Puerto Rico, P.O. Box 42001, Santurce, PR 00940, telephone number (787) 722-7060.

A copy of the Commonwealth Annual Financial Report and the Commonwealth Report may be obtained by contacting a NRMSIR. The address of each NRMSIR is set forth in “Continuing Disclosure Undertaking” above.

The information set forth in this Official Statement was supplied by certain officials of Government Development Bank, the Corporation and 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 in this Official Statement on the authority of such officials or the authority of such publications as public official documents. The information under “The 2001 Series E Bonds—Bond Insurance” (other than the first two paragraphs thereof) was supplied by Ambac.

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

PUERTO RICO PUBLIC FINANCE CORPORATION

By: /s/ José V. Pagán
Executive Vice President

SUMMARY OF THE TRUST AGREEMENT

The following is a summary of certain provisions of the Trust Agreement. The statements contained herein do not purport to be complete and this summary is qualified in its entirety by reference to the Trust Agreement.

Definitions of Certain Terms

The following words and terms have the following meanings, unless the context otherwise requires. Words importing the singular number include the plural number in each case and vice versa, and words importing persons include firms and corporations.

“**Accreted Value**” shall mean with respect to any Capital Appreciation Bond or Capital Appreciation and Income Bond (i) as of any Valuation Date, the amount set forth for such date in the resolution authorizing such Capital Appreciation Bond or Capital Appreciation and Income Bond and (ii) as of any date other than a Valuation Date, the sum of (a) the Accreted Value on the preceding Valuation Date (or, if there is no preceding Valuation Date, the initial principal amount) and (b) the product of (1) a fraction, the numerator of which is the number of days having elapsed from the preceding Valuation Date (or from the original issue date if there is no preceding Valuation Date) and the denominator of which is the number of days from such preceding Valuation Date (or from the original issue date if there is no preceding Valuation Date) to the next succeeding Valuation Date and (2) the difference between the Accreted Values for such Valuation Dates (or between the initial principal amount and the Accreted Value on the first Valuation Date).

“**Act**” shall mean Act Number 164 of the Legislature of Puerto Rico, approved December 17, 2001.

“**Amortization Requirement**” shall mean, for the Term Bonds of any Series for any Bond Year, the principal amount fixed or computed for the retirement by purchase or redemption of Term Bonds in such Bond Year.

The Amortization Requirement for the Term Bonds of each Series shall be initially in the respective principal amounts for each Bond Year as fixed in a resolution of the Corporation adopted prior to the issuance of the Bonds of such Series, and the aggregate amount of such Amortization Requirements for the Term Bonds of such Series shall be equal to the aggregate principal amount of the Term Bonds of such Series.

If at the close of any Bond Year the total principal amount of Term Bonds of any Series retired by purchase or redemption, or called for redemption under the provisions of the Trust Agreement during such Bond Year, shall be in excess of the amount of the Amortization Requirement for the Term Bonds of such Series for such Bond Year, then the amount of the Amortization Requirement for the Term Bonds of such Series shall be reduced for such subsequent Bond Years in such amounts aggregating the amount of such excess as shall be determined by the President of the Corporation in an order filed with the Trustee on or before the fifteenth (15th) day of the August following the close of such Bond Year.

It shall be the duty of the Trustee, on or before the 15th day of each Bond Year, to compute the Amortization Requirement for the then current Bond Year for the Term Bonds of each Series then Outstanding. The Amortization Requirement for the then current Bond Year shall continue to be applicable during the balance of such current Bond Year and no adjustment shall be made therein by reason of Term Bonds purchased or redeemed or called for redemption during such current Bond Year.

“**Appreciated Value**” shall mean, with respect to any Capital Appreciation and Income Bond (i) up to the Interest Commencement Date set forth in the resolution of the Board providing for the issuance of such Bond, an amount equal to the Accreted Value of such Bond and (ii) as of any date of computation on and after the Interest Commencement Date, an amount equal to the Accreted Value of such Bond on the Interest Commencement Date.

“**Authorized Debtors**” shall mean the departments, agencies, instrumentalities and public corporations of the Commonwealth authorized to recognize, formalize, restructure and/or refinance their advances, repayment commitments, obligations and/or loans with Government Development Bank pursuant to the Act.

“**Board**” shall mean the Board of Directors of the Corporation as constituted from time to time and which shall be the Board of Directors of Government Development Bank as provided by Resolution Number Five Thousand Forty-

Four (5044), adopted December twelve (12), nineteen hundred eighty-four (1984) by the Board of Directors of Government Development Bank, as amended, or, if said Board shall be abolished, the board or body succeeding to the principal functions thereof or to whom the powers of the Corporation shall be given by law.

“**Bond Year**” shall mean the period commencing on the first day of August of any year and ending on the last day of July of the following year.

“**Bondholder**,” “**Holder**,” “**holder**,” “**Holder of Bonds**,” or “**Owner**” or any similar term, shall mean any person who shall be the registered owner of any Outstanding Bond or Bonds.

“**Bonds**” or “**bonds**” shall mean the bonds of the Corporation issued under the provisions of the Trust Agreement.

“**Business Day**” means a day other than a Saturday, Sunday or a day on which commercial banks in the City of New York, New York, or San Juan, Puerto Rico, are closed to the public.

“**Capital Appreciation Bonds**” shall mean any Bonds the accruing interest on which is compounded periodically on each of the dates designated for compounding in the resolution authorizing said Bonds and payable in an amount equal to the then current Accreted Value only at the maturity, earlier redemption or other payment date therefor, all as so provided by such resolution, and which may be either Serial Bonds or Term Bonds.

“**Capital Appreciation and Income Bonds**” shall mean any Bonds the accruing interest on which is not paid prior to the Interest Commencement Date specified in the resolution authorizing such Bonds and the Appreciated Value for such Bonds is compounded periodically on the dates designated in such resolution prior to the Interest Commencement Date for such Capital Appreciation and Income Bonds, and which may be either Serial Bonds or Term Bonds.

“**Corporation**” shall mean Puerto Rico Public Finance Corporation, a governmental instrumentality of the Commonwealth of Puerto Rico and a wholly-owned subsidiary of Government Development Bank for Puerto Rico.

“**Corporation Swap Payments**” means the net payments required to be made by the Corporation to the Hedge Counterparty under a Rate Swap (if applicable).

“**Credit Facility**” shall mean an irrevocable letter of credit, policy of municipal bond insurance, guaranty, purchase agreement, credit agreement or similar facility in which the person providing such facility irrevocably agrees to provide funds to make payment of the principal of, premium, if any, and interest on Bonds to which such Credit Facility relates.

“**Fiscal Year**” shall mean the period commencing on the first day of July of any year and ending on the last day of June of the following year or any other twelve month period designated by the Board.

“**GDB Letter of Credit**” shall mean the irrevocable transferable stand-by letter of credit issued by Government Development Bank in favor of the Trustee solely for the benefit of the Bondholders on the date of issue of the Corporation’s 2001 Series C Bonds and 2001 Series D Bonds.

“**Government Development Bank**” shall mean Government Development Bank for Puerto Rico.

