

\$628,110,000**Puerto Rico Highways and Transportation Authority****\$139,875,000 Grant Anticipation Revenue Bonds (Series 2004)****\$82,340,000 Transportation Revenue Refunding Bonds (Series I)****\$405,895,000 Transportation Revenue Bonds (Series J)**

The Grant Anticipation Revenue Bonds (Series 2004) (the “2004 Grant Anticipation Bonds”) are being issued by Puerto Rico Highways and Transportation Authority (the “Authority”) pursuant to Resolution No. 04-18 adopted by the Authority on April 7, 2004 (the “Grant Anticipation Resolution”) for the purpose of financing a portion of the costs of certain qualified federal aid transportation projects in the Commonwealth of Puerto Rico (the “Commonwealth”), to fund a Debt Service Reserve Fund (as defined herein) and to pay the costs of issuance of the 2004 Grant Anticipation Bonds. The 2004 Grant Anticipation Bonds are special and limited obligations of the Authority. The 2004 Grant Anticipation Bonds, together with any additional Grant Anticipation Revenue Bonds that are subsequently issued on a parity therewith, are payable from, and secured solely by a pledge of, the Trust Estate (as defined herein), which consists primarily of Federal Transportation Funds (as defined herein) that are paid or payable to the Authority or Trustee in accordance with Title 23 (as defined herein), and amounts on deposit in the Bond Payment Fund (as defined herein) and the Debt Service Reserve Fund and held by the Trustee.

The Transportation Revenue Refunding Bonds (Series I) (the “Series I Bonds”) and the Transportation Revenue Bonds (Series J) (the “Series J Bonds”) are being issued pursuant to Resolution No. 98-06 adopted by the Authority on February 26, 1998, as amended (the “1998 Resolution”) for the purpose of refunding certain of the Authority’s Transportation Revenue Bonds and to finance various highway projects. The Series I Bonds, the Series J Bonds, the outstanding bonds of the Authority previously issued under the 1998 Resolution and any additional bonds that the Authority may from time to time issue under the 1998 Resolution are payable from and are secured by a pledge of certain revenues of the Authority, which include: (i) the total amount of excise taxes, up to \$120 million per fiscal year, imposed by the Commonwealth on certain petroleum products; (ii) toll revenues on the Authority’s traffic facilities that were not financed with Highway Revenue Bonds issued under Resolution No. 68-18 (the “Highway Revenue Bonds”); (iii) certain investment earnings; and (iv) the following to the extent they are unencumbered and available after payment of debt service of the Authority’s outstanding Highway Revenue Bonds: (x) all current gasoline taxes, a portion of the current gas oil and diesel oil taxes and a portion of the current motor vehicle license fees allocated to the Authority by the Commonwealth, (y) all toll revenues of the Authority’s traffic facilities financed with Highway Revenue Bonds, and (z) certain investment earnings. All of the aforesaid revenues of the Authority that constitute taxes and license fees are subject to being applied first to the payment of general obligation debt of and debt guaranteed by the Commonwealth, if and to the extent that all other Commonwealth revenues are not sufficient therefor.

The 2004 Grant Anticipation Bonds, the Series I Bonds and the Series J Bonds (collectively the “Bonds”) will have the following characteristics:

- They will be dated their date of delivery.
- They will be registered under The Depository Trust Company’s book-entry only system. Purchasers of the Bonds will not receive definitive Bonds.
- Interest on the 2004 Grant Anticipation Bonds will be payable on each March 15 and September 15, commencing on September 15, 2004.
- Interest on the Series I Bonds and the Series J Bonds will be payable on each January 1 and July 1, commencing on July 1, 2004.
- The inside cover pages contain information concerning the maturity schedule, interest rates and prices or yields of the Bonds.
- The scheduled payment of principal and interest on some of the Bonds will be insured by MBIA Insurance Corporation and Financial Guaranty Insurance Company as indicated on the inside cover pages of this Official Statement.
- In the opinion of Bond Counsel, under existing federal laws and regulations, interest on the Bonds will be exempt from federal income taxation and the Bonds and interest thereon will be exempt from state, Commonwealth and local income taxation. However, see *Tax Exemption*, beginning on page 52 of this Official Statement for alternative minimum tax consequences with respect to interest on the Bonds, a description of certain rules that the Authority must comply with to preserve the federal tax exemption of interest, and other tax considerations.
- It is expected that settlement for the Bonds will occur on or about April 20, 2004.

The 2004 Grant Anticipation Bonds and the interest thereon do not constitute a debt of the Commonwealth or any of its political subdivisions, other than a special and limited obligation of the Authority payable solely from the Trust Estate (as defined herein). The owners of the 2004 Grant Anticipation Bonds may not look to any other revenues or funds of the Authority or the Commonwealth for payment of the 2004 Grant Anticipation Bonds.

The Series I Bonds and the Series J Bonds are not a debt of the Commonwealth or any of its political subdivisions, other than the Authority, and neither the Commonwealth nor any such subdivisions, other than the Authority, shall be liable thereon.

Citigroup

Merrill Lynch & Co.
Banc of America Securities LLC
Lehman Brothers
UBS Financial Services Inc.

Goldman, Sachs & Co.
Raymond James & Associates, Inc.

Morgan Stanley
JP Morgan
Samuel A. Ramirez & Co., Inc.
Wachovia Bank, National Association

\$628,110,000
Puerto Rico Highways and Transportation Authority

**\$139,875,000 Grant Anticipation
Revenue Bonds
Series 2004**

**\$82,340,000 Transportation
Revenue Refunding Bonds
Series I**

<u>Sept. 15</u>		<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Price or Yield</u>	<u>July 1</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield</u>	
2005	(M)	1,865,000	2½%	1.12%	2006	345,000	2½%	1.90%	
2005	(M)	4,225,000	2¼	1.12	2007	350,000	2¼	2.27	
2006	(M)	6,235,000	2¼	1.58	2008	360,000	2%	2.73	
2007	(M)	2,605,000	5	1.89	2009	(F)	370,000	2½	2.58
2007	(M)	3,770,000	2¼	1.89	2010	(F)	380,000	2.90	2.93
2008	(M)	1,125,000	5	2.28	2011	(F)	390,000	3⅛	3.21
2008	(M)	5,465,000	2¼	2.28	2012	(F)	400,000	3⅛	3.45
2009	(M)	6,770,000	2½	2.58	2013	(F)	415,000	3.60	3.62
2010	(M)	4,765,000	5	2.93	2014	(F)	430,000	3¾	3.78
2010	(M)	2,170,000	2.90	2.93	2015	(F)	445,000	3.80	3.89
2011	(M)	4,070,000	5	3.21	2016	(F)	465,000	3.90	3.98
2011	(M)	3,170,000	3⅛	3.21	2017	(F)	480,000	4	4.06
2012	(M)	6,400,000	5	3.45	2018	(F)	500,000	4.10	4.14
2012	(M)	1,140,000	3⅛	3.45	2019	(F)	520,000	4.20	4.23
2013	(M)	6,360,000	5	3.62	2020	(F)	540,000	4¼	4.31
2013	(M)	1,540,000	3.60	3.62	2021	(F)	565,000	4.30	4.39
2014	(M)(1)	3,975,000	5	3.75	2022	(F)(2)	13,645,000	5	4.45
2014	(M)	4,300,000	3¾	100	2023	(F)(2)	14,325,000	5	4.52
2015	(M)(1)	6,900,000	5	3.89	2024	(F)(2)	15,040,000	5	4.58
2015	(M)	1,730,000	3.80	3.89	2025	(F)(2)	15,790,000	5	4.59
2016	(M)(1)	8,740,000	5	3.98	2026	(F)(2)	16,585,000	5	4.61
2016	(M)	305,000	3.90	3.98					
2017	(M)(1)	6,540,000	5	4.06					
2017	(M)	2,950,000	4	4.06					
2018	(M)(1)	8,495,000	5	4.12					
2018	(M)	1,440,000	4.10	4.12					
2019	(M)(1)	9,520,000	5	4.20					
2019	(M)	900,000	4.20	100					
2020	(M)(1)	9,690,000	5	4.29					
2020	(M)	1,245,000	4¼	4.29					
2021	(M)(1)	9,620,000	5	4.36					
2021	(M)	1,850,000	4.30	4.36					

- (F) Insured by Financial Guaranty Insurance Company
- (M) Insured by MBIA Insurance Corporation
- (1) Priced to the first call date on March 15, 2014 at par.
- (2) Priced to the first call date on July 1, 2014 at par.
- (3) Term bond

**\$405,895,000 Transportation
Revenue Bonds
Series J**

<u>July 1</u>	<u>Principal Amount</u>	<u>Interest Rate</u>	<u>Yield</u>
2006	2,845,000	5%	1.90%
2006	1,050,000	2½	1.90
2007	2,905,000	5	2.27
2007	1,160,000	2½	2.27
2008	2,045,000	5	2.73
2008	2,195,000	2⅞	2.73
2009 (M)	4,400,000	2½	2.58
2010 (M)	4,510,000	5	2.93
2011 (M)	4,735,000	5	3.21
2012 (M)	4,970,000	5	3.43
2013 (M)	5,220,000	5	3.60
2014 (M)	5,480,000	5	3.76
2015 (M)(2)	5,755,000	5	3.89
2016 (M)(2)	6,040,000	5	3.98
2017 (M)(2)	6,345,000	5	4.06
2018 (M)(2)	6,660,000	5	4.14
2019 (F)(2)	6,995,000	5	4.23
2020 (F)(2)	7,345,000	5	4.31
2021 (2)	7,135,000	5½	4.68
2021	575,000	4⅞	4.68
2022 (2)	7,870,000	5½	4.73
2022	260,000	4.70	4.73
2023 (2)	8,320,000	5½	4.78
2023	255,000	4¾	4.78
2024 (2)	6,625,000	5½	4.85
2024	2,420,000	4.80	4.85
2029 (M)(2)(3)	52,630,000	5	4.64
2034 (3)	67,185,000	5	5.05
2039 (3)	85,945,000	5⅞	5.15
2043 (3)	86,020,000	5⅞	5.20

(F) Insured by Financial Guaranty Insurance Company

(M) Insured by MBIA Insurance Corporation

(1) Priced to the first call date on March 15, 2014 at par.

(2) Priced to the first call date on July 1, 2014 at par.

(3) Term bond

No dealer, broker, sales representative or other person has been authorized by the Authority or the Underwriters to give any information or to make any representations other than those contained herein and, if given or made, such other information or representations must not be relied upon as having been authorized by the Authority or any Underwriter. This Official Statement does not constitute an offer to sell or the solicitation of an offer to buy, nor shall there be any sale of the Bonds by any person, in any jurisdiction in which it is unlawful for such person to make such an offer, solicitation or sale. The information set forth herein has been obtained from the Authority 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 or condition of the Authority since the date hereof.

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

IN CONNECTION WITH THE OFFERING OF THE BONDS, THE UNDERWRITERS MAY EFFECT TRANSACTIONS WHICH STABILIZE OR MAINTAIN THE MARKET PRICES OF THE BONDS AND THE OUTSTANDING TRANSPORTATION REVENUE BONDS OF THE AUTHORITY AT LEVELS ABOVE THOSE WHICH MIGHT OTHERWISE PREVAIL ON THE OPEN MARKET. SUCH STABILIZING, IF COMMENCED, MAY BE DISCONTINUED AT ANY TIME.

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\$628,110,000
Puerto Rico Highways and Transportation Authority
\$139,875,000 Grant Anticipation Revenue Bonds (Series 2004)
\$82,340,000 Transportation Revenue Refunding Bonds (Series I)
\$405,895,000 Transportation Revenue Bonds (Series J)

INTRODUCTION

This Official Statement sets forth information in connection with the sale by Puerto Rico Highways and Transportation Authority (the “Authority”) of \$139,875,000 aggregate principal amount of its Puerto Rico Highways and Transportation Authority Grant Anticipation Revenue Bonds (Series 2004) (the “2004 Grant Anticipation Bonds”), \$82,340,000 aggregate principal amount of its Puerto Rico Highways and Transportation Authority Transportation Revenue Refunding Bonds (Series I) (the “Series I Bonds”) and \$405,895,000 aggregate principal amount of its Puerto Rico Highways and Transportation Authority Transportation Revenue Bonds (Series J) (the “Series J Bonds” and together with the 2004 Grant Anticipation Bonds and the Series I Bonds, the “Bonds”). The 2004 Grant Anticipation Bonds will be issued pursuant to Act No. 74 of the Legislature of Puerto Rico, approved June 23, 1965, as amended (the “Authority Act”), Resolution No. 04-18 adopted by the Authority on April 7, 2004 (the “Grant Anticipation Resolution”) and a resolution adopted by the Authority in connection with the 2004 Grant Anticipation Bonds (the “2004 Supplemental Resolution”). The Series I Bonds and the Series J Bonds (herein collectively called the “2004 Transportation Revenue Bonds”) will be issued pursuant to the Authority Act, Resolution No. 98-06 adopted by the Authority on February 26, 1998, as amended (the “1998 Resolution”), and a resolution adopted by the Authority in connection with the Series I Bonds and the Series J Bonds (the “2004 Transportation Revenue Bonds Resolution”). JPMorgan Chase Bank acts as fiscal agent under the 1998 Resolution (in such capacity, the “1998 Fiscal Agent”) and as trustee under the Grant Anticipation Resolution (in such capacity, the “Trustee”).

The scheduled payment of principal of and interest on the 2004 Grant Anticipation Bonds and the scheduled payment of principal of and interest on the Series J Bonds maturing on July 1, 2009 through July 1, 2018, inclusive, and the Series J Bond maturing on July 1, 2029 will be insured by municipal bond insurance policies (the “MBIA Bond Insurance Policy”) to be issued by MBIA Insurance Corporation (the “MBIA Insured Bonds”) concurrently with the delivery of the Bonds. The scheduled payment of principal of and interest of the Series I Bonds maturing on July 1, 2009 through July 1, 2026, inclusive, and the scheduled payment of principal of and interest on the Series J Bonds maturing on July 1, 2019 and July 1, 2020 will be insured by municipal bond insurance policies (the “FGIC Bond Insurance Policy”) to be issued by Financial Guaranty Insurance Company (the “FGIC Insured Bonds”) concurrently with the delivery of the Bonds. The MBIA Insured Bonds and the FGIC Insured Bonds are herein collectively called the “Insured Bonds.”

2004 Grant Anticipation Bonds

Under the Grant Anticipation Resolution, the Authority is authorized to issue bonds to finance certain transportation projects described below in anticipation of the receipt of revenues from the Federal Highway Administration (“FHWA”). The 2004 Grant Anticipation Bonds will be the first series of obligations issued by the Authority under the Grant Anticipation Resolution. The Authority may issue additional obligations under the Grant Anticipation Resolution on a parity with the 2004 Grant Anticipation Bonds to assist in financing other transportation construction projects.

The Authority has entered into certain grant agreements (the “Federal Aid Agreements”) with the FHWA relating to the construction of certain current transportation projects (current transportation projects are referred to herein as the “2004 Construction Projects” and, together with any future transportation projects the “Construction Projects”). Each of the 2004 Construction Projects qualifies to be financed with federal aid revenues received by or on behalf of the Authority under Title 23, defined below (the “Federal Transportation Funds”). The 2004 Grant Anticipation Bonds are being issued for the purpose of paying a portion of the costs of the 2004 Construction Projects, to fund a Debt Service Reserve Fund (as defined herein) for the 2004 Grant Anticipation Bonds and to pay the costs of issuing the 2004 Grant Anticipation Bonds. Under the Federal Aid Agreements, the FHWA has agreed to make payments to the Trustee, in an amount equal to the principal of and interest on the 2004 Grant Anticipation Bonds; when due, and the cost of replenishing the Debt Service Reserve Fund.

The Bond Payments (as defined in the Grant Anticipation Resolution) on the 2004 Grant Anticipation Bonds, and any additional Grant Anticipation Revenue Bonds (the “Additional Grant Anticipation Bonds”) that may be subsequently issued by the Authority on a parity with the 2004 Grant Anticipation Bonds (collectively, the “Grant Anticipation Bonds”), are payable from and secured solely by a pledge of the Trust Estate (as defined herein), which consists primarily of (i) Federal Transportation Funds that are paid to the Authority or Trustee in accordance with Title 23, United States Code, Highways, as amended and supplemented from time to time and any successor or replacement provision of law (“Title 23”), (ii) amounts on deposit in the Puerto Rico Highways and Transportation Authority Grant

Anticipation Revenue Bonds Bond Payment Fund (the “Bond Payment Fund”), and (iii) amounts that may be on deposit in a separate account within the Puerto Rico Highways and Transportation Authority Grant Anticipation Revenue Bonds Debt Service Reserve Fund (the “Debt Service Reserve Fund”) for the benefit of a particular Series of Bonds (collectively, the “Trust Estate”). The Bonds are special and limited obligations of the Authority. See “SECURITY AND SOURCES OF PAYMENT FOR THE 2004 GRANT ANTICIPATION BONDS.”

The 2004 Grant Anticipation Bonds and the interest thereon do not constitute a debt of the Commonwealth or any of its political subdivisions, other than a special and limited obligation of the Authority payable solely from the Trust Estate (as defined herein) which consists primarily of Federal Transportation Funds. The owners of the 2004 Grant Anticipation Bonds may not look to any other revenues or funds of the Authority or the Commonwealth for payment of the 2004 Grant Anticipation Bonds.