“**Government Obligations**” shall mean (i) direct obligations of, or obligations the timely payment of principal of and the interest on which is unconditionally guaranteed by, the United States Government, (ii) direct obligations of, or obligations the principal of and interest on which are unconditionally guaranteed by, any of the following: Banks for Cooperatives, Federal Farm Credit Banks, Federal Home Loan Banks, Export-Import Bank of the United States, Federal Financing Bank, Government National Mortgage Association, Farmer’s Home Administration, Federal Home Loan Mortgage Corporation, Federal National Mortgage Association or Federal Housing Administration, and which obligations are rated at the time of purchase in the highest rating category by both Moody’s and Standard & Poor’s, (iii)

all other obligations issued or unconditionally guaranteed as to principal and interest by an agency or instrumentality controlled or supervised by and acting as an instrumentality of the United States Government pursuant to authority granted by the Congress, which obligations are rated at the time of purchase in the highest rating category by both Moody's and Standard & Poor's and (iv) receipts evidencing the ownership of payments of principal of or interest on any of such obligations, which receipts are rated in the highest rating category by both Moody's and Standard & Poor's.

"Hedge Counterparty" means the provider of any Rate Swap with respect to the Bonds as counterparty under a Swap Agreement which provider must have a rating with respect to its long-term unsecured debt which is rated in one of the three highest rating categories (without regard to any gradation within such category) by Standard & Poor's or Moody's.

"Hedge Counterparty Swap Payments" means the net payments required to be made by a Hedge Counterparty to the Corporation under a Rate Swap.

"Interest Commencement Date" shall mean, with respect to any Capital Appreciation and Income Bond, the date specified in the resolution providing for the issuance of such Bond after which interest accruing on such Bond shall be payable on a periodic basis, with the first such payment date being the applicable Interest Payment Date immediately succeeding such Interest Commencement Date.

"Interest Payment Dates" shall mean the dates on which interest on a Series of Bonds or portion thereof is scheduled to be due and payable, as is provided by a resolution of the Board adopted prior to the issuance of such Series of Bonds.

"Interim Bonds" shall mean any Bonds issued on an interim basis that are expected to be repaid from the proceeds of Bonds or other indebtedness.

"Investment Agreement" shall mean any agreement for the investment of moneys entered into by the Trustee with a Qualified Financial Institution or collateralized at all times by Government Obligations having a market value at least equal to the principal amount of such agreement, as to which collateral the Trustee has a perfected first priority security interest, which collateral is held by the Trustee or its agent free and clear of claims by third parties and which collateral will result in the agreement being rated in the highest rating category by both Moody's and Standard & Poor's.

"Investment Obligations" shall mean (i) Government Obligations, (ii) time deposits, certificates of deposit or similar arrangements with, or banker's acceptances issued by, any bank, banking association or trust company, including the Trustee, which is a member of the Federal Deposit Insurance Corporation having a combined capital and surplus aggregating not less than \$150,000,000 and reported deposits of not less than \$250,000,000, (iii) repurchase agreements with banks mentioned in (ii) above, including the Trustee, or with primary government dealers having a capital and surplus in excess of \$150,000,000, with respect to any of the securities mentioned in (i) above, provided such securities are on deposit with the Trustee (or any duly appointed agent of the Trustee) and such agreements are structured as sale - purchase agreements rather than secured loans, (iv) obligations issued by the Commonwealth or any state or territory of the United States, which are rated in one of the three highest rating categories (without regard to any gradations within such category) by both Moody's and Standard & Poor's, (v) municipal obligations, the payment of the principal of and the interest on which is insured, which are rated in one of the three highest rating categories (without regard to any gradations within such category) by both Moody's and Standard & Poor's, (vi) commercial paper rated, or backed by a letter of credit or line of credit the provider of which is rated, in the highest rating category (without regard to any gradations within such category) by both Moody's and Standard & Poor's, (vii) an Investment Agreement, (viii) money market accounts of any state, Commonwealth or federally chartered bank, banking association, trust company or subsidiary trust company, including the Trustee, that is rated or whose parent bank is rated in the highest short-term rating category or in the highest long-term rating category by Moody's or Standard & Poor's (without regard to any gradations within such category) or money market funds registered under the Investment Company Act of 1940, as amended, whose shares are registered under the Securities Act of 1933, as amended, and having a rating by Standard & Poor's of "AAAm-G" or "AAAm", (ix) units of beneficial interest in any non-arbitrage investment program pools created by Government Development Bank or any of its subsidiaries or affiliates, (x) any obligation permitted under the laws of the Commonwealth which are rated in one of the three highest rating categories (without regard to any

gradations within such category) by both Moody's and Standard & Poor's, and (xi) any securities otherwise permitted as eligible collateral under Act No. 69 of the Legislature of Puerto Rico, approved August 14, 1991, as amended.

“Legislative Appropriation” shall mean the funds appropriated by the Legislature of Puerto Rico in the annual budget of capital improvements and operating expenses of the Commonwealth for any Fiscal Year for the payment of the Notes pursuant to the provisions of the Act or, in the case such budget of the Commonwealth for any Fiscal Year has not been approved by the commencement of such Fiscal Year, until such budget is approved, the funds representing the amounts which had been appropriated in the budget of the Commonwealth for the previous Fiscal Year for the payment of the Notes pursuant to the provisions of the Act in accordance with Article VI, Section 6 of the Constitution of the Commonwealth.

“Liquidity Facility” shall mean a letter of credit, policy of municipal bond insurance, guaranty, purchase agreement or similar facility in which the person providing such facility agrees to provide funds to pay the purchase price of Put Bonds upon their tender by the Holders of Put Bonds.

“Loans” shall mean the advances, repayment commitments, obligations and/or loans of the Authorized Debtors specified in the Act.

“Maximum Difference” shall mean the maximum increase from one Fiscal Year to the next in the aggregate debt service on the Notes and on the Loans remaining with Government Development Bank.

“Moody's” means Moody's Investors Service, Inc., a corporation organized and existing under the laws of the State of Delaware, its successors and their assigns, and, if such corporation shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, “Moody's” shall be deemed to refer to any other nationally recognized securities rating agency designated by the Corporation.

“Notes” shall mean promissory notes of the Authorized Debtors executed in connection with the restructuring of Loans pursuant to the Act and purchased with the proceeds of any Series of Bonds and pledged to the Trustee pursuant to the Trust Agreement.

“Outstanding” when used with reference to the Bonds shall mean, as of any date of determination, all Bonds theretofore authenticated and delivered except:

- a) Bonds theretofore cancelled by the Trustee or delivered to the Trustee for cancellation;
- b) Bonds that are deemed paid and no longer outstanding, as provided in the Trust Agreement;
- c) Bonds paid or Bonds in lieu of which other Bonds have been issued pursuant to the provisions of the Trust Agreement relating to Bonds destroyed, mutilated, stolen or lost, unless evidence satisfactory to the Trustee has been received that any such Bond is held by a bona fide purchaser;
- d) Bonds tendered or deemed tendered, as provided in the resolution of the Board for any Series of Bonds; and
- e) for purposes of any consent or other action to be taken under the Trust Agreement by the Holders of a specified percentage principal amount of Bonds, Bonds actually known by the Trustee to be held by or for the account of the Corporation.

“Pledged Revenues” shall mean all of the Corporation's right, title and interest in and to (i) all amounts paid and to be paid in respect of the Notes, (ii) all moneys and Investment Obligations on deposit to the credit of the Sinking Fund, (iii) the Hedge Counterparty Swap Payments, if any, and (iv) all investment earnings on the foregoing.