2004 Transportation Revenue Bonds

The Authority is issuing the Series I Bonds to refund a portion of the Authority’s Senior Transportation Revenue Bonds defined below and achieve debt service savings. The Authority is issuing the Series J Bonds to finance various highway projects included in the Authority’s current Construction Improvement Program.

The Authority has heretofore issued, pursuant to Resolution No. 68-18, adopted by the Authority on June 13, 1968, as amended (the “1968 Resolution”), Puerto Rico Highways and Transportation Authority Highway Revenue Bonds, of which \$1,850,105,000 principal amount was outstanding as of January 1, 2004 (said bonds, and any additional bonds that may be issued under the 1968 Resolution (subject to the limitations as to the issuance of such additional bonds contained in the 1998 Resolution, as hereinafter described) are herein collectively called the “Highway Revenue Bonds”).

The Authority has determined to finance most of its future capital requirements, after applying other available funds, through the issuance of bonds under the terms and conditions of the 1998 Resolution and has covenanted in the 1998 Resolution not to issue additional bonds under the 1968 Resolution, other than bonds whose maturity does not extend beyond July 1, 2036 and which are issued to refund outstanding Highway Revenue Bonds to achieve debt service savings. Under the 1998 Resolution, the Authority is authorized to issue bonds on a parity with the 2004 Transportation Revenue Bonds for any lawful purpose of the Authority. Pursuant to this authority, the Authority has heretofore issued Puerto Rico Highways and Transportation Authority Senior Transportation Revenue Bonds, of which \$3,015,559,096 principal amount (including accreted value for capital appreciation bonds as of January 1, 2004) was outstanding as of January 1, 2004 (the “Outstanding Senior Bonds”). The Outstanding Senior Bonds, the 2004 Transportation Revenue Bonds and any additional senior bonds issued under the 1998 Resolution, as described below, are herein collectively referred to as the “Senior Transportation Revenue Bonds.”

As described more fully below, the 1998 Resolution also permits the Authority to issue bonds subordinated in right of payment to the Senior Transportation Revenue Bonds for the purpose of financing transportation projects eligible for federal assistance. The outstanding subordinated bonds and any additional subordinated bonds issued under the 1998 Resolution as described below, are herein collectively referred to as the “Subordinated Transportation Revenue Bonds,” and said bonds, together with the Senior Transportation Revenue Bonds, are herein collectively called the “Transportation Revenue Bonds.”

All Highway Revenue Bonds will be secured equally and ratably under the 1968 Resolution and will be payable from 1968 Resolution Revenues (as defined below). All Senior Transportation Revenue Bonds will be secured equally and ratably under the 1998 Resolution and will be payable from 1998 Resolution Revenues (as defined below). All Subordinated Transportation Revenue Bonds will be secured equally and ratably under the 1998 Resolution (except for differences in any debt service reserve requirements related thereto as permitted by the 1998 Resolution) and will be payable from 1998 Resolution Revenues remaining after providing for the payment of debt service on Senior Transportation Revenue Bonds and providing the required debt service reserve therefor.

Based on the possibility that a significant portion of the Authority’s revenues would have to be used to pay general obligation bonds of the Commonwealth and bonds guaranteed by the Commonwealth in the unlikely event that other Commonwealth revenues are not sufficient to pay these general obligation bonds and Commonwealth guaranteed bonds, this Official Statement also incorporates by reference certain financial information relating to the Commonwealth, specifically (i) the Commonwealth’s Financial Information and Operating Data Report dated September 1, 2003 (the “Commonwealth Report”), which appears as Appendix I to the Official Statement of the Commonwealth, dated October 3, 2003 relating to the sale of its Public Improvement Bonds of 2004, Series A; and (ii) the Comprehensive Annual Financial Report of the Commonwealth for the fiscal year ended June 30, 2002, prepared by the Department of the Treasury of Puerto Rico (the “Commonwealth’s Annual Financial Report”), which includes the basic financial statements of the Commonwealth as of and for the fiscal year ended June 30, 2002, which financial statements have been audited by KPMG LLP, independent auditors, as stated in their report dated April 30, 2003, accompanying the financial statements.

KPMG LLP did not audit the financial statements of the Public Buildings Authority capital project fund (a major fund) and certain activities, funds and component units separately identified in their report. Those financial statements were audited by other auditors whose reports have been furnished to KPMG LLP, and their opinion as to the basic financial statements, insofar as it relates to the amounts included in the basic financial statements pertaining to such activities, funds and component units, is based solely on the reports of the other auditors.

Any official statement of the Commonwealth or of any instrumentality of the Commonwealth filed with each nationally recognized municipal securities information repository ("NRMSIR") and with the Municipal Securities Rulemaking Board ("MSRB"), or any other document filed with each NRMSIR, after the date hereof and prior to the termination of the offering of the Bonds, which supplements or amends the information appearing in the Commonwealth Report 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 or in any of the above described documents 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.

As of January 1, 2004 the aggregate outstanding debt of the Authority, including outstanding Highway Revenue Bonds, Senior Transportation Revenue Bonds, Subordinated Transportation Revenue Bonds and certain notes payable to Government Development Bank for Puerto Rico ("Government Development Bank") amounted to \$5,289,412,870 including accreted value for capital appreciation bonds as of January 1, 2004.

This Official Statement describes the terms of and security for the Bonds and the use of proceeds of the Bonds. Also included are summaries and description of certain provisions of the 1968 Resolution, the 1998 Resolution, the Grant Anticipation Resolution, and Title 23. These descriptions and summaries do not purport to be comprehensive or definitive. All references herein to the 1968 Resolution, the 1998 Resolution and the Grant Anticipation Resolution, are qualified in their entirety by reference to the definitive form thereof, all references to Federal and Commonwealth laws are qualified in their entirety by reference to the complete statutes, regulations and published interpretations by Federal or Commonwealth officials, and all references to the Bonds are qualified by the forms thereof contained in corresponding resolution and are further qualified in their entirety by reference to laws and principles of equity relating to or affecting the enforceability of creditors' rights.

This Official Statement, including information incorporated in this Official Statement by reference, contains certain "forward-looking statements" concerning the operations, financial condition, plans and objectives of the Authority and the Commonwealth. These statements are based upon a number of assumptions and estimates which are subject to significant uncertainties, including general economic conditions, many of which are beyond the control of the Authority and 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.

Capitalized terms used herein but not otherwise defined herein have the meanings assigned to them in the summaries of the Grant Anticipation Resolution and the 1998 Resolution provided in Appendices III and IV, respectively.

2004 GRANT ANTICIPATION BONDS FINANCING PLAN

2004 Grant Anticipation Bonds

The Authority is issuing the 2004 Grant Anticipation Bonds to (i) fund a portion of the costs of the design, acquisition and/or construction of the 2004 Construction Projects, (ii) fund the 2004 Debt Service Reserve Account of the Debt Service Reserve Fund and (iii) pay the costs of issuance of the 2004 Grant Anticipation Bonds.

2004 Construction Projects

The FHWA has authorized the 2004 Construction Projects as advance construction projects under Title 23 and has determined that the 2004 Construction Projects are eligible for federal aid revenues under Title 23. Proceeds from the 2004 Grant Anticipation Bonds are expected to fund up to 80% of the total cost of the 2004 Construction Projects. Under the Federal Aid Agreements, executed or expected to be executed, the Authority is responsible for paying the remaining costs of the 2004 Construction Projects. The Authority expects to use general revenues and the proceeds of other borrowings for this purpose.

The FHWA has agreed under the Federal Aid Agreements to make payments to the Trustee in amounts sufficient to make the Bond Payments, when due. The FHWA will not reimburse the Trustee for any additional amounts, including interest that may be due on the 2004 Grant Anticipation Bonds as a result of any delays in the payments to be made under the Federal Aid Agreements. Such payments shall be used by the Trustee under Title 23 and the terms of the Federal Aid Agreements and the Grant Anticipation Resolution to make Bond Payments on the 2004 Grant Anticipation Bonds. As required by Title 23, the 2004 Construction Projects have been included in the Commonwealth transportation improvement program (the "STIP"). Each of the 2004 Construction Projects constitutes a Qualified Federal Aid Transportation Project, as that term is defined in the Grant Anticipation Resolution. See "INFORMATION CONCERNING THE FUNDING OF FEDERAL-AID HIGHWAYS." Under the Grant Anticipation Resolution, the Authority has covenanted to comply with applicable law and the Federal Aid Agreements to the extent required in order to receive required amounts from the FHWA under the Federal Aid Agreements.

The 2004 Construction Projects consist of the design, acquisition and/or construction by the Authority of the following projects:

- Conversion to expressway of the following sections of PR-2 (Mayaguez to Ponce): overpass intersection of PR-2 and PR-345; intersection of PR-2 and PR-347 (Km. 168.8 to 170.9); intersection of PR-2 and Castro Perez Ave. (Km. 174.1 to 176.7); intersection of PR-2 and PR-360 (Km. 172.9 to 174.1); Km. 217.2 to Km. 219.5; overpass intersection PR-2 Km. 215.8 with Municipal Road; overpass intersection (Km. 220.5 to Km. 222.3); overpass intersection of PR-2 Km. 222.5.
- Overpass intersection of PR-3 and PR-853 (Carolina).
- Overpass intersections of PR-12 in Ponce with Plaza del Caribe entrance and with Caribe Avenue.
- Connector from PR-2 (Km. 39.5) to PR-686, (Km. 16.0) (Vega Baja).
- Bridge over Ensenada Channel and connector (Culebra).

Sources and Uses of Proceeds of the 2004 Grant Anticipation Bonds

Sources:

Principal Amount of 2004 Grant Anticipation Bonds	\$139,875,000.00
Net Original Issue Premium.....	7,482,452.60
Total Sources.....	<u>\$147,357,452.60</u>

Uses:

Deposit into 2004 Construction Fund.....	\$133,376,000.00
Deposit into 2004 Debt Service Reserve Account	12,035,187.50
Underwriting discount and legal, printing, bond insurance and other financing expenses.....	1,946,265.10
Total Uses.....	<u>\$147,357,452.60</u>

SERIES I BONDS FINANCING PLAN

The Authority is issuing the Series I Bonds to (i) refund a portion of the Authority’s Senior Transportation Revenue Bonds in the amounts and maturities identified in the table below (the “Refunded Bonds”) and (ii) pay costs of issuance of the Series I Bonds. See “Issuance of Additional Bonds” in “APPENDIX IV - SUMMARY OF CERTAIN PROVISIONS OF THE 1998 RESOLUTION.”

Refunded Bonds	Maturity Date	Interest Rate	Principal Amount to be Refunded	Redemption Date	Redemption Price
2000 Series B	07/01/05	5.000 %	\$ 3,400,000		
	07/01/26	6.000	73,580,000	07/01/05	101.0 %

Sources and Uses of Proceeds of the Series I Bonds

Sources:

Principal Amount of Series I Bonds.....	\$82,340,000.00
Net Original Issue Premium.....	2,685,831.15
Other available moneys.....	1,146,200.00
Total Sources.....	<u>\$86,172,031.15</u>

Uses:

Deposit into Escrow Fund.....	\$83,142,815.62
Underwriting discount and legal, printing, bond insurance, and other financing expenses.....	3,029,215.53
Total Uses.....	<u>\$86,172.031.15</u>

The Authority will deposit the net proceeds of the Series I Bonds, together with other available moneys, with the 1998 Fiscal Agent, as escrow agent, under the terms of an escrow deposit agreement. The net proceeds, together with such other moneys, will be invested in Government Obligations (as defined in the 1998 Resolution) the principal of and interest on which when due, together with any moneys deposited with the 1998 Fiscal Agent remaining uninvested, will provide moneys sufficient to pay the interest coming due on the Refunded Bonds through their dates of redemption and to pay the principal of and premium, if any, on the Refunded Bonds on their dates of redemption. The sufficiency of the amount so deposited, with investment earnings thereon, to accomplish the refunding of the Refunded Bonds will be verified by The Arbitrage Group, Inc. (the “Verification Agent”).

Upon the deposit with the 1998 Fiscal Agent referred to above, the Refunded Bonds will, in the opinion of Bond Counsel, no longer be deemed to be outstanding under the 1998 Resolution and the Refunded Bonds will thereupon be defeased.

SERIES J BONDS FINANCING PLAN

The Authority is issuing the Series J Bonds to (i) finance or refinance various highway projects included in the Authority's current Construction Improvement Program, (ii) make a deposit to the 1998 Senior Bond Reserve Account, (iii) make a deposit to the 1998 Senior Bond Service Account to be applied to pay interest on the Series J Bonds and (iv) pay costs of issuance of the Series J Bonds. See "Operating Expenses and Capital Expenditures – Construction Improvement Program" under "TRANSPORTATION SYSTEM REVENUES AND EXPENDITURES."

Sources and Uses of Proceeds of the Series J Bonds

Sources:

Principal Amount of Series J Bonds.....	\$405,895,000.00
Net Original Issue Premium.....	7,550,647.10
Total Sources.....	\$413,445,647.10

Uses:

Deposit into 1998 Construction Fund.....	\$360,000,000.00
Deposit into 1998 Senior Bond Reserve Account.....	24,275,575.00
Deposit into 1998 Senior Bond Service Account.....	22,104,922.85
Underwriting discount and legal, bond insurance, printing, and other financing expenses.....	7,065,149.25
Total Uses.....	\$ 413,445,647.10

THE BONDS

General

The Bonds will be issued as registered bonds without coupons, will be dated, will bear interest at the rates, will be payable at the times, and will mature on the dates and in the principal amounts set forth on the inside cover pages of this Official Statement. Principal and interest on the Bonds will be calculated on the basis of a 360-day year consisting of twelve 30-day months and will be payable in the manner described below in "Book-Entry Only System".

Principal and Interest

2004 Grant Anticipation Bonds. The principal of the 2004 Grant Anticipation Bonds shall be payable in lawful money of the United States of America at the designated corporate trust office of the Trustee. Interest on the 2004 Grant Anticipation Bonds shall be payable on the fifteenth day of each March and September, commencing on September 15, 2004, to the person whose name appears on the registration books of the Trustee on the first day of the month in which payment is due.

Series I Bonds and Series J Bonds. The principal and premium, if any, on the Series I Bonds and Series J Bonds shall be payable in lawful money of the United States of America at the designated office of the 1998 Fiscal Agent. Interest on the Series I Bonds and Series J Bonds will be payable on the first day of each January and July, commencing on July 1, 2004, to the person whose name appears on the registration books of the 1998 Fiscal Agent as the registered owner thereof on the 15th day of the month immediately preceding the month in which payment is due.

Redemption of 2004 Grant Anticipation Bonds

The 2004 Grant Anticipation Bonds maturing on or after September 15, 2014 may be redeemed on any date on or after March 15, 2014 at the option of the Authority, either in whole or in part (and, if in part, in such order of maturities as the Authority may direct), at a redemption price equal to the principal amount of the Bonds to be redeemed plus accrued interest to the redemption date, without premium. The 2004 Grant Anticipation Bonds will not be subject to any mandatory redemption or amortization requirement.

If less than all of the 2004 Grant Anticipation Bonds of any one maturity shall be called for redemption, the particular Bonds or portions thereof to be redeemed shall be selected by the Trustee, in such manner as it in its discretion may determine to be appropriate and fair.

Redemption of Series I Bonds

The Series I Bonds maturing on or after July 1, 2015 may be redeemed on any date on or after July 1, 2014 at the option of the Authority, either in whole or in part (and, if in part, in such order of maturities as the Authority may direct), from any available moneys (other than moneys deposited in the 1998 Senior Bond Sinking Fund in respect of an Amortization Requirement) at a redemption price equal to the principal amount of the Bonds to be redeemed plus accrued interest to the redemption date, without premium. The Series I Bonds will not be subject to any mandatory redemption or amortization requirement.

If less than all of the Series I Bonds of any one maturity shall be called for redemption, the particular Series I Bonds or portions thereof to be redeemed shall be selected by the 1998 Fiscal Agent, in such manner as it in its discretion may determine to be appropriate and fair.

Redemption of Series J Bonds

The Series J Bonds maturing on or after July 1, 2015 may be redeemed on any date on or after July 1, 2014 at the option of the Authority, either in whole or in part (and, if in part, in such order of maturities as the Authority may direct), from any available moneys (other than moneys deposited in the 1998 Senior Bond Sinking Fund in respect of an Amortization Requirement) at a redemption price equal to the principal amount of the Bonds to be redeemed plus accrued interest to the redemption date, without premium.

The Series J Bonds maturing on July 1, 2029, July 1, 2034, July 1, 2039 and July 1, 2043 are subject to redemption on each July 1 immediately after the fiscal year for which there is an Amortization Requirement to the extent of the Amortization Requirement for said bonds (less the amount of bonds retired by purchase from moneys in the 1998 Senior Bond Sinking Fund) from moneys in the 1998 Senior Bond Sinking Fund at par plus accrued interest in the years and amounts set forth below:

Amortization Requirements for Series J Bonds due July 1,				
Year	2029	2034	2039	2043
2025	\$ 9,525,000			
2026	10,000,000			
2027	10,500,000			
2028	11,025,000			
2029	11,580,000*			
2030		\$12,160,000		
2031		12,765,000		
2032		13,405,000		
2033		14,075,000		
2034		14,780,000*		
2035			\$15,515,000	
2036			16,310,000	
2037			17,145,000	
2038			18,025,000	
2039			18,950,000*	
2040				\$19,920,000
2041				20,940,000
2042				22,015,000
2043				23,145,000*
Average life (years)	23.30	28.30	33.30	37.76

* Maturity.

If less than all of the Series J Bonds of any one maturity shall be called for redemption, the particular Series J Bonds or portions thereof to be redeemed shall be selected by the 1998 Fiscal Agent, in such manner as it in its discretion may determine to be appropriate and fair.

Book-Entry Only System

The following information concerning The Depository Trust Company (“DTC”) and DTC’s book-entry system has been obtained from sources the Authority believes to be reliable but neither the Authority nor the Underwriters take any responsibility for the accuracy thereof. The Owners should confirm this information with DTC or the DTC Participants.

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

DTC, the world’s largest depository, is a limited-purpose trust company organized under the New York Banking Law, a “banking organization” within the meaning of the New York Banking Law, a member of the Federal Reserve System, a “clearing corporation” within the meaning of the New York Uniform Commercial Code, and a “clearing agency” registered pursuant to the provisions of Section 17A of the Securities Exchange Act of 1934. DTC holds and provides asset servicing for over 2 million issues of U.S. and non-U.S. equity issues, corporate and municipal debt issues, and money market instruments from over 85 countries that DTC’s participants (the “Direct Participants”) deposit with DTC. DTC also facilitates the post-trade settlement among Direct Participants of sales and other securities transactions in deposited securities through electronic computerized book-entry transfers and pledges between Direct Participants’ accounts. This eliminates the need for physical movement of securities certificates. Direct Participants include both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, clearing corporations, and certain other organizations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation (“DTCC”). DTCC, in turn, is owned by a number of Direct Participants of DTC and Members of the National Securities Clearing Corporation, Government Securities Clearing Corporation, MBS Clearing Corporation, and Emerging Markets Clearing Corporation, (NSCC, GSCC, MBSCC, and EECC, also subsidiaries of DTCC), as well as by the New York Stock Exchange, Inc., the American Stock Exchange LLC, and the National Association of Securities Dealers, Inc. Access to the DTC system is also available to others such as both U.S. and non-U.S. securities brokers and dealers, banks, trust companies, and clearing corporations that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly (“Indirect Participants”). DTC has Standard & Poor’s highest rating: AAA. The DTC Rules applicable to its Participants are on file with the Securities and Exchange Commission. More information about DTC can be found at www.dtcc.com.

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

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

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants to 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.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to the Bonds unless authorized by a Direct Participant in accordance with DTC’s Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Authority as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.’s consenting or voting rights to those Direct Participants to whose accounts the 2004 Grant Anticipation Bonds are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and interest payments on the Bonds will be made to Cede & Co. or to such other nominee as may be requested by an authorized representative of DTC. DTC’s practice is to credit Direct Participants’ accounts upon DTC’s

receipt of funds and corresponding detail information from the Authority, 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 Authority, the Trustee, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal and interest to Cede & Co. (or such other nominee as may be requested by an authorized representative of DTC) is the responsibility of the Authority, or the 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.

DTC may discontinue providing its services as securities depository with respect to the Bonds at any time by giving reasonable notice to the Authority, or the 1998 Fiscal Agent and the Trustee. Under such circumstances, in the event that a successor securities depository is not obtained, definitive Bonds are required to be printed and delivered.

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

Payments and Transfers

No assurance can be given by the Authority that DTC will make prompt transfer of payments to the Direct Participants or that Direct Participants will make prompt transfer of payments to Indirect Participants or to Beneficial Owners. The Authority is not responsible or liable for payment by DTC or Participants or for sending transaction statements or for maintaining, supervising or reviewing records maintained by DTC or Participants.

The Authority, the 1998 Fiscal Agent and the Trustee will have no responsibility or obligation to such Direct Participants, Indirect Participants, or the persons for whom they act as nominees with respect to the payments to or the providing of notice for the Direct Participants, the Indirect Participants, or the Beneficial Owners. Payments made to DTC or its nominee shall satisfy the obligations of the Authority to the extent of such payments.

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

Discontinuance of Book-Entry Only System

In the event that such book-entry only system is discontinued for the Bonds, the following provisions will apply to the Bonds: principal of the Bonds will be payable in lawful money of the United States of America at the principal corporate trust office of the Trustee, in New York, New York. Interest on the Bonds will be payable on each March 15 and September 15 in the case of the 2004 Grant Anticipation Bonds and on each January 1 and July 1 in the case of the 2004 Transportation Revenue Bonds, by check mailed to the respective addresses of the registered owners thereof as shown on the registration books of the Authority maintained by the Trustee or the 1998 Fiscal Agent, as applicable, as of the close of business on the record date therefor as set forth in the Grant Anticipation Resolution or the 1998 Resolution, as applicable. The Bonds will be issued only as registered bonds without coupons in authorized denominations. The transfer of the Bonds will be registrable and the Bonds may be exchanged at the principal corporate trust office of the Trustee or the 1998 Fiscal Agent, in New York, New York upon the payment of any taxes or other governmental charges required to be paid with respect to such transfer or exchange.

The Authority will have no responsibility or obligation to DTC, to direct participants or to indirect participants with respect to (1) the accuracy of any records maintained by DTC, any direct participant, or any indirect participant; (2) any notice that is permitted or required to be given to the owners of the Bonds under the Grant Anticipation Resolution or the 1998 Resolution, as applicable; (3) the selection by DTC or any participant or indirect participant of any person to receive payment in the event of a partial redemption of the Bonds; (4) the payment by DTC or any direct participant or indirect participant of any amount with respect to the principal or redemption premium, if any, or interest due with respect to the Bonds; (5) any consent given or other action taken by DTC as the owner of the Bonds; or (6) any other matters.

SECURITY AND SOURCES OF PAYMENT FOR THE 2004 GRANT ANTICIPATION BONDS

Nature of Obligations

The 2004 Grant Anticipation Bonds are special and limited obligations of the Authority and are payable solely from the sources specified in the Grant Anticipation Resolution. The 2004 Grant Anticipation Bonds and the payment of Bond Payments thereon are not general obligations of the Authority and shall not be payable out of any moneys of the Authority other than the Trust Estate. The 2004 Grant Anticipation Bonds are not obligations, general, special or otherwise, of the Commonwealth, do not constitute a debt of the Commonwealth or any of its political subdivisions nor shall payment thereof be enforceable out of any moneys of the Commonwealth other than Federal Transportation Funds.

The Grant Anticipation Resolution authorizes the Authority to issue one or more series of Grant Anticipation Bonds to finance Construction Projects after the Authority has entered into Federal Aid Agreements with FHWA to reimburse the Authority for the federally-eligible costs of such projects. Pursuant to the 2004 Supplemental Resolution, the Authority will issue the 2004 Grant Anticipation Bonds in anticipation of the receipt by the Authority of the federal aid revenues received by or on behalf of, or available to, the Authority pursuant to Title 23, any extension of Title 23 or any successor to Title 23 that are legally available for the payment of Bond Payments and Construction Costs (as defined in the Grant Anticipation Resolution).

Creation of a Trust Estate

The Grant Anticipation Resolution shall constitute a contract between the Authority and the owners of the Grant Anticipation Bonds, and the pledge, covenants and agreements of the Authority set forth in the Grant Anticipation Resolution shall be for the equal benefit, protection and security of the owners of any and all of the Grant Anticipation Bonds, all of which, regardless of time or times of their issuance or maturity, shall be of equal rank without preference, priority or distinction of any of the Grant Anticipation Bonds over any other Grant Anticipation Bond, except as expressly provided in or permitted by the Grant Anticipation Resolution. The pledge by the Authority of the Trust Estate, which consists primarily of all Federal Transportation Funds that are paid to the Authority or the Trustee in accordance with Title 23, and amounts on deposit in the Bond Payment Fund and amounts on deposit in a separate account within the Debt Service Reserve Fund for the benefit of a particular Series of Grant Anticipation Bonds, is irrevocable so long as any Grant Anticipation Bonds are Outstanding under the terms of the Grant Anticipation Resolution.

The assignment and pledge of Federal Transportation Funds to the Trustee for the benefit of the owners of the Grant Anticipation Bonds under the Grant Anticipation Resolution shall constitute a first priority lien on such Federal Transportation Funds received by the Authority or the Trustee.

The remedies available to the Trustee and the owners of the 2004 Grant Anticipation Bonds upon an Event of Default (as defined in the Grant Anticipation Resolution) do not include the right to declare all amounts immediately due and payable and are in many respects dependent upon regulatory and judicial actions which are often subject to discretion and delay. Such remedies may also not be readily available or may be limited and the legal opinions rendered in connection with this financing will be qualified to the extent that enforceability of provisions of such agreements are affected by such limitations, including as such enforceability may be limited by bankruptcy, insolvency or other laws generally affecting creditors' rights.

Deposits of Federal Transportation Funds as Pledged Funds

The Authority has entered into Federal Aid Agreements with the FHWA. Under the provisions of the Federal Aid Agreements, the FHWA has agreed to make payments of Federal Transportation Funds in amounts equal to the Bond Payments, when due, on the 2004 Grant Anticipation Bonds. An owner of a 2004 Grant Anticipation Bond may not compel the payment of Federal Transportation Funds to the Authority. Title 23 provides that such Federal Aid Agreements do not create any right in any party (other than the Authority) against the FHWA and do not constitute a commitment, guarantee or obligation on the part of the United States to provide for the payment of Bond Payments on the 2004 Grant Anticipation Bonds.

For a discussion of the authorization of Federal Transportation Funds see "INFORMATION CONCERNING THE FUNDING OF FEDERAL-AID HIGHWAYS" and for information concerning the amount of Federal Transportation Funds received by the Authority see "FEDERAL AID REVENUES."

The Assignment Agreement

The Department of Transportation and Public Works (the “Department”) and the Authority have entered into an Assignment Agreement dated as of March 30, 2004, (the “Assignment Agreement”) pursuant to which the Department reaffirmed the designation of the Authority as the exclusive agency of the Commonwealth to receive Federal Transportation Funds and to carry out the responsibilities of expending said funds in accordance with the provisions of Title 23. The Department has covenanted in the Assignment Agreement that such designation shall be irrevocable for as long as any Bonds remain outstanding under the Grant Anticipation Resolution.

Funds and Accounts

The Grant Anticipation Resolution creates the Bond Payment Fund, the Debt Service Reserve Fund, the Construction Fund and an Earnings Account within the Construction Fund, and a Rebate Fund. The Bond Payment Fund and amounts on deposit in that fund are part of the Trust Estate, but the Construction Fund (including the Earnings Account), the Rebate Fund and amounts on deposit in those funds and accounts are not part of the Trust Estate and, therefore, are not pledged to the payment of the Grant Anticipation Bonds. Amounts in each account of the Debt Service Reserve Fund shall be pledged to the payment of the related Series of Grant Anticipation Bonds.

Bond Payment Fund. The Trustee is required to create and maintain separate accounts identified by the appropriate series designation within the Bond Payment Fund to account for the receipt of moneys to pay, and the payment of, the Bond Payments on and Redemption Price of each Series of Grant Anticipation Bonds, but such separate accounts shall not affect the rights of the owners of the Grant Anticipation Bonds with respect to moneys in the Bond Payment Fund.

Debt Service Reserve Fund. Each supplemental resolution authorizing the issuance of a Series of Grant Anticipation Bonds may provide for the establishment of an account in the Debt Service Reserve Fund related to such Series of Grant Anticipation Bonds which shall be funded pursuant to the terms of such supplemental resolution. Amounts in each account in the Debt Service Reserve Fund shall be used to pay debt service on the related Series of Grant Anticipation Bonds on the date such debt service is due when insufficient funds for that purpose are available in the Bond Payment Fund. In lieu of or in substitution for any moneys deposited in an account in the Debt Service Reserve Fund, the Authority may, as provided in the corresponding supplemental resolution, deposit or cause to be deposited with the Trustee a Reserve Account Credit Facility. Each account of the Debt Service Reserve Fund shall be subject to restoration by the Authority up to its corresponding Series Debt Service Reserve Requirement from Federal Transportation Funds.

Construction Fund. Proceeds of each Series of Grant Anticipation Bonds are, except proceeds used to fund the Debt Service Reserve Fund, to be deposited into the Construction Fund and amounts on deposit in the Construction Fund (including the Earnings Account) may be applied by the Authority to pay costs of issuance and, so long as no payment default has occurred with respect to the Grant Anticipation Bonds, may be requisitioned by the Authority for Construction Costs in the manner provided by the Grant Anticipation Resolution. In the event of a payment default with respect to the Grant Anticipation Bonds, the Executive Director of the Authority may direct, in his or her discretion, that the amounts in the Construction Fund (including the Earnings Account) be transferred to the Bond Payment Fund, but no such transfers are required.

Rebate Fund. Amounts may be deposited into the Rebate Fund from Federal Transportation Funds, from amounts in the funds and accounts held under the Grant Anticipation Resolution or from any other legally available source and, to the extent necessary, are to be applied to make rebate payments to the United States in accordance with the Tax Certificates. Any excess in the Rebate Fund may be transferred to the Bond Payment Fund, the Construction Fund, the Debt Service Reserve Fund or to the Authority.

Federal Transportation Funds. The assignment and pledge of Federal Transportation Funds to the Trustee for the benefit of the owners of the Grant Anticipation Bonds under the Grant Anticipation Resolution constitutes a first priority lien on the Federal Transportation Funds received by the Authority or the Trustee. The Federal Transportation Funds received by the Authority or the Trustee are required by the Grant Anticipation Resolution to be deposited and used only in the manner and order of priority specified below.

Flow of Funds. Deposits are first made into the Bond Payment Fund, and amounts on deposit in an account of the Bond Payment Fund may be used only to pay Bond Payments and Redemption Price on the Bonds and for the purposes of the Rebate Fund. Moneys on deposit in the Bond Payment Fund are used to make the following payments or for the following purposes:

Interest Component. To pay the next maturing interest payment on the Grant Anticipation Bonds;

Principal Payments. To pay the next maturing principal or mandatory sinking fund redemption payment on the Grant Anticipation Bonds;

Redemption Price. To pay the Redemption Price of the Grant Anticipation Bonds next coming due pursuant to redemption prior to maturity.

Deposits are next made, as necessary, into the Debt Service Reserve Fund and then into the Rebate Fund.

Federal Transportation Funds may then be used to pay obligations that do not have a lien on Federal Transportation funds equal to the lien securing the Grant Anticipation Bonds.

After meeting the foregoing requirements, Federal Transportation Funds may be released free and clear of the lien of the Grant Anticipation Resolution, if and to the extent (i) not required for Current Payments and not expected to be needed for any subsequent Bond Payments and (ii) as provided in a certificate of the Executive Director.

Except for the application required above and for amounts held for the payment of Grant Anticipation Bonds no longer deemed Outstanding, Federal Transportation Funds need not be retained for any use or in any account described above in excess of the Federal Transportation Funds required for Current Payments if and to the extent such amounts are not expected to be needed for any subsequent Bond Payments.

Notwithstanding the above, in each Federal Fiscal Year, upon securing Obligation Authority (as defined herein) sufficient to pay the Bond Payments and Program Costs coming due in the current Federal Fiscal Year, the Authority need not deposit the Federal Transportation Funds received in the manner and priority set forth above; provided, however, that the Authority shall forward, or cause to be forwarded, to the Trustee an amount of Federal Transportation Funds sufficient to pay the Bond Payments and the Program Costs due in such Federal Fiscal Year when such costs are due and payable.

Debt Service Reserve Requirement for the 2004 Grant Anticipation Bonds

Under the 2004 Supplemental Resolution, the Authority is required to deposit into the 2004 Debt Service Reserve Account of the Debt Service Reserve Fund, from the proceeds of the 2004 Grant Anticipation Bonds, an amount equal to \$12,035,187.50, which shall be available to pay debt service on the 2004 Grant Anticipation Bonds when insufficient funds for that purpose are available in the Bond Payment Fund.

Covenants Concerning Federal Transportation Funds

In the Grant Anticipation Resolution, the Authority covenants that it will take all action necessary to ensure that (i) each Construction Project at all times qualifies as a Qualified Federal Aid Transportation Project and (ii) each Construction Project that may be financed, in whole or in part, with Federal Transportation Funds paid pursuant to Title 23, at all times qualifies as a project with respect to which the Authority is entitled to reimbursement of previously-expended funds.

The Authority also covenants that it will (i) comply with its obligations under the Federal Aid Agreements, and will take all other actions required to maintain the Federal Aid Agreements in full force and effect and (ii) will annually apply for and reasonably cooperate with FHWA in order to receive the greatest amount of Federal Transportation Funds reasonably available to the Authority, including amounts sufficient for payment of the Bond Payments and Program Costs.

As soon as practicable prior to or in each Federal Fiscal Year while the Grant Anticipation Bonds are outstanding, the Grant Anticipation Resolution requires the Authority to request FHWA to provide Obligation Authority sufficient to pay Bond Payments and Program Costs due in the current Federal Fiscal Year prior to obligating Federal Transportation Funds for any other purpose coming due in that Federal Fiscal Year.