“Put Bonds” shall mean Bonds that by their terms may be tendered by and at the option of the Holder thereof for payment prior to the stated maturity thereof.

“Qualified Financial Institution” means the Federal National Mortgage Association, or any bank, trust company or national banking association, or a corporation subject to registration with the Board of Governors of the Federal Reserve System under the Bank Holding Company Act of 1956, as amended, or any government securities dealer, insurance company or other financial institution, in each case whose unsecured obligations or uncollateralized long term debt obligations (or obligations guaranteed by its parent entity) shall at all times during the term of the Investment Agreement issued by such Qualified Financial Institution have been assigned a rating by Standard & Poor’s and Moody’s in one of the three highest rating categories (without regard to any gradations within any such category), or which has issued a letter of credit, contract or agreement in support of debt obligations which at all times shall have been so rated.

“Rate Swap” means any interest rate swap arrangement between the Corporation and a Hedge Counterparty pursuant to any Swap Agreement and related documentation.

“Rating Agencies” shall mean Standard & Poor’s and Moody’s.

“Reimbursement Agreement” shall mean any letter of credit and reimbursement agreement or other similar agreement to pay the amounts due to the provider of a Credit Facility or a Liquidity Facility between the Corporation and any provider of a Credit Facility or a Liquidity Facility.

“Reimbursement Obligation” shall mean all amounts payable by the Corporation to a provider of a Credit Facility or Liquidity Facility pursuant to its agreement with such provider, including any fees payable and expenses reimbursable to such provider.

“Reserve Account” shall mean the account of that name which may be established in the Sinking Fund.

“Reserve Account Insurance Policy” shall mean the insurance policy, surety bond or other evidence of insurance deposited to the credit of the Reserve Account in lieu of or in partial substitution for cash or securities on deposit therein, which policy, bond or other evidence of insurance constitutes an unconditional senior obligation of the issuer thereof. The issuer thereof shall be a municipal bond insurer whose senior debt obligations, ranking pari passu with its obligations under such policy, bond or other evidence of insurance, are rated, at the time of deposit for the credit of the Reserve Account, in any of the three highest rating categories (without regard to any gradations within any such category) by Moody’s and Standard & Poor’s.

“Reserve Account Letter of Credit” shall mean the irrevocable, transferable letter of credit deposited to the credit of the Reserve Account in lieu of or in partial substitution for cash or securities on deposit therein, which letter of credit constitutes an unconditional senior obligation of the issuer thereof. The issuer of such letter of credit shall be Government Development Bank or a banking association, bank or trust company or branch thereof whose senior debt obligations, ranking pari passu with its obligations under such letters of credit are rated at the time of deposit to the credit of the Reserve Account, in any of the three highest rating categories (without regard to any gradations within any such category) by Moody’s and Standard & Poor’s.

“Serial Bonds” shall mean the Bonds designated as serial bonds in the resolutions authorizing such Bonds.

“Series” shall mean all of the Bonds authenticated and delivered at one time on original issuance and pursuant to any resolution authorizing such Bonds as a separate Series of Bonds, or any Bonds thereafter authenticated and delivered in lieu of or in substitution for such Bonds pursuant to the Trust Agreement, regardless of variations in maturity, interest rate or other provisions.

“Sinking Fund” shall mean the “Puerto Rico Public Finance Corporation Act 164 Sinking Fund,” a special fund created and designated pursuant to the Trust Agreement.

“Standard & Poor’s” means Standard & Poor’s Ratings Services, a division of the McGraw-Hill Companies, Inc., a corporation organized and existing under the laws of the State of New York, its successors, their assigns, and, if such corporation shall be dissolved or liquidated or shall no longer perform the functions of a securities rating agency, “Standard & Poor’s” shall be deemed to refer to any other nationally recognized securities rating agency designated by the Corporation.

“**Swap Agreement**” shall mean any Interest Rate Swap Agreement between the Corporation and a Hedge Counterparty related to the Bonds.

“**Term Bonds**” shall mean the Bonds designated as term bonds in the resolutions authorizing such Bonds.

“**Valuation Date**” shall mean, with respect to any Capital Appreciation Bond or Capital Appreciation and Income Bond, the date or dates set forth in the resolution authorizing such bonds on which Accreted Values are assigned to the Capital Appreciation Bonds or Capital Appreciation and Income Bonds.

“**Variable Rate Bonds**” shall mean Bonds issued with a variable, adjustable, convertible or similar interest rate that is not fixed in percentage at the date of issue for the term thereof.

Sinking Fund and Accounts

A special fund is created under the Trust Agreement and designated the “Puerto Rico Public Finance Corporation Act 164 Sinking Fund” (the “Sinking Fund”) to be held by the Trustee. There are created three separate accounts in the Sinking Fund designated “Bond Service Account,” “Redemption Account,” and “Surplus Account.” If the resolution of the Board providing for the issuance of Bonds under the Trust Agreement requires that a Reserve Account be established, a separate account in the Sinking Fund designated “Reserve Account” is authorized to be created in accordance with such resolution. Subject to the terms and conditions set forth in the Trust Agreement, moneys held to the credit of the Sinking Fund shall be held in trust and applied by the Trustee solely for the purposes set forth below and pending such application shall be subject to the lien and charge created pursuant to the Trust Agreement until paid out or transferred as provided therein.

The Corporation shall cause the Secretary of the Treasury of the Commonwealth to transfer to the Trustee, no later than July 15 of each Fiscal Year while the Bonds are Outstanding, funds representing the entire Legislative Appropriation for such Fiscal Year.

All funds received by the Trustee representing the Legislative Appropriation (or funds received in substitution therefor or in respect of the Notes, including any moneys received pursuant to a draw under the GDB Letter of Credit) and other funds received by the Trustee, including any Hedge Counterparty Swap Payments (other than any moneys received from draws made under any Credit Facility or Liquidity Facility, other than the GDB Letter of Credit, which moneys will be deposited in special subaccounts as provided below), shall be deposited in the Sinking Fund in the following order:

first, to the credit of the Bond Service Account, such amount as may be required to make the total amount then to the credit of the Bond Service Account equal to the sum of (i) the amount of interest then or to become due and payable on the Bonds of each Series then Outstanding during the Bond Year commencing within the Fiscal Year with respect to which such Legislative Appropriation is made or such funds are received and (ii) the amount of principal then or to become due and payable not later than July 31 of such Bond Year on the Serial Bonds of each Series then Outstanding;

second, to the credit of the Redemption Account, such amount as may be required to make the total amount then to the credit of the Redemption Account in the Bond Year commencing within the Fiscal Year with respect to which such Legislative Appropriation is made or such funds are received equal to the Amortization Requirement for such Bond Year for the Term Bonds of each Series then Outstanding; and

third, to the credit of the Surplus Account, any remaining amount.

In lieu of any required deposit or in substitution of moneys on deposit to the credit of the Reserve Account (if applicable), the Corporation may cause to be deposited to the credit of the Reserve Account a Reserve Account Insurance Policy or a Reserve Account Letter of Credit in an amount equal to such required deposit, which Reserve Account Insurance Policy or Reserve Account Letter of Credit shall be satisfactory in form and substance to the Trustee and shall be payable or available to be drawn upon, as the case may be (upon the giving of notice as required thereunder), on any payment date for the Bonds on which a withdrawal from the Reserve Account would be required

under the Trust Agreement, and give the Trustee the right to draw on any Reserve Account Insurance Policy or Reserve Account Letter of Credit prior to the expiration thereof unless the Corporation has furnished a replacement Reserve Account Insurance Policy or Reserve Account Letter of Credit or has provided sufficient moneys to make the amounts then on deposit to the credit of the Reserve Account equal to the amount required therefor. If a disbursement is made under a Reserve Account Insurance Policy or a Reserve Account Letter of Credit, the funds thereafter becoming available for deposit to the credit of the Reserve Account shall be used by the Trustee to reinstate the amounts available to be drawn under such Reserve Account Insurance Policy or Reserve Account Letter of Credit in an amount at least equal to the amount being reimbursed to the provider of such Reserve Account Insurance Policy or Reserve Account Letter of Credit or, if such reinstatement is not available, to deposit to the credit of the Reserve Account moneys in the amount of the disbursement made under such Reserve Account Insurance Policy or Reserve Account Letter of Credit or a combination of such alternatives.

If the Corporation issues Variable Rate Bonds pursuant to the Trust Agreement, the assumptions for calculating interest for the current Bond Year to ensure a sufficient deposit for the payment of said interest shall be made on the basis established in the resolution authorizing the issuance of such Variable Rate Bonds.

If there is a Credit Facility or a Liquidity Facility issued by a provider in connection with the issuance of a Series of Bonds, any moneys received from draws under such Credit Facility or a Liquidity Facility shall be deposited in separate subaccounts in the Bond Service Account or the Redemption Account, as appropriate, and used to pay the principal of and interest on the Bonds secured thereby.

To the extent required by a resolution of the Board in connection with the issuance of any Series of Bonds, the Trustee shall establish one or more subaccounts within the Bond Service Account and the Redemption Account to segregate amounts paid under any of the Notes and make withdrawals from such subaccounts to make payments under any Series of Bonds designated in such resolution. Nothing in the foregoing sentence shall be deemed to affect the parity status of the Bonds.

Withdrawals from Bond Service Account

On each Interest Payment Date or as otherwise provided in the resolution of the Board authorizing the issuance of a Series of Bonds, the Trustee shall withdraw from the Bond Service Account and (1) remit by mail (or by wire transfer if so provided by resolution of the Board) to each Holder of Bonds the amounts required for paying interest upon such Bonds as such interest becomes due, and (2) set aside sufficient moneys for paying the principal of Serial Bonds as such principal becomes due.

Withdrawals from Redemption Account

Moneys held to the credit of the Redemption Account shall be applied to the retirement of Bonds as follows:

(a) Subject to the provisions of paragraph (c) below, the Trustee shall endeavor to purchase Bonds or portions of Bonds, whether or not such Bonds or portions shall then be subject to redemption, at the most advantageous price obtainable by it with reasonable diligence, such price not to exceed the principal of such Bonds plus the amount of the premium, if any, that would be payable on the next redemption date to the holders of such Bonds under the redemption provisions of the Trust Agreement if such Bonds or portions of Bonds should be called for redemption on such date from the moneys in the Sinking Fund. The Trustee shall pay the interest accrued on such Bonds or portions of Bonds to the date of delivery thereof from the Bond Service Account and the principal portion of such purchase price from the Redemption Account. No such purchase shall be made by the Trustee within the period of forty-five (45) days immediately preceding the date on which such Bonds are subject to call for redemption under the redemption provisions of the Trust Agreement except from moneys in excess of the amounts set aside or deposited for such redemption of Bonds;

(b) Subject to the provisions of paragraph (c) below, the Trustee shall call for redemption on each date on which Bonds are subject to redemption from moneys in the Sinking Fund such amount of Bonds or portions of Bonds then subject to redemption as, with the redemption premium, if any, will exhaust the moneys then held for the credit of the Redemption Account as nearly as may be; provided, however, that not less than \$100,000 principal amount of Bonds shall be called for redemption at any one time. Such redemption shall be made pursuant to the redemption

provisions of the Trust Agreement. Prior to calling Bonds or portions of Bonds for redemption the Trustee shall withdraw from the Bond Service Account and from the Redemption Account (including moneys transferred from the Reserve Account (if applicable) to the credit of the Redemption Account) and set aside in separate accounts or deposit with the paying agents the respective amounts required for paying the interest on, and the principal and redemption premium, if any, of the Bonds or portions of Bonds so called for redemption;

(c) Moneys in the Redemption Account shall be applied by the Trustee in each Bond Year to the retirement of Bonds of each Series then Outstanding in the following order:

first, the Term Bonds of each such Series to the extent of the Amortization Requirement, if any, for such Bond Year for the Term Bonds of each such Series then Outstanding, plus the applicable premium, if any, and, if the amount available in such Bond Year shall not be sufficient therefor, then in proportion to the Amortization Requirement, if any, for such Bond Year for the Term Bonds of each such Series then Outstanding, plus the applicable premium, if any;

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

third, any balance then remaining shall be applied to the retirement of Bonds of each Series as directed by the Corporation.

Withdrawals from Surplus Account

Moneys held to the credit of the Surplus Account shall be applied by the Trustee to make payments in the following order: (i) to make up any deficiency in the Bond Service Account and the Redemption Account; (ii) to pay the compensation of the Trustee and other amounts payable to the Trustee under the Trust Agreement upon the written request of the Corporation; (iii) to make Corporation Swap Payments (if applicable); (iv) to pay any fees and expenses payable to the providers of any Credit Facility, Liquidity Facility, Reserve Account Insurance Policy or Reserve Account Letter of Credit (if applicable); and (v) to reimburse or pay any provider of such facilities (if applicable) for any other amounts due under the agreement with such provider.

Any moneys held to the credit of the Surplus Account after all amounts described in the preceding paragraph required to be paid in respect of a Bond Year have been paid shall, upon the written request of the Corporation, be transferred to the credit of the Bond Service Account or the Redemption Account.

Reserve Account

If the resolution of the Board providing for the issuance of Bonds under the Trust Agreement requires that a Reserve Account be established, a separate account in the Sinking Fund designated "Reserve Account" is authorized to be created in accordance with said resolution, in which Reserve Account there shall be established separate subaccounts as provided in such resolution. In such event the Trustee shall, from the funds received by the Trustee in accordance with the Trust Agreement, prior to depositing any amounts to the credit of the Surplus Account, deposit to the credit of each subaccount within the Reserve Account such amount as may be required to make the amount then on deposit to the credit of each such subaccount equal to the amount established in such resolution of the Board. Any Reserve Accounts created under the Trust Agreement will be applicable to one or more Series of Bonds issued under the Trust Agreement as provided in the resolution of the Board authorizing any such Series.