See "APPENDIX III – SUMMARY OF CERTAIN PROVISIONS OF THE GRANT ANTICIPATION RESOLUTION" for a more detailed discussion of the representations, covenants and warranties of the Authority. For a discussion of how the Federal Transportation Funds are obligated under Title 23, how advance construction projects are converted and other requirements of Federal law that must be satisfied before the FHWA pays Federal Transportation Funds to the Authority, see "INFORMATION CONCERNING THE FUNDING OF FEDERAL-AID HIGHWAYS" herein.

Additional Grant Anticipation Bonds

The Authority may issue, from time to time, one or more Series of Additional Grant Anticipation Bonds, which are payable from and secured by the Trust Estate on a parity with the 2004 Grant Anticipation Bonds and any Additional Grant Anticipation Bonds that may be subsequently issued, upon satisfaction of the requirements of the Grant Anticipation Resolution before such issuance. No Additional Grant Anticipation Bonds may be issued unless an authorized officer of the Authority certifies:

(1) The lowest amount of Federal Transportation Funds received by the Authority in any Federal Fiscal Year during the three Federal Fiscal Years preceding the authentication and delivery of the Series of Additional Grant Anticipation Bonds then proposed to be issued;

(2) The maximum annual Bond Payments for the Outstanding Grant Anticipation Bonds in the current and each future Federal Fiscal Year including the Series of Additional Grant Anticipation Bonds proposed to be issued, but in the case of a Series of Additional Grant Anticipation Bonds for refunding purposes, excluding the Bond Payments on the Grant Anticipation Bonds to be refunded; and

(3) That the Federal Transportation Funds set forth in (1) is not less than four hundred percent (400%) of the maximum annual Bond Payments set forth in (2) above.

(4) In addition, an authorized officer must certify that the Authority has no information which indicates that Federal Transportation Funds will not be available to the Authority or will be substantially reduced (i) during the term of the Federal Aid Authorization then in effect in amounts sufficient to pay, when due, Bond Payments on the Grant Anticipation Bonds to be outstanding during such term and (ii) it is the Executive Director's reasonable belief that sufficient Federal Transportation Funds will continue to be available to the Authority pursuant to Title 23 during that period of time.

The requirements of paragraphs (1), (2) and (3) above may be waived upon the Authority's receipt of written evidence from each Rating Agency then maintaining a rating on the Outstanding Grant Anticipation Bonds, to the effect that such waiver will not by itself result in the withdrawal, reduction, or suspension of any such rating by such Rating Agency.

The Authority may also issue Additional Grant Anticipation Bonds without complying with paragraphs (1), (2) and (3) above for the purpose of refunding in whole or in part any Grant Anticipation Bonds Outstanding under the Grant Anticipation Resolution provided that the Authority certifies that: (a) the annual Bond Payments for all Grant Anticipation Bonds Outstanding immediately after the issuance of such proposed refunding Grant Anticipation Bonds (including Bond Payments on the refunding Grant Anticipation Bonds, but excluding Bond Payments on refunded Grant Anticipation Bonds) for the current and each future Federal Fiscal Year to and including the Federal Fiscal Year of the latest maturity on any Grant Anticipation Bonds then Outstanding is no greater than (b) the annual Bond Payments for all Grant Anticipation Bonds Outstanding immediately prior to such issuance during the same Federal Fiscal Years.

For further discussion of issuance of Additional Grant Anticipation Bonds, see "APPENDIX III – SUMMARY OF CERTAIN PROVISIONS OF THE GRANT ANTICIPATION RESOLUTION."

Credit Facilities and Interest Rate Exchange Agreements

Notwithstanding any other provision of the Grant Anticipation Resolution, (i) the Authority may purchase or arrange for a Credit Facility to secure any Grant Anticipation Bonds and may agree to reimburse the provider for any draws to make Bond Payments on a parity with or on a basis subordinate to the payment of Bond Payments and (ii) to the extent permitted by law, the Authority may purchase or arrange for an Interest Rate Exchange Agreement with respect to any Grant Anticipation Bonds and may agree to make payments to the provider of an Interest Rate Exchange Agreement, which may be on a parity with or on a basis subordinate to the payment of Bond Payments.

Defeasance

If the Authority pays or causes to be paid, or there is otherwise paid, to the owners of all or a portion of the outstanding Grant Anticipation Bonds, the principal and interest due or to become due thereon, at the times and in the manner stipulated therein and in the Grant Anticipation Resolution, such Grant Anticipation Bonds will cease to be entitled to any pledge, benefit or security under the Grant Anticipation Resolution, and all covenants, agreements and obligations of the Authority to the owners of such Grant Anticipation Bonds will thereupon cease, terminate and become void and be discharged and satisfied.

Subject to the provisions of the Grant Anticipation Resolution, any outstanding Grant Anticipation Bonds will be deemed to have been paid within the meaning and with the effect expressed in the foregoing paragraph if there has been

deposited with an escrow agent appointed for such purpose either money in an amount which will be sufficient, or Defeasance Securities as prescribed in the Grant Anticipation Resolution, the principal of and the interest on which, when due, will provide money which, together with the money, if any, deposited with the escrow agent at the time, will be sufficient to pay when due the principal and interest due and to become due on such Grant Anticipation Bonds on or prior to the maturity date thereof. See "Defeasance" in "APPENDIX III - SUMMARY OF CERTAIN PROVISIONS OF THE GRANT ANTICIPATION RESOLUTION."

SECURITY AND SOURCES OF PAYMENT FOR THE 2004 TRANSPORTATION REVENUE BONDS

Pledged Revenues

The 2004 Transportation Revenue Bonds, the Outstanding Senior Bonds and any additional senior bonds issued under the 1998 Resolution are payable solely from, and secured by a pledge of, the 1998 Resolution Revenues and all other moneys held for the credit of the 1998 Senior Bond Sinking Fund, which includes the 1998 Senior Bond Service Account, the 1998 Senior Bond Redemption Account and the 1998 Senior Bond Reserve Account. Under certain circumstances described below, unencumbered moneys in the 1998 Construction Fund or the 1998 Subordinated Bond Sinking Fund, derived from 1998 Resolution Revenues may be used to pay debt service on the Senior Transportation Revenue Bonds, if moneys in the 1998 Senior Bond Service Account or the 1998 Senior Bond Redemption Account are insufficient therefor, prior to applying moneys in the 1998 Senior Bond Reserve Account.

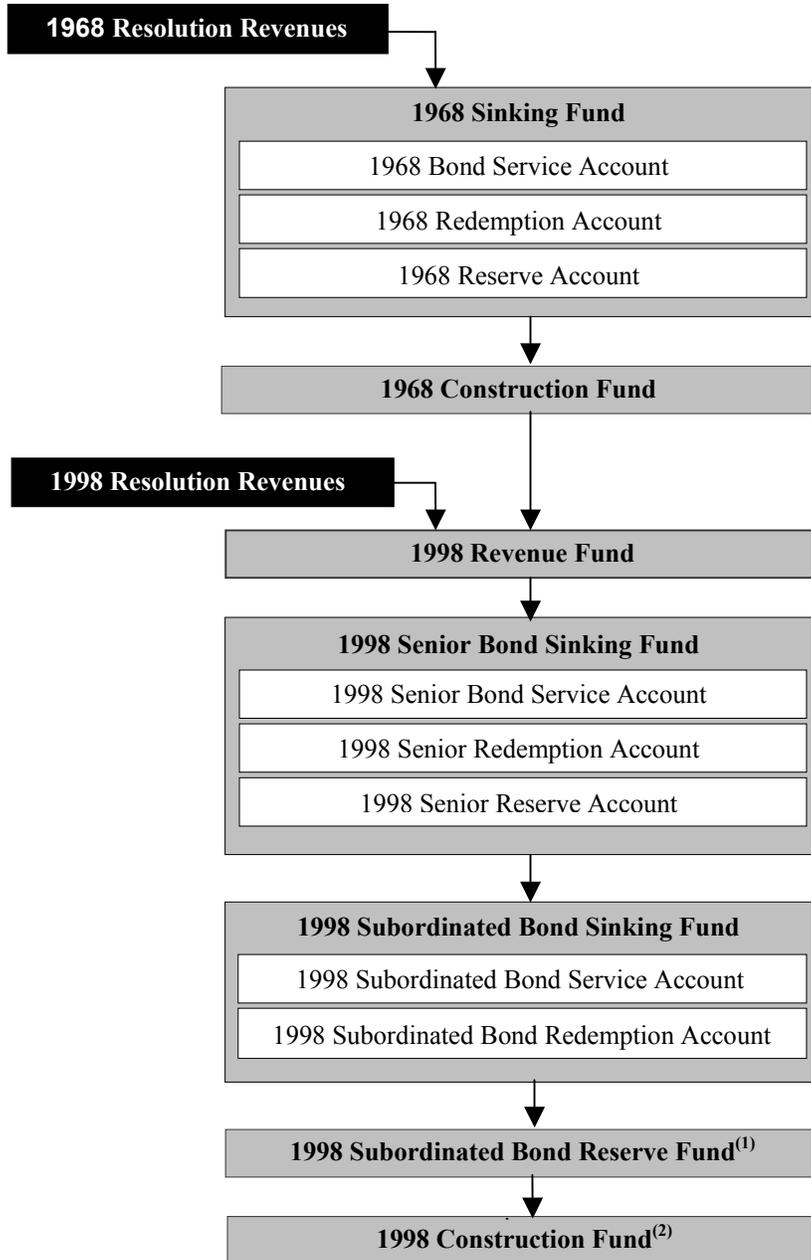
1998 Resolution Revenues. The 1998 Resolution Revenues consist of: (i) all excise taxes on crude oil, unfinished oil and derivative products ("petroleum products"), up to \$120 million per fiscal year, imposed by the Commonwealth and allocated to the Authority by Act No. 34 of the Legislature of Puerto Rico, approved July 16, 1997, as amended ("Act No. 34"), which amended Subtitle B of Act No. 120 of the Legislature of Puerto Rico approved October 31, 1994, as amended (the "1994 Code"); (ii) the tolls and other charges imposed by the Authority for the use of Toll Facilities (other than Existing Toll Facilities Revenues prior to the repeal and cancellation of the 1968 Resolution); (iii) the proceeds of any other taxes, fees or charges which the Legislature of Puerto Rico allocates to the Authority in the future and which the Authority pledges to the payment of Transportation Revenue Bonds; (iv) investment earnings on deposit to the credit of funds and accounts established under the 1998 Resolution, except for the 1998 Construction Fund; and (v) prior to the repeal and cancellation of the 1968 Resolution, any unencumbered 1968 Resolution Revenues remaining on deposit in the 1968 Construction Fund after payment or provision for payment of debt service and required reserves on the outstanding Highway Revenue Bonds (the "Excess 1968 Resolution Revenues") and, after said repeal and cancellation, all 1968 Resolution Revenues. The 1998 Resolution Revenues do not include excise taxes on petroleum products which may be levied or collected from time to time other than the amount of such taxes described in this paragraph unless allocated to the Authority and pledged by the Authority to the payment of Transportation Revenue Bonds. The excise tax on petroleum products imposed by the 1994 Code and allocated to the Authority by Act No. 34 is a different tax from the excise tax on gasoline and gas oil and diesel oil imposed by the 1994 Code and allocated to the Authority, as discussed below.

1968 Resolution Revenues. The 1968 Resolution Revenues consist of: (i) the gross receipts of the current \$0.16 per gallon excise tax on gasoline and \$0.04 of the current \$0.08 per gallon excise tax on gas oil and diesel oil imposed by the Commonwealth and allocated to the Authority (after any deductions for taxes on fuels used in sea and air transportation that are required to be reimbursed under certain circumstances) by the 1994 Code (the remaining \$0.04 per gallon excise tax has been allocated to the Metropolitan Bus Authority by Act No. 39 of July 19, 1997); (ii) the gross receipts derived from the \$15 per vehicle increase of annual motor vehicle license fees imposed by the Commonwealth and allocated to the Authority by Act No. 9 of the Legislature of Puerto Rico, approved August 12, 1982 ("Act No. 9"); (iii) Existing Toll Facilities Revenues; and (iv) investment earnings on deposits to the credit of funds and accounts established under the 1968 Resolution, except for the 1968 Construction Fund. 1968 Resolution Revenues do not include gasoline taxes, gas oil and diesel oil taxes, and motor vehicle license fees which may be levied or collected from time to time other than the amounts of the taxes and fees described in this paragraph unless allocated to the Authority and pledged by the Authority to the payment of Highway Revenue Bonds.

Flow of Funds Under 1968 Resolution and 1998 Resolution

The following chart illustrates the flow of 1968 Resolution Revenues and 1998 Resolution Revenues into the various funds and accounts established under the 1968 Resolution and the 1998 Resolution. The chart is provided only as a summary of the flow of funds under the 1968 Resolution and the 1998 Resolution, and does not purport to be complete. Reference is made to the summary of the 1998 Resolution in Appendix IV, which should be read in conjunction herewith.

Flow of Funds Under the 1968 and 1998 Resolutions



(1) Under the 1998 Resolution, separate accounts in the Subordinated Bond Reserve Fund may be established for Series of Subordinated Bonds with different Subordinated Reserve Requirements.

(2) Certain Authority operation and maintenance expenses are paid from the 1998 Construction Fund.

Upon receipt of any moneys constituting 1968 Resolution Revenues, including moneys in the Special Fund constituting 1968 Resolution Revenues received from the Department of the Treasury (see “Special Fund” below), the Authority is required under the 1968 Resolution to deposit such moneys in equal monthly amounts into the 1968 Bond Service Account and the 1968 Redemption Account to provide for the payment of principal of and interest and premium, if any, on the Highway Revenue Bonds and in the amounts necessary for the required deposits to the 1968 Reserve Account. Any remaining 1968 Resolution Revenues (other than investment earnings) are deposited into the 1968 Construction Fund. Under the 1998 Resolution, the Authority has agreed not to encumber or withdraw or pledge any 1968 Resolution Revenues deposited in the 1968 Construction Fund except for the transfer of Excess 1968 Resolution Revenues to the 1998 Revenue Fund, which Excess 1968 Resolution Revenues must be withdrawn monthly and transferred to the 1998 Revenue Fund for application as described below. See “APPENDIX IV - SUMMARY OF CERTAIN PROVISIONS OF THE 1998 RESOLUTION.”

Upon receipt of any moneys constituting 1998 Resolution Revenues (other than investment earnings), including moneys in the Special Fund constituting 1998 Resolution Revenues received from the Department of the Treasury, the Authority is required under the 1998 Resolution to deposit such moneys into the 1998 Revenue Fund. In addition, the Authority is required to deposit monthly into the 1998 Revenue Fund all Excess 1968 Resolution Revenues. The Authority is required to withdraw monthly from the 1998 Revenue Fund and deposit into the 1998 Senior Bond Service Account and the 1998 Senior Bond Redemption Account the respective equal monthly amounts necessary to provide for the payment of principal of and interest and premium, if any, on the Senior Transportation Revenue Bonds and deposit to the 1998 Senior Bond Reserve Account the amount necessary, if any, to replenish the 1998 Senior Bond Reserve Account. Any remaining 1998 Resolution Revenues (other than investment earnings) are then required to be deposited monthly (in the respective equal monthly amounts) first into the accounts within the 1998 Subordinated Bond Service Account and the 1998 Subordinated Bond Redemption Account to provide for the payment of principal of and interest and premium, if any, on the Subordinated Transportation Revenue Bonds and then, into the 1998 Subordinated Bond Reserve Fund, as required. Any remaining 1998 Resolution Revenues are then deposited into the 1998 Construction Fund and are available to the Authority for any of its authorized purposes, but subject to the payment of certain operation and maintenance expenses and repair, renewal and replacement costs, as required by the 1998 Resolution. Once all outstanding Highway Revenue Bonds are paid or defeased and the 1968 Resolution is repealed and canceled, all revenues of the Authority formerly constituting 1968 Resolution Revenues will be deposited monthly into the 1998 Revenue Fund for application as described above.

Neither the 1968 Resolution nor the 1998 Resolution contains events of default or provides for the acceleration of the maturities of the Highway Revenue Bonds or the Transportation Revenue Bonds.

1998 Senior Bond Reserve Account

The 1998 Resolution establishes a 1998 Senior Bond Reserve Account, the moneys in which are to be applied to the payment of interest on the Senior Transportation Revenue Bonds, and maturing principal of serial Senior Transportation Revenue Bonds whenever moneys in the 1998 Senior Bond Service Account are insufficient for such purpose and thereafter for the purpose of making deposits to the credit of the 1998 Senior Bond Redemption Account to satisfy any Amortization Requirements for the term Senior Transportation Revenue Bonds whenever 1998 Resolution Revenues are insufficient for such purpose. The 1998 Resolution provides, however, that before the moneys in the 1998 Senior Bond Reserve Account are used to cover any insufficiency in the 1998 Senior Bond Service Account or the 1998 Senior Bond Redemption Account, the 1998 Fiscal Agent shall cover such insufficiency by first withdrawing from the 1998 Construction Fund any unencumbered 1998 Resolution Revenues deposited therein and, to the extent such moneys are insufficient to cover said deficiency, by withdrawing moneys on deposit in the 1998 Subordinated Bond Service Account and 1998 Subordinated Bond Redemption Account.

The Authority covenants to accumulate and maintain in the 1998 Senior Bond Reserve Account an amount equal to the lesser of the maximum annual Principal and Interest Requirements for any fiscal year on all outstanding Senior Transportation Revenue Bonds and 10% of the original principal amount of each Series of Senior Transportation Revenue Bonds outstanding (the “1998 Senior Bonds Reserve Requirement”).

On March 1, 2004, approximately \$203,443,781 was in deposit in the 1998 Senior Bond Reserve Account. The Senior Bonds Reserve Requirement will be \$223,525,412 upon the issuance of the 2004 Transportation Revenue Bonds and the refunding of the Refunded Bonds, and such amount will be on deposit in the 1998 Senior Bond Reserve Account following the issuance of the 2004 Transportation Revenue Bonds. The 1998 Resolution permits any increase in the Senior Bonds Reserve Requirement to be funded over not more than five years and allows the Authority to use a letter of credit or insurance policy to fund the Senior Bonds Reserve Requirement. See APPENDIX IV – SUMMARY OF 1998 RESOLUTION.

Excess moneys in the 1998 Senior Bond Reserve Account may be retained in such Reserve Account, may be applied to the payment of outstanding notes issued by the Authority to finance temporarily any Transportation Facilities or outstanding Senior Transportation Revenue Bonds to be refunded or may be transferred to the 1998 Senior Bond Service Account, the 1998 Senior Bond Redemption Account, or the 1998 Construction Fund, as directed by the Authority.

Replenishment of 1968 and 1998 Reserve Accounts

Under the 1994 Code, if moneys in the 1968 Reserve Account, 1998 Senior Bond Reserve Account or any accounts established in the 1998 Subordinated Bond Reserve Fund (collectively, the “Reserve Accounts”) are applied to cover a deficiency in the amounts necessary for payment of the principal of and interest on the Highway Revenue Bonds, Senior Transportation Revenue Bonds or Subordinated Transportation Revenue Bonds, respectively, the amounts used from any of the applicable Reserve Accounts to cover said deficiency shall be reimbursed to the Authority from the first amounts received in the next fiscal year or subsequent years by the Commonwealth derived from (i) any other taxes which may then be in effect on any other fuel or propellant which is used, among other purposes, to propel highway vehicles, and (ii) any remaining portion of the gasoline tax and petroleum products tax then in effect. The proceeds of said other taxes and the remainder of the gasoline tax and petroleum products tax to be used to reimburse the applicable Reserve Accounts are not deposited in the General Fund of the Commonwealth when collected, but are deposited instead in the Special Fund for the benefit of the Authority, and, subject to the provisions of Section 8 of Article VI of the Constitution of Puerto Rico, used to reimburse said Reserve Accounts. In the 1998 Resolution, the Authority covenants to apply any such reimbursement received first to replenish the 1968 Reserve Account, then to replenish the 1998 Senior Bond Reserve Account, and finally to replenish any accounts in the 1998 Subordinated Bond Reserve Fund.

Commitment Not to Reduce Taxes and Fees

The Commonwealth has agreed and committed in the 1994 Code that it will not reduce the gasoline tax below \$0.16 per gallon, the tax on gas oil and diesel oil below \$0.04 per gallon or the tax on petroleum products below the tax rates in effect on July 16, 1997 (as described below), and that it will not reduce the amount of any such taxes allocated to the Authority until all obligations of the Authority, including the Highway Revenue Bonds and the Transportation Revenue Bonds, secured by the pledge thereof are fully paid. The Commonwealth has also agreed and pledged in Act No. 9 that it will not reduce the motor vehicle license fees allocated and pledged to the payment of obligations of the Authority, including the Highway Revenue Bonds and the Transportation Revenue Bonds, so long as the proceeds of such fees remain pledged to the payment of such obligations.

Special Fund

Under the 1994 Code and Act No. 9, the proceeds of the taxes and license fees allocated to the Authority are deposited by the Department of the Treasury in a special fund (the “Special Fund”) in favor of the Authority. In accordance with the Constitution of Puerto Rico, the proceeds of such taxes and license fees are subject to being applied first to the payment of general obligation debt of and debt guaranteed by the Commonwealth, if and to the extent that all other Commonwealth revenues are insufficient therefor. The Commonwealth has never applied the proceeds of such taxes or license fees allocated to the Authority to the payment of such debt nor has the Commonwealth ever defaulted on the payment of principal of or interest on any of such debt. For information with respect to the Commonwealth’s debt and the economic and financial condition of the Commonwealth, see “Prior Payment of Full Faith and Credit Obligations of the Commonwealth” below and *Debt* in the Commonwealth Report.

Prior Payment of Full Faith and Credit Obligations of the Commonwealth

Provision for Prior Payment. The Constitution of Puerto Rico provides that public debt of the Commonwealth constitutes a first lien on available Commonwealth taxes and revenues. Public debt includes bonds and notes of the Commonwealth to which the full faith, credit and taxing power of the Commonwealth are pledged, and, according to opinions heretofore rendered by the Secretary of Justice of the Commonwealth, any payments which are required to be made by the Commonwealth under its guarantees of bonds and notes issued by its public corporations. The 2004 Transportation Revenue Bonds do not constitute public debt.

The proceeds of the gasoline tax, the gas oil and diesel oil tax, the petroleum products tax and the motor vehicle license fees allocated to the Authority by the 1994 Code and Act No. 9 are available Commonwealth taxes and revenues under the Constitution. Accordingly, if needed, they are subject to being applied first to the payment of debt service on the public debt of the Commonwealth but, under the 1994 Code and Act No. 9, such taxes and license fees are to be used for such payments only if and to the extent that all other available revenues of the Commonwealth under the Constitution are insufficient for such purpose. Tolls and other fees and charges collected by the Authority and investment earnings are not available Commonwealth taxes and revenues.

The Commonwealth has never applied taxes or license fees allocated to the Authority to the payment of its public debt nor has the Commonwealth ever defaulted on the payment of principal of or interest on any of its public debt. See *Debt* in the Commonwealth Report.

Under the provisions of Act No. 39 of the Legislature of Puerto Rico, approved May 13, 1976, as amended (“Act No. 39”), the Secretary of the Treasury of Puerto Rico is obligated to fund annual debt service on general obligation bonds and notes of the Commonwealth by monthly deposits into the Special Fund for the Amortization of General Obligations Evidenced by Bonds and Promissory Notes (the “Commonwealth Redemption Fund”). As of the date of this Official Statement, the amount on deposit in the Commonwealth Redemption Fund complied with such requirement. Moneys in the Commonwealth Redemption Fund may also be applied to payment of other Commonwealth guaranteed obligations outstanding prior to adoption of Act No. 39. Such moneys are not available to pay the 2004 Transportation Revenue Bonds.

Debt Limitation. Section 2 of Article VI of the Constitution of Puerto Rico provides that direct obligations of the Commonwealth evidenced by full faith and credit bonds or notes shall not be issued if the amount of the principal of and interest on such bonds and notes and on all such bonds and notes theretofore issued which is payable in any fiscal year, together with any amount paid by the Commonwealth in the preceding fiscal year on account of bonds or notes guaranteed by the Commonwealth, exceeds 15% of the average annual revenues raised under the provisions of Commonwealth legislation and covered into the Treasury of Puerto Rico (hereinafter “internal revenues”) in the two fiscal years preceding the then current fiscal year. Section 2 of Article VI does not limit the amount of debt that the Commonwealth may guarantee so long as the 15% limitation is not exceeded.

Internal revenues consist principally of income taxes, property taxes and excise taxes. Certain revenues, such as federal excise taxes on offshore shipments of alcoholic beverages and tobacco products and customs duties, which are collected by the United States Government and returned to the Treasury of Puerto Rico, and motor vehicle fuel taxes and license fees, which are allocated to the Authority, are not included as internal revenues for the purpose of calculating the debt limit, although they may be available for the payment of debt service. On December 21, 1995, the Puerto Rico Aqueduct and Sewer Authority issued \$400,340,000 Puerto Rico Aqueduct and Sewer Authority Refunding Bonds, guaranteed by the Commonwealth (the “PRASA Guaranteed Bonds”). On January 1, 1997, the Commonwealth began to make payments of debt service on the PRASA Guaranteed Bonds under the full faith and credit guarantee of the Commonwealth. The amounts paid by the Commonwealth under the PRASA Guaranteed Bonds are taken into account for purposes of computing the above described 15% constitutional debt limitation.

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

Future maximum annual debt service for the Commonwealth’s currently outstanding general obligation debt is \$518,432,766 in the fiscal year ending June 30, 2003. Debt service for the PRASA Guaranteed Bonds paid during fiscal 2003 was \$33,215,868. The sum of those amounts (\$551,648,634) is equal to 8.2% of \$6,748,772 which is the average of the adjusted internal revenues for the prior two fiscal years ended June 30, 2003.

Information about the Commonwealth public sector debt and debt service requirements for the Commonwealth’s general obligation bonds and the Commonwealth’s guaranteed debt appear in *Public Sector Debt of the Commonwealth* in the Commonwealth Report.

The 2004 Transportation Revenue Bonds are not a debt of the Commonwealth or any of its political subdivisions (other than the Authority), and neither the Commonwealth nor any such subdivision (other than the Authority) shall be liable thereon.

Additional Bonds under the 1968 Resolution and the 1998 Resolution

Highway Revenue Bonds. The Authority may not issue additional Highway Revenue Bonds under the 1968 Resolution except bonds maturing no later than July 1, 2036, which are issued to refund outstanding Highway Revenue Bonds in order to achieve debt service savings. The issuance of such Highway Revenue Bonds must meet the tests for the issuance of such bonds under the 1968 Resolution.

Senior Transportation Revenue Bonds. The Authority may issue additional Senior Transportation Revenue Bonds under the 1998 Resolution to provide funds for any lawful purpose of the Authority, including the payment of all or any part of the cost of Transportation Facilities (including the payment of any outstanding notes of the Authority issued for the purpose of paying all or a part of such cost); provided that the 1998 Resolution Revenues for any 12 consecutive months of the 15 months immediately preceding the issuance of such Senior Transportation Revenue Bonds (adjusted to

take into account for such entire 12 months moneys allocated to and pledged by the Authority to the payment of the Transportation Revenue Bonds under legislation enacted and toll rate revisions made effective on or prior to the date of delivery of such bonds and tolls from Toll Facilities to be financed from the proceeds of such bonds) are not less than 150% of the maximum Principal and Interest Requirements for any fiscal year thereafter on account of all outstanding Senior Transportation Revenue Bonds and the additional Senior Transportation Revenue Bonds then to be issued and not less than 100% of the maximum Principal and Interest Requirements for any fiscal year thereafter on account of all outstanding Transportation Revenue Bonds (including Subordinated Transportation Revenue Bonds) and the additional Senior Transportation Revenue Bonds then to be issued.

The Authority may also issue additional Senior Transportation Revenue Bonds to refund all or any part of the outstanding Senior Transportation Revenue Bonds of any Series without satisfying such requirement, provided that the Authority certifies that the maximum annual Principal and Interest Requirements on the Senior Transportation Revenue Bonds to be outstanding after the issuance of such additional Senior Transportation Revenue Bonds will be equal to or less than the maximum annual Principal and Interest Requirements on the Senior Transportation Revenue Bonds outstanding immediately prior to the issuance of the additional Senior Transportation Revenue Bonds. See “Issuance of Additional Bonds” in “APPENDIX IV – SUMMARY OF CERTAIN PROVISIONS OF THE 1998 RESOLUTION.”

Any additional Senior Transportation Revenue Bonds issued under the 1998 Resolution will be on a parity with the outstanding Senior Transportation Revenue Bonds and will be entitled to the equal benefit, protection and security of the provisions, covenants and agreements of the 1998 Resolution. The 2004 Transportation Revenue Bonds are being issued as Senior Transportation Revenue Bonds.

Subordinated Transportation Revenue Bonds. The Authority may issue Subordinated Transportation Revenue Bonds under the 1998 Resolution to pay all or any part of the cost of any highway project or transit project eligible for financial assistance under federal legislation, provided that the 1998 Resolution Revenues for any 12 consecutive months of the 15 months immediately preceding the issuance of such Subordinated Transportation Revenue Bonds (adjusted to take into account for such entire 12 months moneys allocated to and pledged by the Authority to the payment of the Transportation Revenue Bonds under legislation enacted and toll rate changes made effective on or prior to delivery of such bonds and tolls from Toll Facilities to be financed from the proceeds of such bonds) are not less than 125% of the maximum Principal and Interest Requirements for any fiscal year thereafter on account of all outstanding Transportation Revenue Bonds and the Subordinated Transportation Revenue Bonds then to be issued.

The Authority may also issue Subordinated Transportation Revenue Bonds to refund all or any part of the outstanding Subordinated Transportation Revenue Bonds of any Series without satisfying such requirement, provided that the Authority certifies that the maximum Principal and Interest Requirements on the Subordinated Transportation Revenue Bonds to be outstanding after the issuance of such additional Subordinated Transportation Revenue Bonds will be equal to or less than the maximum annual Principal and Interest Requirements on the Subordinated Transportation Revenue Bonds outstanding immediately prior to the issuance of the additional Subordinated Transportation Revenue Bonds. See “Issuance of Additional Bonds” in “APPENDIX IV – SUMMARY OF CERTAIN PROVISIONS OF THE 1998 RESOLUTION.”

In December 1997, the Authority entered into a Cooperative Agreement with the FHWA, the Federal Transit Administration (“FTA”) and the Department that provides for the establishment of a State Infrastructure Bank (“SIB”) under the provisions of Section 350 of the National Highway System Designation Act of 1995, which bank was capitalized 80% by federal capitalization grants and 20% by matching Authority funds. The SIB has been used to provide various forms of financial assistance to the Authority to finance eligible highway and transit projects.

In August 1998, the Authority issued its 1998 SIB Bonds in the principal amount of \$75,050,000 under the 1998 Resolution. The reserve account in the Subordinated Bond Reserve Fund established as part of the security for the 1998 SIB Bonds (the “1998 SIB Reserve Account”) is entitled to the benefits of an agreement with the SIB under which agreement the 1998 Fiscal Agent is authorized and directed to request funds from the depository institution holding the SIB moneys (currently the Government Development Bank), up to the full amount on deposit in the SIB, in the event it is necessary to apply moneys in such account in the Subordinated Bond Reserve Fund to pay debt service on the 1998 SIB Bonds. The Authority’s obligation to repay any amounts drawn under the agreement with the SIB also will be secured by a lien on 1998 Resolution Revenues subordinate to the lien securing the Senior Transportation Revenue Bonds. See “Sinking Fund” in “APPENDIX IV – SUMMARY OF CERTAIN PROVISIONS OF THE 1998 RESOLUTION.”

In April 2003, the Authority issued its Subordinated Transportation Revenue Bonds (Series 2003) in the principal amount of \$320,545,000 under the 1998 Resolution to refund a \$300 million loan from the United States Department of Transportation under the Transportation Infrastructure Finance and Innovation Act of 1998, as amended, related to the financing of the Tren Urbano Project.

Proposed 1998 Supplemental Resolution

The Authority proposes to adopt a supplemental resolution (the “1998 Variable Rate Supplement”) when the consent of the owners of a majority in aggregate principal amount of the Senior Transportation Revenue Bonds and of the Subordinate Transportation Revenue Bonds outstanding has been obtained. Such supplemental resolution will permit the 1998 Fiscal Agent to treat Transportation Revenue Bonds bearing interest at a variable rate as having an assumed fixed interest rate equal to the latest five-year or one-year (if higher) average of the historical interest rates on such bonds or based upon certain commonly used interest rate indices for the purpose of calculating Principal and Interest Requirements (as defined in the 1998 Resolution).

Consent of Transportation Revenue Bondholders

By purchasing the 2004 Transportation Revenue Bonds, the owners of such bonds will have consented to and approved, for themselves and future owners of such 2004 Transportation Revenue Bonds, the adoption of the 1998 Variable Rate Supplement. Upon the issuance of the 2004 Transportation Revenue Bonds and the refunding of the Refunded Bonds, the owners of 31.87% of the aggregate principal amount of the Senior Transportation Revenue Bonds and of 81.03% of the aggregate principal amount of the Subordinated Transportation Revenue Bonds outstanding will have consented to the adoption of such supplemental resolution.

BOND INSURANCE

The following has been provided by MBIA Insurance Corporation (“MBIA”) and Financial Guaranty Insurance Company (“FGIC”), with respect to the MBIA Insured Bonds and the FGIC Insured Bonds, respectively, as indicated on the inside cover pages of this Official Statement for use in this Official Statement.

No representation is made by the Authority as to the accuracy or completeness of the information. Reference is made to Appendices VI and VII for specimens of the Bond Insurance Policies.

MBIA Insurance Corporation

MBIA’s policy unconditionally and irrevocably guarantees the full and complete payment required to be made by or on behalf of the Authority to the Trustee or the 1998 Fiscal Agent, or their respective successors, of an amount equal to (i) the principal of (either at the stated maturity or by an advancement of maturity pursuant to a mandatory sinking fund payment) and interest on, the MBIA Insured Bonds as such payments shall become due but shall not be so paid (except that in the event of any acceleration of the due date of such principal by reason of mandatory or optional redemption or acceleration resulting from default or otherwise, other than any advancement of maturity pursuant to a mandatory sinking fund payment, the payments guaranteed by the MBIA Bond Insurance Policy shall be made in such amounts and at such times as such payments of principal would have been due had there not been any such acceleration); and (ii) the reimbursement of any such payment which is subsequently recovered from any owner of the MBIA Insured Bonds pursuant to a final judgment by a court of competent jurisdiction that such payment constitutes an avoidable preference to such owner within the meaning of any applicable bankruptcy law (a “Preference”).