Additional Bonds

Additional Bonds may be issued under and secured by the Trust Agreement, subject to certain conditions, at any time or times solely for the purpose of (i) purchasing any additional Notes from Government Development Bank, (ii) providing funds for refunding all or any part of the Outstanding Bonds of any one or more Series by payment at maturity or redemption at a selected redemption date or dates or combination of such payment at maturity and redemption, including the payment of any redemption premium thereon, (iii) making a deposit to a Reserve Account (if applicable), (iv) paying capitalized interest, and (v) paying the costs of issuance of such additional Bonds. No

additional Bonds may be issued unless the amounts of principal and interest payable under the Notes after the issuance of such additional Bonds are sufficient to pay the principal of and interest on all Bonds Outstanding after the issuance of such additional Bonds, together with other amounts required to be paid by the Corporation with respect to the Bonds, any Credit Facility or Liquidity Facility relating thereto, any Corporation Swap Payments and the Trust Agreement. In addition, no additional Bonds may be issued unless the GDB Letter of Credit is amended to change the stated amount, if necessary, or a successor letter of credit issued in favor of the Trustee is obtained, so that in either case the stated amount of the GDB Letter of Credit or such successor letter of credit is not less than the estimated Maximum Difference after the issuance of such additional Bonds as certified by the Corporation. Any successor letter of credit must be issued by a bank, banking association or trust company whose long-term debt obligations are rated at the time of issuance of the letter of credit in any of the three highest rating categories (without regard to any gradations within any such category) by Moody's and Standard & Poor's.

Investment of Moneys

Moneys held to the credit of the Bond Service Account and the Redemption Account (except any subaccounts established by one or more resolutions of the Board to segregate amounts received from a Credit Facility or a Liquidity Facility, which resolution or resolutions may provide for the investment of moneys deposited to the credit of any such subaccount) shall, as nearly as may be practicable, be continuously invested and reinvested, at the written direction of the Corporation specifying the particular investment to be made, in (i) Government Obligations that shall mature, or that shall be subject to redemption by the holder thereof at the option of such holder, not later than the respective dates when moneys held for the credit of said accounts will be required for the purposes intended; or (ii) Investment Agreements pursuant to which funds would be available not later than the respective dates when moneys held for the credit of said accounts would be required for the purposes intended. Moneys held to the credit of the Surplus Account shall be continuously invested and reinvested at the written direction of the Corporation in any Investment Obligations selected by it. Moneys held to the credit of the Reserve Account (if applicable) shall, as nearly as may be practicable, be continuously invested and reinvested at the written direction of the Corporation in Investment Obligations selected by it that shall mature no later than the final maturity of the Bonds.

Obligations so purchased as an investment of moneys in any such fund or account shall be deemed at all times to be a part of such fund or account, and any investment earnings and profit or loss realized on the sale or maturity thereof, shall be credited or debited to such fund or account; provided, however, that if the required deposit to any account in the Sinking Fund has been made for the current Bond Year, the investment earnings on moneys held to the credit of such account shall be deposited to the credit of any other account of the Sinking Fund for which such required deposit has not been made, in the order required by the Trust Agreement, and thereafter shall be deposited to the credit of such account in the Sinking Fund as shall be directed by the Corporation.

No Impairment

The Corporation covenants and agrees that, so long as any of the Bonds shall be Outstanding and so long as any of its other obligations under any Reimbursement Agreement (if applicable) or Swap Agreement (if applicable) shall remain unpaid, none of the Pledged Revenues will be used for any purpose other than as provided in the Trust Agreement, and that no contract or contracts will be entered into or any action taken by which the rights of the Trustee, the holders or such other parties secured by the Trust Agreement to such Pledged Revenues might be impaired or diminished.

Inclusion of Principal and Interest Requirement in Budget

Each year while any Bonds are Outstanding, the Corporation shall file a timely request with the Director of the Office of Management and Budget of Puerto Rico to include in the annual budget of capital improvements and operating expenses of the Commonwealth for the next Fiscal Year the necessary Legislative Appropriation so that payments in respect of the Notes shall be sufficient to cover the principal and interest payable with respect to the Bonds and all other amounts payable in respect of the Bonds or payable under the Trust Agreement during the Bond Year commencing within such Fiscal Year.

Enforcement of Remedies

At the request of the holders of not less than 20% of the aggregate principal amount of Bonds then Outstanding, the Trustee shall proceed, subject to the Trustee's rights to indemnification under the Trust Agreement, to protect and enforce its rights and the rights of the holders under the laws of Puerto Rico or under the Trust Agreement, including all rights with respect to the Notes and the Pledged Revenues, provided, that the Trustee may not sell or otherwise dispose of the Notes.

Pro Rata Application of Funds

If at any time the moneys in the Sinking Fund shall not be sufficient to pay the interest on or the principal of the Bonds as the same shall become due and payable, such moneys (except for any moneys obtained from a drawing on a Credit Facility, other than the GDB Letter of Credit, or Liquidity Facility (if applicable) and deposited in a separate subaccount which shall secure only one or more specified Series of Bonds or moneys deposited in any subaccount within the Reserve Account that secures only such specified Series of Bonds), together with any moneys then available or thereafter becoming available for such purpose, whether through the exercise of the remedies provided for in the Trust Agreement or otherwise, shall be applied as follows:

first, to the payment to the persons entitled thereto of all installments of interest then due and payable in the order in which such installments became due and payable and, if the amount available shall not be sufficient to pay in full any particular installment, then to the payment, ratably, according to the amounts due on such installment, to the persons entitled thereto, without any discrimination or preference except as to any difference in the respective rates of interest specified in such Bonds;

second, to the payment to the persons entitled thereto of the unpaid principal of any of the Bonds which shall have become due and payable (other than Bonds called for redemption for the payment of which moneys are held pursuant to the provisions of the Trust Agreement) in the order of their due dates, with interest on such Bonds at the respective rates specified therein from the respective dates upon which such Bonds became due and payable, and, if the amount available shall not be sufficient to pay in full the principal of such Bonds due and payable on any particular date, together with such interest, then to the payment first of such interest, ratably, according to the amount of such interest due on such date, and then to the payment of such principal, ratably, according to the amount of such principal due on such date, to the persons entitled thereto, without any discrimination or preference except as to any difference in the respective rates of interest specified in such Bonds;

third, to the payment of the interest on and the principal of such Bonds, to the purchase and retirement of Bonds and to the redemption of Bonds, all in accordance with the provisions of the Trust Agreement;

fourth, to the payment of any amounts then due and owing to a provider of a Credit Facility or a Liquidity Facility (if applicable); and

fifth, to the payment of any amounts then due and payable to a Hedge Counterparty under a Swap Agreement (if applicable).

Supplemental Agreements Without Bondholders' Consent

The Corporation and the Trustee may, without the consent or approval of, or notice to, any of the Bondholders, from time to time and at any time, enter into agreements supplemental to the Trust Agreement as shall not be inconsistent with the terms and provisions thereof, for the following purposes:

(a) to cure any ambiguity or formal defect or omission in the Trust Agreement or in any supplemental agreement or to correct or supplement any provision contained therein that may be defective or inconsistent with any other provisions contained therein; or

(b) to grant to or confer upon the Trustee for the benefit of the Bondholders any additional rights, remedies, powers, authority or security that may lawfully be granted to or conferred upon the Bondholders or the Trustee; or

(c) to add to the conditions, limitations and restrictions on the issuance of Bonds under the provisions of the Trust Agreement, other conditions, limitations and restrictions thereafter to be observed; or

(d) to add to the covenants and agreements of the Corporation in the Trust Agreement other covenants and agreements thereafter to be observed by the Corporation or to surrender any right or power therein reserved to or conferred upon the Corporation; or

(e) to permit the issuance of Bonds in coupon form; or

(f) to qualify the Bonds or any of the Bonds for registration under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended; or

(g) to qualify the Trust Agreement as an “indenture” under the Trust Indenture Act of 1939, as amended; or

(h) to make such changes as may be necessary to adjust the terms of the Trust Agreement so as to facilitate the issuance of Variable Rate Bonds, Capital Appreciation Bonds, Capital Appreciation and Income Bonds, Put Bonds, Interim Bonds and such other Bonds as may be marketable from time to time; or

(i) to make such changes as may be necessary to comply with the provisions of Puerto Rico law relating to the exclusion of interest on the Bonds from gross income thereunder; or

(j) to make such changes as may evidence the right and interest of an issuer of a Credit Facility or a Liquidity Facility that secures any Series of Bonds; or

(k) to make such changes as may be necessary to create a Reserve Account for any Bonds.