The MBIA Bond Insurance Policy does not insure against loss of any prepayment premium which may at any time be payable with respect to any MBIA Insured Bonds. The MBIA Bond Insurance Policy does not, under any circumstance, insure against loss relating to: (i) optional or mandatory redemptions (other than mandatory sinking fund redemptions); (ii) any payments to be made on an accelerated basis; (iii) payments of the purchase price of MBIA Insured Bonds upon tender by an owner thereof; or (iv) any Preference relating to (i) through (iii) above. MBIA’s policy also does not insure against nonpayment of principal of or interest on the MBIA Insured Bonds resulting from the insolvency, negligence or any other act or omission of the Trustee, the 1998 Fiscal Agent or any other paying agent for the MBIA Insured Bonds.

Upon receipt of telephonic or telegraphic notice, such notice subsequently confirmed in writing by registered or certified mail, or upon receipt of written notice by registered or certified mail, by MBIA from the Trustee, or the 1998 Fiscal Agent, as applicable, or any owner of an MBIA Insured Bond the payment of an insured amount for which is then due, that such required payment has not been made, MBIA on the due date of such payment or within one business day after receipt of notice of such nonpayment, whichever is later, will make a deposit of funds, in an account with U.S. Bank Trust National Association, in New York, New York, or its successor, sufficient for the payment of any such insured amounts which are then due. Upon presentment and surrender of such MBIA Insured Bonds or presentment of such other proof of ownership of the MBIA Insured Bonds, together with any appropriate instruments of assignment to evidence the

assignment of the insured amounts due on the MBIA Insured Bonds as are paid by MBIA, and appropriate instruments to effect the appointment of MBIA as agent for such owners of the MBIA Insured Bonds in any legal proceeding related to payment of insured amounts on the MBIA Insured Bonds, such instruments being in a form satisfactory to U.S. Bank Trust National Association, U.S. Bank Trust National Association shall disburse to such owners or the Trustee or 1998 Fiscal Agent, as applicable, payment of the insured amounts due on such MBIA Insured Bonds, less any amount held by the Trustee or 1998 Fiscal Agent, as applicable, for the payment of such insured amounts and legally available therefor.

MBIA is the principal operating subsidiary of MBIA Inc., a New York Stock Exchange listed company (the "Company"). The Company is not obligated to pay the debts of or claims against MBIA. MBIA is domiciled in the State of New York and licensed to do business in and subject to regulation under the laws of all 50 states, the District of Columbia, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, the Virgin Islands of the United States and the Territory of Guam. MBIA has three branches, one in the Republic of France, one in the Republic of Singapore and one in the Kingdom of Spain. New York has laws prescribing minimum capital requirements, limiting classes and concentrations of investments and requiring the approval of policy rates and forms. State laws also regulate the amount of both the aggregate and individual risks that may be insured, the payment of dividends by MBIA, changes in control and transactions among affiliates. Additionally, MBIA is required to maintain contingency reserves on its liabilities in certain amounts and for certain periods of time.

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

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

The following document filed by the Company with the Securities and Exchange Commission (the "SEC") is incorporated herein by reference:

- (1) The Company's Annual Report on Form 10-K for the year ended December 31, 2003.

Any documents filed by the Company pursuant to Sections 13(a), 13(c), 14 or 15(d) of the Exchange Act of 1934, as amended, after the date of this Official Statement and prior to the termination of the offering of the MBIA Insured Bonds offered hereby shall be deemed to be incorporated by reference in this Official Statement and to be a part hereof. Any statement contained in a document incorporated or deemed to be incorporated by reference herein, or contained in this Official Statement, shall be deemed to be modified or superseded for purposes of this Official Statement to the extent that a statement contained herein or in any other subsequently filed document which also is or is deemed to be incorporated by reference herein modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of this Official Statement.

The Company files annual, quarterly and special reports, information statements and other information with the SEC under File No. 1-9583. Copies of the SEC filings (including (1) the Company's Annual Report on Form 10-K for the year ended December 31, 2003, and (2) the Company's Quarterly Reports on Form 10-Q for the quarters ended March 31, 2003, June 30, 2003 and September 30, 2003) are available (i) over the Internet at the SEC's web site at <http://www.sec.gov>; (ii) at the SEC's public reference room in Washington D.C.; (iii) over the Internet at the Company's web site at <http://www.mbia.com>; and (iv) at no cost, upon request to MBIA Insurance Corporation, 113 King Street, Armonk, New York 10504. The telephone number of MBIA is (914) 273-4545.

As of December 31, 2002, MBIA had admitted assets of \$9.2 billion (audited), total liabilities of \$6.0 billion (audited), and total capital and surplus of \$3.2 billion (audited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities. As of December 31, 2003 MBIA had admitted assets of \$9.9 billion (unaudited), total liabilities of \$6.2 billion (unaudited), and total capital and surplus of \$3.7 billion (unaudited) determined in accordance with statutory accounting practices prescribed or permitted by insurance regulatory authorities.

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

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

Fitch Ratings rates the financial strength of MBIA “AAA.”

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

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

Financial Guaranty Insurance Company

Concurrently with the issuance of the Bonds, FGIC will issue the FGIC Bond Insurance Policy for the FGIC Insured Bonds. The FGIC Bond Insurance Policy unconditionally guarantees the payment of that portion of the principal or accreted value (if applicable) of and interest on the FGIC Insured Bonds which has become due for payment, but shall be unpaid by reason of nonpayment by the Authority. FGIC will make such payments to U.S. Bank Trust National Association, or its successor as its agent (the “Fiscal Agent”), on the later of the date on which such principal or accreted value (if applicable) and interest is due or on the business day next following the day on which FGIC shall have received telephonic or telegraphic notice, subsequently confirmed in writing, or written notice by registered or certified mail, from an owner of FGIC Insured Bonds or the 1998 Fiscal Agent, of the nonpayment of such amount by the Authority. The Fiscal Agent will disburse such amount due on any FGIC Insured Bond to its owner upon receipt by the Fiscal Agent of evidence satisfactory to the Fiscal Agent of the owner’s right to receive payment of the principal, accreted value or interest (as applicable) due for payment and evidence, including any appropriate instruments of assignment, that all of such owner’s rights to payment of such principal, accreted value or interest (as applicable) shall be vested in FGIC. The term, “nonpayment” in respect of a FGIC Insured Bond includes any payment of principal, accreted value or interest (as applicable) made to an owner of such a Bond which has been recovered from such owner pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction.

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

Generally, in connection with its insurance of an issue of municipal securities, FGIC requires, among other things, (i) that it be granted the power to exercise any rights granted to the holders of such securities upon the occurrence of an event of default, without the consent of such holders, and that such holders may not exercise such rights without FGIC’s consent in each case so long as FGIC has not failed to comply with its payment obligations under its insurance policy; and (ii) that any amendment or supplement to or other modification of the principal legal documents be subject to FGIC’s consent. The rights, if any, granted to FGIC in connection with its insurance of the FGIC Insured Bonds are generally described below.

This Official Statement contains a section regarding the ratings assigned to the Bonds and reference should be made to such section for a discussion of such ratings, including the ratings, if any, assigned to the Authority’s outstanding uninsured bonds.

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

FGIC is a monoline financial guaranty insurer domiciled in the State of New York and subject to regulation by the State of New York Insurance Department. As of December 31, 2003, the total capital and surplus of FGIC was approximately \$1.153 billion. FGIC prepares financial statements on the basis of both statutory accounting principles and generally accepted accounting principles. Copies of such financial statements may be obtained by writing to FGIC at 125 Park Avenue, New York, New York 10017, Attention: Communications Department (telephone number : 212-312-3000) or to the New York State Insurance Department at 25 Beaver Street, New York, New York 10004-2319, Attention: Financial Condition Property/Casualty Bureau (telephone number: 212-480-5187).

FGIC is a wholly-owned subsidiary of FGIC Corporation. On December 18, 2003, an investor group consisting of The PMI Group, Inc. (“PMI”), The Blackstone Group L.P. (“Blackstone”), The Cypress Group L.L.C. (“Cypress”) and CIVC Partners L.P. (“CIVC”) acquired approximately 95% of the common stock of FGIC Corporation (the “Common Stock”) from General Electric Capital Corporation (“GE Capital”), a subsidiary of General Electric Company (“GE”). PMI, Blackstone, Cypress and CIVC acquired approximately 42%, 23%, 23% and 7% respectively, of the Common Stock. Prior to the closing on December 18, 2003, FGIC paid GE Capital approximately \$284.3 million in cash dividends. GE retained direct or indirect ownership of approximately 5% of FGIC Corporation’s common stock.

Concerning the Policies

As provided in the insurance agreements to be entered into by the Authority with each of MBIA and FGIC concurrently with the delivery of their respective Bond Insurance Policies, as long as MBIA and FGIC shall not be in default on their respective obligations under their respective Bond Insurance Policies, MBIA and FGIC shall be deemed to be the respective owners of the Bonds insured by each of them for purposes of, among other things, the giving of consents to the adoption of any supplements to the Grant Anticipation Resolution or the 1998 Resolution, as the case may be.

THE AUTHORITY

General Description

The Authority was created in 1965 to assume responsibility for the construction of roads and highways and related transportation facilities in Puerto Rico. The Authority is a separate entity from the Department for purposes of financing and constructing Puerto Rico’s transportation system, but since 1971, the Secretary of Transportation and Public Works (the “Secretary”), appointed by the Governor, has overseen the management of the Authority and exercises the powers of the Governing Board of the Authority.

The Authority has adopted a long-term master plan for development of the transportation infrastructure necessary to foster and sustain Puerto Rico’s economic growth and a five-year Construction Improvement Program to implement that plan. (The current Construction Improvement Program covers the period from fiscal year 2004, which ends on June 30, 2004, through fiscal year 2008). As required by the 1968 Resolution and the 1998 Resolution, the Authority supplements the master plan as necessary and annually updates the five-year Construction Improvement Program.

The Authority Act gives the Authority broad powers to carry out its responsibilities in accordance with the Department’s overall transportation policies. These powers include, among other things, the complete control and supervision of any highway and other transportation facilities owned, operated or constructed by it; the ability to set tolls and other charges for the use of the highway and other transportation facilities; and the power to issue bonds, notes or other obligations. The Authority plans and manages the construction of all major projects relating to Puerto Rico’s transportation system, undertakes major repairs and maintains the toll highways. The Department maintains Puerto Rico’s highway system, other than the toll highways, and undertakes construction of smaller projects. As noted above, the Assignment Agreement reaffirms that the Department has designated the Authority as the exclusive agency of the Commonwealth to receive Federal Transportation Funds.

The Authority made a revision of the highway classification system during fiscal year 1999. The new functional classification implemented includes the following categories: primary, primary urban, secondary, and tertiary.

As of December 31, 2003, the Commonwealth had 4,589 miles of highways and 10,592 miles of local streets and roads. The highway system comprises 379 miles of primary system highways, which are the more important inter-regional traffic routes and include the Luis A. Ferré (PR-52), the De Diego (PR-22), PR-53 and Martínez Nadal (PR-20) toll highways, 229 miles of primary urban system highways, 954 miles of secondary system highways serving the needs of intra-regional traffic and 3,027 miles of tertiary highways and roads and public housing development roads serving local, intra-regional traffic.

In August 1990, the Authority Act was amended to empower the Authority to enter into concession agreements, subject to approval by a government board of adjudications, with private parties for the design, construction, operation and maintenance of highway projects. Such projects, to be owned by the Authority and the Commonwealth, could be financed by such private parties by the imposition of tolls or otherwise. To date, the only highway facility subject to a private concession agreement is the Teodoro Moscoso Bridge which is operated by Autopistas de Puerto Rico y Compañía, S.E.

In March 1991, the Authority Act was further amended to authorize the Authority to work with and implement policies established by the Secretary for the purpose of developing a multi-modal transportation system for the Commonwealth to alleviate traffic congestion. In line with this expanded power, the Authority undertook the planning, design, construction and operation of Tren Urbano, a mass transit rail project for the San Juan Metropolitan area. See “Operating Expenses and Capital Expenditures – Construction Improvement Program – Tren Urbano” under TRANSPORTATION REVENUES OR EXPENDITURES.

Organization

To carry out its responsibilities to develop the Commonwealth’s transportation system, the Authority is organized into the Executive Director’s Office, which provides overall management of the Authority, and the offices of four Deputy Executive Directors, each of whom reports to the Executive Director. The Deputy Executive Director for Infrastructure oversees the Planning Area, which is responsible for the development of the Construction Improvement Program as well as long-term planning; the Design Area, which is responsible for designing and supervising the design by consultants of Authority projects; the Property Acquisition Area, which acquires necessary easements and rights-of-way for Authority projects; and the Construction Area, which supervises and inspects the construction work performed by the Authority’s contractors. The Deputy Executive Director for Administration and Finance oversees the Finance Area, which is responsible for the financial affairs of the Authority, including budgetary services; the Administration Area, which provides administrative support to the Authority; and the Information Technologies Area, which oversees computer operations. The Deputy Executive Director for Human Resources oversees personnel services and recruitment. The Deputy Executive Director for Traffic and Toll Operations oversees all aspects of the operation, maintenance, and repair of the Martínez Nadal (PR-20), the Luis A. Ferré (PR-52), De Diego (PR-22), and PR-53 toll highways. Most construction, renovation and improvement of highway facilities is performed by private contractors selected through a public bidding process mandated by the Authority Act. The Authority plans, inspects and supervises such work.

Management

The Secretary of Transportation and Public Works, who has ultimate managerial power over the Authority, is Fernando E. Fagundo, Ph.D. Dr. Fagundo was appointed Secretary by the Governor of Puerto Rico on December 19, 2002. Prior to his appointment as Secretary, Mr. Fagundo was the Executive Director of the Authority. Prior to joining the Authority, Dr. Fagundo was Engineering Director of the engineering consulting firm of CSA Group and a professor of structural engineering at the University of Florida in Gainesville, Florida. Dr. Fagundo received a B.S. degree in civil engineering as well as a master’s degree in civil engineering from the University of Puerto Rico and a Ph.D. in structural engineering from Cornell University.

The Executive Director of the Authority, who oversees the Authority’s operations, is Jack T. Allison, Ph.D. Dr. Allison was appointed Executive Director of the Authority on December 19, 2002. Prior to his appointment as Executive Director, Dr. Allison was the Authority’s Deputy Executive Director. He also served as project manager of the Tren Urbano project and as President of the Bids Award Board since February of 2001. Dr. Allison holds a doctorate in industrial engineering from Texas A&M University and a bachelor’s degree from the University of Puerto Rico (Mayaguez campus). He has served on the faculty of the University of Puerto Rico for 26 years, including four years as the University’s dean of engineering. Dr. Allison has also worked as a consultant in the private sector and has written a number of scientific papers.

The Authority retains the firm of Roy Jorgensen Associates, Inc. as independent traffic engineers to carry out certain responsibilities under the 1968 Resolution and the 1998 Resolution. These include an annual evaluation of the Authority’s master plan and Construction Improvement Program for capital improvements and the maintenance activities of the Department and the Authority with respect to Puerto Rico’s highway system. The Authority employs Ernst & Young LLP as independent accountants responsible for auditing the Authority’s books and accounts.

The administrative offices of the Authority are in the Minillas Government Center, De Diego Avenue, Stop 22, San Juan, Puerto Rico. The mailing address is P.O. Box 42007, San Juan, Puerto Rico 00940-2007. The telephone number is (787) 721-8787.

Employee Relations

As of December 31, 2003, the Authority employed 3,634 persons, of whom 215 were high management officials, 1,555 were professionals and office workers, and 1,864 were technicians and laborers. Of the total number of employees, 2,015 were permanent employees and 1,619 were temporary employees. The Authority believes that relations with its employees are good.

In 1987, the Puerto Rico Supreme Court classified the Authority as a “private employer” for purposes of the Puerto Rico labor law provisions, permitting the Authority’s employees to engage in collective bargaining. An independent union, representing approximately 969 of the Authority’s 2,015 permanent employees, has been certified for collective bargaining purposes. The current collective bargaining agreement expires on June 30, 2005.

TRANSPORTATION SYSTEM REVENUES AND EXPENDITURES

Revenues

Various factors affect the level of 1998 Resolution Revenues and 1968 Resolution Revenues available to the Authority, including, in particular, general economic conditions, the supply and cost of crude oil and gasoline and other oil-derived fuels. These factors have an impact on motor vehicle usage and fuel consumption and are discussed further below. In addition, decisions by the Authority as to the types and level of charges it may impose for the use of its Transportation Facilities will affect the amount of moneys available to the Authority for its authorized purposes.

Sources of 1998 Resolution Revenues

Petroleum Products Tax. On July 16, 1997, the 1994 Code was amended by Act No. 34 to allocate to the Authority, beginning on July 16, 1997, the total amount of excise taxes, up to \$120 million per fiscal year, imposed by the Commonwealth on petroleum products (which includes crude oil, unfinished oil and derivative products.) The tax is imposed on any petroleum product introduced, consumed, sold or transferred in the Commonwealth. The petroleum products tax rate varies on a monthly basis according to an index price of crude oil determined by the Department of the Treasury (based on the market price of crude oil quoted in certain markets specified in the 1994 Code), as follows:

<u>Index Price of Crude Oil (per barrel)</u>	<u>Rate of Tax (\$ per barrel)</u>
\$0.01 to \$16.00	\$6.00
\$16.01 to \$24.00	\$5.00
\$24.01 to \$28.00	\$4.00
\$28.01 and higher	\$3.00

Petroleum products taxes are collected by the Department of the Treasury. All taxes collected, up to \$11 million per month, are deposited in a special fund in favor of the Authority (the “Special Fund) and transferred on a monthly basis to the Authority during the first ten months of the fiscal year. All taxes collected during the last two months of each fiscal year are also transferred, subject to the \$120 million annual limit. If the total amount of the taxes collected by the Department of the Treasury and transferred to the Authority in any month is less than \$11 million, such deficiency must be made up by the Department of the Treasury with the amount of such taxes in excess of \$11 million which were collected in any prior month or which may be collected in any subsequent month of the same fiscal year.

The following table presents the number of barrels of crude oil on which the petroleum products tax was imposed, the average annual tax rate (per barrel) and the total taxes collected by the Department of the Treasury in each fiscal year since fiscal 1987 (the first full fiscal year in which the tax was collected).

COLLECTIONS OF PETROLEUM PRODUCTS TAX

Fiscal Year Ended June 30,	Number of Barrels Taxed (millions)	Average Annual Tax Rate* (\$ per barrel)	Total Tax Collected (\$ million)
1987	23.67	\$4.91	\$119.90
1988	22.13	4.41	98.54
1989	25.11	5.00	128.23
1990	22.74	4.91	112.79
1991	26.80	4.16	112.17
1992	24.07	5.00	120.37
1993	26.09	5.00	130.47
1994	28.27	5.42	152.91
1995	27.90	5.00	139.59
1996	31.55	5.00	157.74
1997	32.29	4.92	158.74
1998	32.20	5.33	171.64
1999	31.70	6.00	190.10
2000	32.20	4.50	144.80
2001	34.82	3.50	121.90
2002	35.88	4.42	158.60
2003	38.00	3.50	132.90

*The average annual tax rate is the arithmetic average of the monthly tax rate determined by the Department of the Treasury during such fiscal year. The total tax collected is the actual amount of tax collected during the fiscal year. Due to the monthly fluctuations in the tax rate, the total tax collected is different from the result produced from multiplying the number of barrels taxed by the average annual tax rate.

Source: Department of the Treasury and the Authority.

In the first six months of the current fiscal year (July 1, 2003 through December 31, 2003), the Department of the Treasury transferred to the Authority \$60 million from petroleum product taxes collected. Although crude oil prices have been relatively high (and consequently the tax rate has been relatively low) during the current fiscal year, the Authority expects to receive the full \$120 million allocated to it during this fiscal year. Since the Authority has been allocated the full amount of these taxes collected up to \$120 million per fiscal year, the Authority is not affected by reductions in collections of these taxes unless such collections fall below \$120 million in a fiscal year. In the event the price of crude oil remains high for an extended period, the Authority believes that petroleum products taxes collected could fall below \$120 million per fiscal year, but that such collections should not fall below \$110 million per fiscal year.

The 1994 Code authorizes the Authority to pledge the entire amount of petroleum products tax allocated to the Authority (not to exceed \$120 million in any fiscal year) to the payment of the principal of and interest on bonds and other obligations of the Authority or for any other lawful purpose of the Authority. The Authority has pledged the petroleum products tax receipts to the holders of the Transportation Revenue Bonds, but such pledge is subject to the Constitution of Puerto Rico, which permits the Commonwealth to apply such tax receipts to the payment of certain Commonwealth debts to the extent other Commonwealth moneys are insufficient therefor. The Commonwealth has agreed and committed in the 1994 Code not to eliminate or reduce the rates of excise tax on petroleum products in effect on July 16, 1997 (set forth above) and the amount of such taxes allocated to the Authority until all obligations of the Authority secured by the pledge thereof, together with the interest thereon, are fully paid. Any petroleum product tax collected in excess of \$120 million per fiscal year is not required to be allocated to the Authority and is not pledged by the Authority to the holders of Transportation Revenue Bonds.

Tolls and Other Charges. The Authority is authorized to impose tolls and other charges on its Transportation Facilities. Until the 1968 Resolution is repealed and canceled, all Existing Toll Facilities Revenues will constitute 1968 Resolution Revenues and are pledged to the payment of the Transportation Revenue Bonds only to the extent they become Excess 1968 Resolution Revenues. Upon the repeal and cancellation of the 1968 Resolution, the Existing Toll Facilities Revenues will constitute 1998 Resolution Revenues and will be pledged to the payment of the Transportation Revenue Bonds.

The Authority is not pledging the fare box revenues of Tren Urbano to the payment of the bonds issued under the 1998 Resolution or the 1968 Resolution.

The Authority Act grants to the Authority plenary power to fix, impose, alter and collect tolls and other reasonable charges for the use of the Transportation Facilities operated by the Authority or for services rendered thereby. The Authority is obligated to take into account in setting or changing such tolls and other charges such factors as will promote the use of the Transportation Facilities in the broadest and most varied manner economically possible. Prior to fixing or altering such tolls or other charges, the Authority must hold a public hearing to receive comments with respect thereto.

Excess 1968 Resolution Revenues. Before the repeal and cancellation of the 1968 Resolution, the Excess 1968 Resolution Revenues (which consist of all unencumbered 1968 Resolution Revenues remaining after payment of debt service and required reserves on the outstanding Highway Revenue Bonds issued under the 1968 Resolution) are included as 1998 Resolution Revenues. After the payment or defeasance of all Highway Revenue Bonds and the repeal and cancellation of the 1968 Resolution, all 1968 Resolution Revenues will become 1998 Resolution Revenues. The sources of the 1968 Resolution Revenues are discussed below.

Investment Earnings. Moneys held for the credit of the 1998 Senior Bond Service Account, the 1998 Senior Bond Redemption Account, the 1998 Subordinated Bond Service Account and the 1998 Subordinated Bond Redemption Account shall, as nearly as may be practicable, be continuously invested and reinvested at the written direction of the Authority in Government Obligations. Moneys held for the credit of the 1998 Senior Bond Reserve Account and each account in the 1998 Subordinated Bond Reserve Fund shall, as nearly as may be practicable, be continuously invested and reinvested at the written direction of the Authority in Investment Obligations. Such Government Obligations and Investment Obligations shall mature, or be subject to redemption, at the option of the holder, not later than the respective dates when moneys held for the credit of such Accounts will be required for the purposes intended; provided, however, that the amounts on deposit in the 1998 Senior Bond Reserve Account and each account in the 1998 Subordinated Bond Reserve Fund shall be invested in Investment Obligations which mature not later than the final maturity date of any Senior Transportation Revenue Bonds or Subordinated Transportation Revenue Bonds outstanding. Income from investments of moneys held for the credit of the 1998 Construction Fund is not considered 1998 Resolution Revenues under the 1998 Resolution.

Sources of 1968 Resolution Revenues

General. The major sources of the Authority's 1968 Resolution Revenues are the gasoline tax and the gas oil and diesel oil tax allocated to the Authority pursuant to the 1994 Code, the motor vehicle license fee allocated to the Authority pursuant to Act No. 9 and the toll charges on the Authority's existing toll highways, including tolls collected on any extension thereof however financed. In fiscal 2003, 1968 Resolution Revenues were derived 47% from gasoline taxes, 37% from toll charges, 9% from motor vehicle license fees, 4% from gas oil and diesel oil taxes and 3.5% from investment earnings.

Gasoline and Gas Oil Taxes. The 1994 Code currently imposes a \$0.16 per gallon tax on gasoline and an \$0.08 per gallon tax on gas oil and diesel oil, provides for the deposit of the entire \$0.16 tax on gasoline and \$0.04 of the tax on gas oil and diesel oil in the Special Fund, and authorizes the Authority to pledge such amounts to the payment of the principal of and interest on its bonds and other obligations or for any other lawful purpose of the Authority. The Authority has pledged such tax receipts to the holders of the Highway Revenue Bonds, but such pledge is subject to the Constitution of Puerto Rico, which permits the Commonwealth to apply such taxes to payment of certain Commonwealth debts to the extent other Commonwealth moneys are insufficient therefor. The Authority has also pledged such tax receipts to the holders of the Transportation Revenue Bonds, subject to the prior application of such tax receipts to the payment of debt service on Highway Revenue Bonds and the maintenance of a reserve therefor. The Commonwealth has agreed and committed in the 1994 Code that the tax on gasoline will not be reduced below \$0.16 per gallon and the tax on gas oil and diesel oil will not be reduced below \$0.04 per gallon and that the amount of such taxes allocated to the Authority will not be reduced until all obligations of the Authority secured by the pledge thereof, together with the interest thereon, are fully paid. Gasoline taxes and gas oil and diesel oil taxes which may be levied or collected from time

to time other than the amounts of the taxes and fees described in this paragraph are not required to be allocated to the Authority or pledged by the Authority to the holders of the Highway Revenue Bonds or the Transportation Revenue Bonds.

Gasoline taxes, gas oil and diesel oil taxes are collected by the Department of the Treasury. The portions of such taxes allocated to the Authority are transferred to the Authority at least monthly as such taxes are collected.

The Department of the Treasury periodically conducts an audit of gasoline, gas, oil, diesel oil and petroleum products importers, producers and wholesalers to verify amounts reported and paid. In addition to such audit procedures, the Authority reviews monthly the records of the Department of the Treasury for consistency with monthly reports provided to the Authority by distributors of oil, gasoline and petroleum products.

Motor Vehicle License Fees. Under the Vehicle and Traffic Law (Act No. 141 of the Legislature of Puerto Rico, approved July 20, 1960, as amended), the Commonwealth imposes annual license fees on various classes of motor vehicles. The current license fees range from \$25 to \$40 for passenger cars and vary for other vehicles. Act No. 9 increased the per vehicle annual motor vehicle license fees by \$15 and provided for the deposit of the proceeds of the \$15 increase in the Special Fund for the Authority, which may pledge such proceeds to the payment of debt service on obligations of the Authority or any other legal purpose of the Authority. As with the gasoline and gas and diesel oil taxes described above, the Authority has pledged such license fees to the holders of the Highway Revenue Bonds and, subject to the prior application of such fees to the payment of debt service on Highway Revenue Bonds and the maintenance of a reserve therefor, the Authority has also pledged such fees to the holders of the Transportation Revenue Bonds. Such fees are also collected by the Department of the Treasury and the portion of such fees allocated to the Authority is transferred to the Authority at least monthly, as such fees are collected. Under Act No. 9, the Commonwealth has agreed and pledged that the license fees allocated to the Authority, as described herein, will not be reduced so long as such proceeds remain pledged to the payment of such obligations.

Tolls on Existing Toll Highways. Until the 1968 Resolution is repealed and canceled, all tolls collected on the Authority's existing toll highways, including tolls collected on any extension thereof financed with Transportation Revenue Bonds (the "Existing Toll Facilities Revenues"), will constitute 1968 Resolution Revenues. As such, they will be pledged to the payment of the Highway Revenue Bonds and, subject to the prior application of such toll revenues to the payment of debt service on the Highway Revenue Bonds and the maintenance of a reserve therefor, will be additionally pledged to the payment of Transportation Revenue Bonds.

Under the 1968 Resolution, the Authority has covenanted not to reduce or eliminate any tolls and other charges for the use of Traffic Facilities if such tolls and other charges have been taken into account in the calculation of 1968 Resolution Revenues for purposes of satisfying the tests for the issuance of additional bonds under the 1968 Resolution and if the 1968 Resolution Revenues for any 12 consecutive months out of the immediately preceding 15 months prior to the proposed adjustment, after adjusting such revenues for the proposed decrease in tolls, would have been less than 150% of the maximum Principal and Interest Requirements for any fiscal year thereafter for all Highway Revenue Bonds then outstanding. Such tolls and other charges have been taken into account for satisfying such additional bonds' test under the 1968 Resolution.

The Authority has also covenanted, under the 1998 Bond Resolution, that it will not reduce or eliminate any tolls or other charges imposed for the use of its Toll Facilities unless the 1998 Resolution Revenues received by the Authority for any 12 consecutive months out of the 15 months immediately prior to such reduction (adjusted to give effect for such entire 12 months to moneys allocated to and pledged by the Authority to the payment of the Transportation Revenue Bonds under legislation enacted and toll rate changes made effective on or prior to the effective date of any such toll reduction, and tolls from Toll Facilities which have begun operations or been removed from operation during such 12 months) is at least equal to 150% and 100% of the maximum Principal and Interest Requirements for any fiscal year thereafter for all Senior Transportation Revenue Bonds then outstanding and for all Transportation Revenue Bonds then outstanding, respectively.

Tolls are currently imposed on the Luis A. Ferré toll highway (PR-52), which extends 67 miles from San Juan to Ponce, the De Diego toll highway (PR-22), which extends 52 miles from San Juan to Arecibo, and PR-53, which will connect Fajardo and Salinas upon its completion, a distance of 57 miles. Approximately 37 miles of PR-53 have been completed. The Luis A. Ferré toll highway has four toll stations in the northerly direction and three toll stations in the southerly direction, and the total minimum toll for a vehicle making a round-trip between San Juan and Ponce is currently \$3.65. An extension of the Luis A. Ferré toll highway bypassing Ponce includes a toll station with a minimum toll of \$0.50. The De Diego toll highway has six toll stations, and the total minimum toll for a vehicle passing through all six stations is \$2.40. PR-53 currently has five toll stations with a total minimum toll of \$1.55. The Martínez Nadal toll

highway (PR-20), which was inaugurated in July 2000, extends 6.0 miles, connects PR-2 with PR-1 at the La Muda sector near Caguas and has one toll station with a minimum toll of \$0.50. The Authority expects to inaugurate the first toll stations of the PR-5 toll highway (which connects PR-2 to PR-199, Las Cumbres) in fiscal 2004 and the Eastern Corridor toll highway (described below) during fiscal 2006, with minimum tolls of \$0.50 and \$1.00, respectively.

The Authority is currently implementing a highway-speed electronic toll collection (ETC) system. The new system is being implemented and financed by a private sector firm. The new technology, which employs radio transmissions from transponder-equipped vehicles to plaza-mounted antennas and video systems for violation enforcement, is intended to significantly increase vehicle throughput at toll plazas without costly infrastructure expansion, which should result in reduced travel time and increased convenience for customers. Direct benefits to the Authority include reduced cost of toll collection, enhanced auditing capabilities, additional payment option offering and receipt of toll payments in advance. The ETC project became operational on the Buchanan, Toa Baja, Vega Alta, Caguas Norte, Caguas Sur and Salinas toll plazas in March 2004.

The Authority's toll highway revenues have always exceeded its toll highway operation and maintenance expenses. Toll highway revenues and operation and maintenance expenses for fiscal 2003 were \$135.4 million and \$38.9 million, respectively, compared to \$130.5 million and \$37.3 million, respectively, for fiscal 2002.

Investment Earnings. Moneys held for the credit of the 1968 Bond Service Account and the 1968 Redemption Account shall, as nearly as may be practicable, be continuously invested and reinvested at the written direction of the Authority in Government Obligations. Moneys held for the credit of the 1968 Reserve Account shall, as nearly as may be practicable, be continuously invested and reinvested at the written direction of the Authority in Investment Obligations. Such Government Obligations and Investment Obligations shall mature, or be subject to redemption, at the option of the holder, not later than the respective dates when moneys held for the credit of such Accounts will be required for the purposes intended; provided, however, that the amounts on deposit in the 1968 Reserve Account shall be invested in Investment Obligations which mature not later than the final maturity date of any Highway Revenue Bonds outstanding. Income from investments of moneys held for the credit of the 1968 Construction Fund is not considered 1968 Resolution Revenues under the 1968 Resolution.

Historical Revenues

The following table presents the Authority's revenues, debt service and debt service coverage ratio for the five fiscal years ended June 30, 1999 to June 30, 2003 and for the six-month periods ending December 31, 2002 and December 31, 2003. Under the 1998 Resolution, the Excess 1968 Resolution Revenues representing unencumbered funds in the 1968 Construction Fund must be deposited monthly in the 1998 Revenue Fund and are available for the payment of debt service on Transportation Revenue Bonds, for required deposits to the reserve accounts established thereunder and for other authorized purposes under the 1998 Resolution.