Modification with Consent of Holders of Majority of Bonds

Subject to the terms and provisions contained in the Trust Agreement, and not otherwise, the holders of not less than a majority in aggregate principal amount of the Bonds at the time Outstanding (or in case less than all of several Series of Bonds then Outstanding are affected by the proposed supplemental agreement, the holders of not less than a majority in principal amount of the Bonds of each Series so affected and Outstanding at the time the consent is given) shall have the right, from time to time, anything contained in the Trust Agreement to the contrary notwithstanding, to consent to and approve the execution by the Corporation and the Trustee of such agreement or agreements supplemental thereto as shall be deemed necessary or desirable by the Corporation for the purpose of modifying, altering, amending, adding to or rescinding, in any particular, any of the terms or provisions contained in the Trust Agreement or in any supplemental agreement; provided, however, that nothing contained in the Trust Agreement shall permit, or be construed as permitting, without the consent of the holders of 100% of the Bonds Outstanding affected by the proposed supplemental agreement (a) an extension of the time for the payment 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 any lien or a pledge of funds other than the lien and pledge created by the Trust Agreement, 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 agreement or any waiver under the Trust Agreement.

Amendments to the Notes

The Trustee (as assignee of the Notes) may, without the consent or approval of, or notice to any of the Bondholders, enter into, from time to time and at any time, such amendments to the Notes, in form satisfactory to the Trustee, as shall not be inconsistent with the terms and provisions thereof to (a) cure any ambiguity or formal defect or omission in the Notes, provided such action shall not materially adversely affect the interests of the Bondholders, or (b) grant to or confer upon the Corporation or Trustee for the benefit of the Bondholders any additional rights, remedies,

powers, authority or security that may lawfully be granted to or conferred upon the Corporation or Bondholders or the Trustee, or (c) provide for the substitution of any Notes for other notes of Authorized Debtors, provided that such substitution does not restrict, limit or reduce the obligation of the Authorized Debtors to make payments sufficient to pay the principal of and interest on the Bonds, or otherwise impair the security of the Bondholders of any Series of Bonds under the Trust Agreement, or (d) change the Applicable Percentage (as defined in the Notes) with respect to any Note, or (e) make any other change which, in the judgment of the Trustee, based upon an opinion of counsel, will not restrict, limit or reduce the obligation of the Authorized Debtors to make the payments under the Notes sufficient to pay the principal of or interest on the Bonds, or otherwise impair the security of the Bondholders under the Trust Agreement.

Except for amendments provided for in the preceding paragraph, the Trustee shall not enter into any amendment to the Notes unless notice of the proposed amendment shall have been given and the holders of not less than a majority in aggregate principal amount of the Bonds then Outstanding shall have consented to and approved the execution thereof, all as provided for under "Modification with Consent of Holders of Majority of Bonds" above; and provided further that without the consent of all of the holders of the Bonds Outstanding affected by such change, no such amendment shall be entered into by the Trustee which would restrict, limit or reduce the obligations of the Authorized Debtors with respect to the Bonds.

Supplements and Amendments to the GDB Letter of Credit

The Trustee, the Corporation and Government Development Bank may, without the consent or approval of, or notice to, any of the Bondholders, agree to and execute, from time to time and at any time, such amendments and supplements to the GDB Letter of Credit as shall not be inconsistent with the terms and provisions thereof, which amendments or supplements in the opinion of the Trustee, based upon an opinion of counsel, shall not be detrimental to the interests of the Holders of the Bonds to:

- (a) cure any ambiguity or formal defect or omission in the GDB Letter of Credit or in any supplement thereto,
- (b) grant to or confer upon the Trustee for the benefit of the Holders of the Bonds any additional rights, remedies, powers, authority or security that may lawfully be granted to or conferred upon the Holders of the Bonds or the Trustee, or
- (c) reduce the stated amount of the GDB Letter of Credit to the extent that the Maximum Difference is reduced, as certified by the President or any Executive Vice President of the Corporation, or
- (d) make any other change which, in the judgment of the Trustee, based upon an opinion of counsel, will not restrict, limit or reduce the obligation of Government Development Bank to make the payments under the GDB Letter of Credit to pay the principal of or interest on the Bonds or otherwise impair the security of the Holders of the Bonds under the Trust Agreement.

Except for supplements and amendments described above, the Trustee shall not agree to any supplement or amendment to the GDB Letter of Credit unless notice of the proposed execution of such supplement or amendment shall have been given to the Holders of the Bonds and the Holders of not less than a majority in aggregate principal amount of the Bonds at the time Outstanding shall have consented to and approved the execution thereof. Except as described above, nothing contained in the Trust Agreement shall permit or be construed as permitting any amendment or modification of any provision of the GDB Letter of Credit which would reduce the amount of any payment required to be made thereunder to the Trustee, or would postpone the time of any such payment, or would alter the conditions under which any such payment is made, or any other amendment or modification which would adversely affect the security of the Holders of the Bonds, as the case may be.

Defeasance

If all the Outstanding Bonds shall have been paid or deemed to have been paid as provided below and all amounts due and owing to any provider of a Credit Facility, Liquidity Facility or Rate Swap shall have been paid, then and in that case the right, title and interest of the Trustee under the Trust Agreement shall cease, terminate and become void, and such Bonds shall cease to be entitled to any benefit or security under the Trust Agreement. In such event, the

Trustee shall transfer and assign to the Corporation all property then held by the Trustee, shall execute such documents as may be reasonably required by the Corporation to evidence such transfer and assignment and shall turn over to the Corporation any surplus in any account in the Sinking Fund.

Any Outstanding Bond shall be deemed to have been paid within the meaning and with the effect expressed in the Trust Agreement when the whole amount of the principal of and interest on such Bond shall have been paid or when (a) there shall have been deposited with the Trustee or another fiduciary institution acting as escrow agent for the holder of such Bond either moneys in an amount which shall be sufficient, or Government Obligations, which shall not contain provisions permitting the redemption thereof at the option of the issuer, the principal of and interest on which when due, and without any reinvestment thereof, will provide moneys which, together with the moneys, if any, deposited with or held by the Trustee available therefor, shall be sufficient, to pay when due the principal of and premium, if any, and interest due and to become due on such Bond on or prior to the redemption date or maturity date thereof, as the case may be, and (b) in the event such Bond does not mature and is not to be redeemed within the next succeeding sixty 60 days, the Corporation shall have given the Trustee irrevocable instructions to give, as soon as practicable, a notice to the holder of such Bond by first-class mail, postage prepaid, stating that the deposit of moneys or Government Obligations has been made with the Trustee or another fiduciary institution acting as escrow agent for the holder of such Bond and that such Bond is deemed to have been paid in accordance with the Trust Agreement and stating such maturity or redemption date upon which moneys are to be available for the payment of the principal of and premium, if any, and interest on such Bond.

PROPOSED FORM OF OPINION OF BOND COUNSEL

Upon delivery of the 2001 Series E Bonds, Nixon Peabody LLP, Bond Counsel to the Corporation, proposes to issue its approving opinion with respect to the 2001 Series E Bonds in substantially the following form.

Puerto Rico Public Finance Corporation
San Juan, Puerto Rico

Ladies and Gentlemen:

We have acted as Bond Counsel in connection with the authorization and issuance by the Puerto Rico Public Finance Corporation (the "Corporation"), an independent governmental instrumentality of the Commonwealth of Puerto Rico (the "Commonwealth") created by Government Development Bank for Puerto Rico ("Government Development Bank") as a wholly-owned subsidiary pursuant to Resolution No. 5044, adopted by the Board of Directors of Government Development Bank on December 12, 1984, as amended ("Resolution No. 5044"), of its \$1,095,845,000 aggregate principal amount of Puerto Rico Public Finance Corporation 2001 Series E Bonds (the "2001 Series E Bonds"). Government Development Bank is a corporation and governmental instrumentality of the Commonwealth created pursuant to Act No. 17 of the Legislature of the Commonwealth approved September 23, 1948, as amended ("Act No. 17"), which, among other things, acts as the financial advisor and fiscal agent for the Commonwealth, its instrumentalities, commissions, authorities, municipalities and political subdivisions, and makes loans and advances funds to the Commonwealth and such entities.

The 2001 Series E Bonds are being issued under and pursuant to a Trust Agreement, dated December 27, 2001 (the "Trust Agreement"), by and between the Corporation and The Bank of New York, as trustee thereunder (the "Trustee"), and a Resolution of the Board of Directors of the Corporation adopted on December 19, 2001 authorizing the issuance and sale of the 2001 Series E Bonds (the "2001 Series E Bond Resolution"). The Corporation has heretofore issued on December 27, 2001 its Puerto Rico Public Finance Corporation 2001 Series C Bonds (the "2001 Series C Bonds") and Puerto Rico Public Finance Corporation 2001 Series D Bonds (the "2001 Series D Bonds," and together with the 2001 Series C Bonds and the 2001 Series E Bonds, the "Series 2001 Bonds") under and pursuant to the Trust Agreement and a Resolution of the Board of Directors of the Corporation adopted on December 19, 2001 authorizing the execution and delivery of the Trust Agreement and the issuance and sale of the 2001 Series C Bonds and 2001 Series D Bonds (the "2001 Series C and D Bond Resolution").

The Series 2001 Bonds have and are being issued to finance the Corporation's acquisition from Government Development Bank of several promissory notes (the "Series 2001 Notes") issued by certain departments, agencies, instrumentalities and public corporations of the Commonwealth ("Authorized Debtors") in connection with the restructuring and refinancing of certain outstanding loans made by Government Development Bank to such Authorized Debtors, to pay capitalized interest on such bonds and to pay costs of issuance in connection with the issuance of such bonds.

Pursuant to the Trust Agreement, the Corporation is authorized to issue additional series of bonds from time to time, upon the terms and conditions set forth therein, to purchase from Government Development Bank additional notes of other Authorized Debtors (such notes, together with the Series 2001 Notes, being referred to as the "Notes"), to refund the Series 2001 Bonds and any other bonds issued under the Trust Agreement, to fund a reserve account, to pay capitalized interest on any such additional bonds and to pay the costs of issuance of any such additional bonds; and any such bonds will be on a parity with the Series 2001 Bonds and all other bonds issued under the Trust Agreement (all such additional series of bonds, together with the Series 2001 Bonds, being herein collectively referred to as the "Bonds").

The principal of and the interest on the 2001 Series E Bonds and all other Bonds issued under the Trust Agreement are payable solely from the Pledged Revenues (as such term is defined in the Trust Agreement), consisting initially of payments of principal of and interest on the Series 2001 Notes and other funds held by the Trustee under the Trust Agreement. Upon the issuance of additional Bonds under the Trust Agreement for the purpose of providing funds to purchase additional Notes, the Pledged Revenues shall also include payments of principal of and interest on such additional Notes purchased. The principal of and interest on the Notes is payable solely from annual appropriations made by the Legislature of the Commonwealth pursuant to Act No. 164 of the Legislature of the Commonwealth, approved December 17, 2001 (the "Act").

The 2001 Series E Bonds are dated, mature, are payable, bear interest and are subject to redemption prior to maturity in the manner and upon the terms set forth in the 2001 Series E Bond Resolution and the Trust Agreement. The 2001 Series E Bonds are issuable in the form of fully registered bonds in denominations of \$5,000 each or any integral multiple thereof and will be initially registered in the name of Cede & Co., as registered owner and nominee for The Depository Trust Company, New York, New York, which will act as securities depository for the 2001 Series E Bonds.

As Bond Counsel, we have examined Act No. 17, Resolution No. 5044, the Act and such other law as we have deemed necessary or appropriate for the purposes of rendering the opinions set forth below. We have also examined originals or copies, certified or otherwise identified to our satisfaction, of such instruments, certificates and documents (including all documents constituting the Transcript of Proceedings with respect to the issuance of the 2001 Series E Bonds) as we have deemed necessary or appropriate for the purposes of rendering the opinions set forth below. In such examination, we have assumed the genuineness of all signatures, the authenticity and due execution of all documents submitted to us as originals and the conformity to the original documents of all documents submitted to us as copies. As to any facts material to our opinion, without having conducted any independent investigation, we have relied upon, and assumed the accuracy and truthfulness of, the aforesaid instruments, certificates and documents. In addition, in rendering the opinions set forth below, we have relied upon, among other things, certain representations, warranties and covenants made by the Corporation, Government Development Bank and the Authorized Debtors.

The Internal Revenue Code of 1986, as amended (the "Code"), establishes certain requirements that must be met subsequent to the issuance and delivery of the 2001 Series E Bonds in order that interest on the 2001 Series E Bonds be and remain excluded from gross income for Federal income tax purposes under Section 103 of the Code. The Corporation, Government Development Bank and the Authorized Debtors have each covenanted to comply with certain provisions and procedures pursuant to which the pertinent Code requirements can be satisfied. Noncompliance with such requirements may cause interest on the 2001 Series E Bonds to become includable in gross income for Federal income tax purposes retroactive to their date of issue, irrespective of the date on which such noncompliance is ascertained. In rendering our opinion below in respect of the Federal income tax treatment of interest on the 2001 Series E Bonds, we have assumed compliance with the aforementioned covenants.

Based upon the foregoing, we are of the opinion that:

1. Act No. 17 has been validly enacted and is in full force and effect, and Resolution No. 5044 has been duly adopted and is in full force and effect, and the Corporation is a duly constituted and existing subsidiary corporation of Government Development Bank and an independent governmental instrumentality of the Commonwealth.

2. The 2001 Series C and D Bond Resolution and the 2001 Series E Bond Resolution have each been validly and legally adopted.

3. As authorized by Resolution No. 5044 and the 2001 Series C and D Bond Resolution, the Trust Agreement has been duly executed and delivered.

4. The 2001 Series E Bonds have been duly authorized and issued, among other things, to provide funds for the purchase of the Series 2001 Notes.

5. The 2001 Series E Bonds are valid and binding obligations of the Corporation, payable solely from the Pledged Revenues.

6. The 2001 Series E Bonds do not constitute a debt of the Commonwealth, any of its public instrumentalities (other than the Corporation) or any of its municipalities or other political subdivisions, and neither the Commonwealth, any of its public instrumentalities (other than the Corporation) nor any of such municipalities or other political subdivisions are liable thereon.

7. Under existing laws, interest on the 2001 Series E Bonds is excludable from gross income for Federal income tax purposes and interest on the 2001 Series E Bonds is not an item of tax preference for purposes of the calculation of the alternative minimum tax imposed under the Code with respect to corporations and individuals. In addition, the 2001 Series E Bonds and interest thereon are exempt from Commonwealth, state and local income taxation.

8. Bond Counsel is further of the opinion that the difference between the principal amount of the 2001 Series E Bonds maturing on August 1, 2025, 2029 and 2030 (the "Discount Bonds"), and the initial offering price to the public (excluding bond houses, brokers, or similar persons or organizations acting in the capacity of underwriters or wholesalers) at which price a substantial amount of such Discount Bonds of each such maturity was sold constitutes original issue discount which is excluded from gross income for Federal income tax purposes to the same extent as interest on the 2001 Series E Bonds. Further, such original issue discount accrues actuarially on a constant interest rate basis over the term of each Discount Bond and the basis of each Discount Bond acquired at such initial offering price by an initial purchaser thereof will be increased by the amount of such accrued original issue discount. The accrual of original issue discount may be taken into account as an increase in the amount of tax-exempt income for purposes of determining various other tax consequences of owning the Discount Bonds, even though there will not be a corresponding cash payment.

9. The 2001 Series E Bonds maturing on August 1, 2026 and 2027 (the "Premium Bonds") are being offered at prices in excess of their principal amounts. Bond Counsel is of the opinion that an initial purchaser with an initial adjusted basis in a Premium Bond in excess of its principal amount will have amortizable bond premium which is not deductible from gross income for Federal income tax purposes. The amount of amortizable bond premium for a taxable year is determined actuarially on a constant interest rate basis over the term of each Premium Bond. For purposes of determining gain or loss on the sale or other disposition of a Premium Bond, an initial purchaser who acquires such obligation with an amortizable bond premium is required to decrease such purchaser's adjusted basis in such Premium Bond annually by the amount of amortizable bond premium for the taxable year. The amortization of bond premium may be taken into account as a reduction in the amount of tax-exempt income for purposes of determining various other tax consequences of owning the Premium Bonds.

In rendering this opinion, we are advising you that the enforceability of rights and remedies with respect to the 2001 Series E Bonds, the 2001 Series C and D Bond Resolution, the 2001 Series E Bond Resolution and the Trust Agreement may be limited by bankruptcy, insolvency, reorganization, moratorium and other laws affecting creditors' rights or remedies generally heretofore or hereafter enacted, and is subject to general principles of equity (regardless of whether such enforceability is considered in a proceeding in equity or at law).

Except as stated in paragraphs 7, 8 and 9 above, we express no opinion as to any other Federal, Commonwealth or state or local tax consequences of the ownership or disposition of the 2001 Series E Bonds. Furthermore, we express no opinion as to any Federal, Commonwealth, state or local tax law consequences with respect to the 2001 Series E Bonds, or the interest thereon, if any action is taken with respect to the 2001 Series E Bonds or the proceeds thereof upon the advice or approval of bond counsel other than ourselves.

We have examined the first executed 2001 Series E Bond and, in our opinion, the form of said 2001 Series E Bond and its execution are regular and proper.

Very truly yours,

GOVERNMENT DEVELOPMENT BANK FOR PUERTO RICO

The following information has been obtained from Government Development Bank. Neither the Corporation nor the Underwriters have verified such information, and they shall have no liability with respect to such information.

Government Development Bank is a government instrumentality of the Commonwealth created by Act No. 17 of the Legislature of Puerto Rico, approved September 13, 1948, as amended. Government Development Bank's primary purpose is to act as fiscal agent for the Commonwealth and its public entities. In that capacity, Government Development Bank acts as fiscal agent in connection with all short-term borrowings and bond issues of the Commonwealth, its public corporations and municipalities. In addition, Government Development Bank makes loans to the Commonwealth, its public corporations and municipalities, and to the private sector.

As of June 30, 2000, Government Development Bank had total assets of \$8.3 billion, total deposits of \$3.5 billion and capital of \$1.6 billion. For the year ended June 30, 2000, it reported net income of \$102.5 million.

As of June 30, 2001, Government Development Bank had total assets of \$7.8 billion, total deposits of \$3.2 billion and capital of \$1.7 billion. For the year ended June 30, 2001, it reported net income of \$84.9 million.

The principal offices of Government Development Bank are located at Minillas Government Center, De Diego Avenue, Stop 22, Santurce, Puerto Rico. For more detailed information on Government Development Bank, please refer to its Annual Report for the year ended June 30, 2000, a copy of which may be obtained by calling or writing to Director - New York Office, Government Development Bank for Puerto Rico, 140 Broadway, 38th Floor, New York, NY 10005, telephone number (212) 422-6420 or to Director - Public Finance Department, Government Development Bank for Puerto Rico, P.O. Box 42001, San Juan, PR 00940, telephone number (787) 722-4170. Upon request, Government Development Bank will furnish a copy of its Annual Report for the year ended June 30, 2001 when it becomes available.



Financial Guaranty Insurance Policy

Ambac Assurance Corporation
One State Street Plaza, 15th Floor
New York, New York 10004
Telephone: (212) 668-0340

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

\$1,095,845,000
Puerto Rico Public Finance Corporation
2001 Series E Bonds
(Commonwealth Appropriation Bonds)

SUPPLEMENT TO OFFICIAL STATEMENT

The following information supplements the information appearing in the Official Statement of Puerto Rico Public Finance Corporation dated December 19, 2001 relating to the offering of the captioned bonds (the "Official Statement").

Recent Developments Relating to the Projected General Fund Revenues and Expenditures of the Commonwealth of Puerto Rico for Fiscal Year 2002

The Commonwealth of Puerto Rico (the "Commonwealth") periodically monitors and revises its projected revenues and expenses. In the beginning of January 2002, in making its periodic review of revenues and expenditures, the Commonwealth became aware of a \$193 million reduction in the projected revenues from nonresident corporation income tax withholding. This reduction is due to the inclusion in the budget for fiscal year 2002 of a tax payment from a single taxpayer based on a similar tax payment received from that taxpayer in fiscal year 2001. The Commonwealth discovered that the fiscal year 2001 tax payment had included a prepayment of fiscal year 2002 taxes; therefore, a comparable tax payment may not be made by such taxpayer in fiscal year 2002.

To address this revenue reduction, the Commonwealth has identified certain non-recurring unbudgeted revenue sources to make up any potential budgetary shortfall. The use of one or more of these revenue sources may require the enactment of Commonwealth legislation. The Commonwealth currently projects General Fund revenues (excluding proceeds from special funds) to total \$7,485 million for fiscal year 2002.

Current projections of expenditures through the end of fiscal year 2002 indicate that they could exceed the budgeted amount by approximately \$160 million if corrective action is not taken. The Commonwealth anticipates that it will take corrective action in this regard to ensure a balanced budget by fiscal year end.

January 11, 2002