HISTORICAL REVENUES AND DEBT SERVICE COVERAGE
(dollars in thousands)

	Fiscal Year ended June 30,					Six Months of Fiscal Year Ended*	
	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2003</u>	<u>2004</u>
1968 Resolution Revenues:							
Gasoline taxes (1)	\$168,397	\$176,737	\$169,782	\$174,885	\$173,507	\$89,216	\$89,865
Gas oil and diesel oil taxes (2)	<u>20,711</u>	<u>22,520</u>	<u>20,491</u>	<u>18,922</u>	<u>15,298</u>	<u>7,934</u>	<u>8,116</u>
Subtotal	\$189,108	\$199,257	\$190,273	\$193,807	\$188,805	\$97,150	\$97,981
Motor vehicle license fees	<u>28,089</u>	<u>28,996</u>	<u>29,772</u>	<u>30,693</u>	<u>31,920</u>	<u>15,663</u>	<u>16,342</u>
Subtotal	\$217,197	\$228,253	\$220,045	\$224,500	\$220,725	\$112,813	\$114,323
Toll receipts	116,030	120,524	125,695	130,498	135,352	67,412	69,472
Investment income	<u>14,314</u>	<u>16,852</u>	<u>10,260</u>	<u>10,168</u>	<u>12,947</u>	<u>5,662</u>	<u>5,293</u>
Total 1968 Resolution Revenues	<u>\$347,541</u>	<u>\$365,629</u>	<u>\$356,000</u>	<u>\$365,166</u>	<u>\$369,024</u>	<u>\$185,887</u>	<u>\$189,088</u>
Debt Service on Highway Revenue Bonds	\$180,787	\$181,988	\$181,727	\$177,400	\$95,120	\$75,279	\$60,361
Excess 1968 Resolution Revenues	<u>\$166,754</u>	<u>\$183,641</u>	<u>\$174,273</u>	<u>\$187,766</u>	<u>\$273,904</u>	<u>\$110,608</u>	<u>\$128,727</u>
1998 Resolution Revenues:							
Petroleum Products Tax	\$120,000	\$120,000	\$120,000	\$120,000	\$120,000	\$66,000	\$66,000
Excess 1968 Resolution Revenues	166,754	183,641	174,273	187,766	273,904	110,608	128,727
Investment income	<u>3,840</u>	<u>5,069</u>	<u>7,456</u>	<u>11,198</u>	<u>11,586</u>	<u>5,684</u>	<u>6,009</u>
Total 1998 Resolution Revenues	<u>\$290,594</u>	<u>\$308,710</u>	<u>\$301,729</u>	<u>\$318,964</u>	<u>\$405,490</u>	<u>\$182,292</u>	<u>\$200,736</u>
Debt Service on Senior Transportation Revenue Bonds	\$64,832	\$64,410	\$102,194	\$116,150	\$135,068	\$74,908	\$80,119
Senior coverage ratio ⁽³⁾	4.48	4.79	2.95	2.75	3.00	--	--
Total 1998 Resolution Revenues available to pay Subordinated Transportation Revenue Bonds ⁽⁴⁾	<u>\$225,762</u>	<u>\$244,300</u>	<u>\$199,535</u>	<u>\$202,814</u>	<u>\$270,422</u>	<u>\$107,384</u>	<u>\$120,617</u>
Debt Service on Subordinated Transportation Revenue Bonds	\$3,426	\$3,795	\$3,795	\$3,795	\$6,654	\$1,878	\$10,199
Senior and Subordinated coverage ratio ⁽⁵⁾	4.26	4.50	2.85	2.66	2.86	--	--
Aggregate Revenues ⁽⁶⁾	\$471,381	\$490,698	\$483,456	\$496,364	\$500,610	\$257,571	\$261,097
Aggregate Debt Service ⁽⁷⁾	\$249,045	\$250,193	\$303,171	\$314,565	\$251,258	\$160,695	\$150,679
Aggregate Coverage Ratio ⁽⁸⁾	1.89	1.96	1.59	1.58	1.99	--	--

* Refers to six-month period July 1 through December 31 of each fiscal year.

- (1) Excludes \$10.2 million, \$10.3 million and \$2.7 million for fiscal years 1999, 2000 and 2001, respectively, in delinquent taxes owed by one taxpayer.
- (2) Excludes \$1.4 million, \$1.5 million and \$28,000 for fiscal years 1999, 2000 and 2001, respectively, in delinquent taxes owed by one taxpayer.
- (3) Equals ratio of Total 1998 Resolution Revenues to Debt Service on the Senior Transportation Revenue Bonds for the fiscal year in question.
- (4) Represents Total 1998 Resolution Revenues less Debt Service on Senior Transportation Revenue Bonds.
- (5) Equals ratio of Total 1998 Resolution Revenues to Debt Service on the Senior Transportation Revenue Bonds and the Subordinated Transportation Revenue Bonds for the fiscal year in question.
- (6) Represents the sum of Total 1968 Resolution Revenues and Total 1998 Resolution Revenues (less Excess 1968 Resolution Revenues) for the fiscal year in question.
- (7) Represents the sum of Debt Service on the Highway Revenue Bonds, the Transportation Revenue Bonds and Debt Service on a \$300 million loan from the federal government (repaid in full in April 2003) incurred to finance a portion of the costs of construction of Tren Urbano.
- (8) Aggregate Revenues divided by Aggregate Debt Service.

The Authority's 1968 Resolution Revenues rose at a compound annual rate of 1.5% during the period from fiscal 1999 through fiscal 2003 due primarily to the growth in tax collections and toll receipts.

Gasoline taxes, which accounted for approximately 47% of 1968 Resolution Revenues for fiscal 2003, remained stable during this five-year period. The number of vehicles in the Commonwealth decreased from approximately 2.5 million to approximately 2.2 million from fiscal year 1999 to fiscal 2002 mainly as a result of a revision on the data for inventory of registered vehicles. This inventory revision, however, did not affect the revenues for vehicles license fees which have been increasing every year. The amount of gasoline taxes collected during the 1999, 2000 and 2001 fiscal years varied significantly from the amount projected as a result of delinquencies by one gasoline wholesaler which filed for bankruptcy. This wholesaler currently owes the Puerto Rico Treasury Department approximately \$8.9 million in

gasoline and gas oil and diesel taxes, and approximately \$170 million in other taxes. The Treasury Department expects to collect only a fraction of the amount owed. The Treasury Department does not anticipate that the amount of delinquent taxes owed by this wholesaler will increase because its right to introduce and sell gasoline and diesel products under a bond has been revoked and the taxpayer must now pay the applicable taxes before these products are introduced into the Commonwealth. The Authority does not expect that the bankruptcy of this wholesaler will have any material adverse impact on aggregate gasoline and gas oil and diesel oil consumption, and therefore on future revenues of the Authority.

Gas oil and diesel oil tax receipts, which accounted for approximately 4.2% of 1968 Resolution Revenues for fiscal 2003, increased from fiscal 1999 through fiscal 2000, and decreased from fiscal 2000 through fiscal 2003. This decrease, which is expected to continue until the end of fiscal 2005, resulted primarily from the Puerto Rico's Electric Power Authority's decision to increase the amount of electricity purchased from private co-generation plants using natural gas and coal as fuels. For the first six months of fiscal 2004, gas oil and diesel oil taxes increased by 2.8% over the same period in fiscal 2003.

Toll receipts rose at an average compound annual rate of 3.9% during the period from fiscal 1999 through fiscal 2003, increasing in every year during the period. Toll receipts have grown as a percentage of total 1968 Resolution Revenues over the last five fiscal years, from 33% in 1999 to 37% in fiscal 2003. This increase corresponded principally to the growing number of vehicles using toll roads, and the expansion of the toll highway network. For the first six months of fiscal 2004, toll receipts increased by 3.1% over the same period in fiscal 2003.

Motor vehicle license fees accounted for approximately 8.4% of annual 1968 Resolution Revenues for fiscal 2003. From fiscal 1999 to fiscal 2003, fee collections rose at a compound annual rate of 3.2%. For the first six months of fiscal 2004, motor vehicle license fees decreased by 0.15% over the same period in fiscal 2003.

The revenues allocated to the Authority from the petroleum products tax are capped at \$120 million in each fiscal year. The Authority received this amount each year during the five fiscal years ending on June 30, 2003. As mentioned above, for the first six months of fiscal 2004, the Authority has received or accrued the maximum amount permitted by law, \$66 million, as it did in the first six months of fiscal 2003.

The foregoing discussion of past revenue growth is not intended to be predictive of future revenue growth. In particular, the Authority is anticipating that two new toll facilities, PR-5 and the Eastern Corridor (discussed below), will be coming into service prior to fiscal 2008. Economic conditions in Puerto Rico, as well as the price of oil and petroleum products and the levels of automobile registration and usage, will affect the Authority's revenues in the future.

Projected 1968 Resolution Revenues and 1998 Resolution Revenues

The following table presents the Authority's estimates of 1968 Resolution Revenues for each of the five fiscal years ending June 30, 2004 to June 30, 2008 and its estimates of 1998 Resolution Revenues expected to be available for the payment of debt service on its Transportation Revenue Bonds, including Transportation Revenues Bonds expected to be issued during this period, together with debt service coverage for each of the five fiscal years ending June 30, 2004 to 2008, inclusive. The projected 1968 Resolution Revenues and 1998 Resolution Revenues shown below are based on tax rates and allocations to the Authority now in effect and debt service is based on Highway Revenue Bonds and Transportation Revenue Bonds currently outstanding and projected to be issued during the forecast period. Such projections are subject to periodic review and may be adjusted to reflect such factors as changes in general economic conditions, in the demand for gasoline and other petroleum products and in the levels of automobile registration and usage. The projections are based on assumptions which the Authority believes to be reasonable; however, there is no assurance that the projections will prove to be accurate.

PROJECTED REVENUES AND DEBT SERVICE COVERAGE ¹

**Fiscal year ending June 30,
(dollars in thousands)**

	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>
<u>1968 Resolution Revenues:</u>					
Gasoline taxes	\$178,900	\$187,580	\$191,640	\$195,690	\$199,750
Gas oil and diesel oil taxes	<u>17,160</u>	<u>19,200</u>	<u>23,160</u>	<u>24,090</u>	<u>24,900</u>
Subtotal	196,060	206,780	214,800	219,780	224,650
Motor vehicle license fees	<u>33,590</u>	<u>34,480</u>	<u>35,370</u>	<u>36,260</u>	<u>37,150</u>
Subtotal	229,650	241,260	250,170	256,040	261,800
Toll receipts	141,960	147,360	152,950	158,730	164,730
Investment income	<u>9,000</u>	<u>9,700</u>	<u>11,900</u>	<u>11,900</u>	<u>11,900</u>
Total 1968 Resolution Revenues	<u>\$380,610</u>	<u>\$398,320</u>	<u>\$415,020</u>	<u>\$426,670</u>	<u>\$438,430</u>
Debt Service on Highway Revenue Bonds	\$120,723	\$153,925	\$146,832	\$147,116	\$138,057
Excess 1968 Resolution Revenues	<u>\$259,887</u>	<u>\$244,395</u>	<u>\$268,188</u>	<u>\$279,554</u>	<u>\$300,373</u>
<u>1998 Resolution Revenues:</u>					
Petroleum Products Tax	\$120,000	\$120,000	\$120,000	\$120,000	\$120,000
Eastern Corridor Toll Receipts	-	-	25,800	26,800	27,800
Investment income	12,800	14,300	15,100	15,200	15,200
Subtotal 1998 Resolution Revenues	132,800	134,300	160,900	162,000	163,000
Excess 1968 Resolution Revenues	<u>259,887</u>	<u>244,395</u>	<u>268,188</u>	<u>279,554</u>	<u>300,373</u>
Total 1998 Resolution Revenues	<u>\$392,687</u>	<u>\$378,695</u>	<u>\$429,088</u>	<u>\$441,554</u>	<u>\$463,373</u>
Debt Service on Senior Transportation Revenue Bonds ^{2, 10}	\$158,738	\$178,548	\$207,624	\$207,724	\$216,582
Senior coverage ratio ³	2.47	2.12	2.07	2.13	2.14
Additional bonds test, Senior Transportation Revenue Bonds ⁴	1.76	1.69	1.92	1.98	1.61
Total 1998 Resolution Revenues available to pay Subordinated Transportation Revenue Bonds⁵	\$233,950	\$200,147	\$221,464	\$233,831	\$246,791
Debt Service on Subordinated Transportation Revenue Bonds	\$20,398	\$20,398	\$24,018	\$28,269	\$30,365
Senior and Subordinated coverage ratio ⁶	2.19	1.90	1.85	1.87	1.88
Aggregate Revenues ⁷	\$513,410	\$532,620	\$575,920	\$588,670	\$601,430
Aggregate Debt Service ^{8, 10}	\$299,859	\$352,871	\$378,475	\$383,108	\$385,004
Aggregate Coverage Ratio⁹	1.71	1.51	1.52	1.54	1.56

- (1) Assumes that all taxes will be collected on their due dates.
- (2) Assumes the issuance of additional Transportation Revenue Bonds in June of 2005 and 2008 at an assumed average interest rate of 7% per annum with a 30-year final maturity.
- (3) Equals ratio of Total 1998 Resolution Revenues to Debt Service on the Senior Transportation Revenue Bonds for the fiscal year in question.
- (4) This test uses as its denominator maximum annual Debt Service on all Senior Transportation Revenue Bonds outstanding under the 1998 Resolution (including any Senior Transportation Revenue Bonds then proposed to be issued) and as its numerator the 1998 Resolution Revenues of the Authority for the fiscal year in question.
- (5) Represents Total 1998 Resolution Revenues less Debt Service on Senior Transportation Revenue Bonds.
- (6) Equals ratio of Total 1998 Resolution Revenues to Debt Service on the Senior Transportation Revenue Bonds and the Subordinated Transportation Revenue Bonds for the fiscal year in question.
- (7) Represents the sum of Total 1968 Resolution Revenues and Total 1998 Resolution Revenues (less Excess 1968 Resolution Revenues) for the fiscal year in question.
- (8) Represents the sum of Debt Service on the Highway Revenue Bonds and the Transportation Revenue Bonds.
- (9) Aggregate Revenues divided by Aggregate Debt Service.
- (10) Debt service figures shown are net of capitalized interest.

Total 1968 Resolution Revenues and 1998 Resolution Revenues for the period from fiscal 2004 through fiscal 2008 are projected by the Authority to grow at a compound annual rate of 3.6% and 4.2%, respectively. The projected growth in gasoline tax revenues is based on econometric models prepared for the Authority by Applied Research, an independent firm, which project increases in disposable income in Puerto Rico. The Authority has found such projections to be the most reliable indicator of future growth in gasoline tax receipts. The Authority's projections of growth in its other revenues is based on historic trends and, in the case of toll revenues, on the additional receipts expected from the growth in traffic and the opening of new toll plazas such as those located on PR-5 and the Eastern Corridor.

In fiscal year 2003 the Authority's actual revenues exceeded the Authority's projected revenues for such fiscal years. In fiscal 1999 actual revenues fell below the Authority's projections due to one taxpayer's failure to pay the taxes

due on time, as discussed above. In fiscal 2001 and fiscal 2002 actual revenues fell below the Authority's projections due to the unanticipated downturn in the U.S. and Puerto Rico economies. In fiscal 2003, gasoline tax revenues decreased by approximately \$2.0 million due to a change in the method of payment by a taxpayer, which went from paying the applicable gasoline tax at the time of importation to paying the gasoline tax upon consumption.

Operating Expenses and Capital Expenditures

Operation and Maintenance- Highway Facilities

The Department has the responsibility for maintaining Puerto Rico's highway system, except for the Luis A. Ferré (PR-52), the De Diego (PR-22), PR-53 and the Martínez Nadal (PR-20) toll highways and related connecting roads, which are maintained by and at the expense of the Authority. The maintenance expenses of the Department are paid with moneys appropriated annually by the Legislature of Puerto Rico. On occasion the Authority advances funds to pay the costs of emergency repairs which are the responsibility of the Department. It is subsequently reimbursed for these advances. To the extent funds are not provided by the Legislature, the Authority has agreed under the 1998 Resolution that it will pay from available moneys in the 1998 Construction Fund the costs of maintenance of the Traffic Facilities financed with proceeds of Highway Revenue Bonds and Transportation Revenue Bonds. The 1998 Resolution requires the Authority to pay from available moneys in the 1998 Construction Fund (and not from moneys in the 1968 Construction Fund) the costs of any necessary repairs to, or renewals or replacements of, Traffic Facilities financed with proceeds of Highway Revenue Bonds and Transportation Revenue Bonds, as recommended by the transportation engineers retained by the Authority.

The Authority's operation and maintenance expenses payable from available moneys in the 1998 Construction Fund consist of the expenses of operating and maintaining the toll highways and related roads and, upon completion, Tren Urbano. Under the 1998 Resolution, these expenses are payable from available moneys in the 1998 Construction Fund after payment of debt service on the Highway Revenue Bonds and Transportation Revenue Bonds and any required deposits to the 1998 Senior Bond Reserve Account and the accounts in the 1998 Subordinated Bond Reserve Fund. Other expenses of the Authority, including its administration costs, are included in the Construction Improvement Program and are capitalized.

The following table sets forth the annual maintenance expenses paid by the Department for non-toll highways and the annual toll highway operation and maintenance expenses paid by the Authority from unencumbered moneys in the 1998 Construction Fund, for each of the five fiscal years ended June 30, 2003. The table also sets forth the Authority's projections of annual highway maintenance expenses to be paid by the Department for non-toll highways and projected annual toll highway operation and maintenance expenses to be paid by the Authority from unencumbered moneys in the 1998 Construction Fund for the five fiscal years ending June 30, 2008.

HIGHWAY FACILITIES OPERATION AND MAINTENANCE EXPENSES (in thousands)

Fiscal Year Ended June 30	Department		Authority		Total
	Contributions of the Authority to the Department	Non-Toll Highway Maintenance	Toll Highway Maintenance	Toll Highway Operation	
1999	\$10,000	\$18,000	\$16,871	\$15,573	\$32,444
2000	5,000	23,382	20,259	17,258	37,517
2001	5,000	25,177	21,130	18,720	39,850
2002	5,000	24,999	21,060	16,233	37,293
2003	10,000	26,200	21,902	16,882	38,784
2004 ^(p)	5,000	25,700	23,606	19,314	42,920
2005 ^(p)	5,000	28,900	24,624	20,147	44,770
2006 ^(p)	5,000	30,300	25,421	20,799	46,220
2007 ^(p)	5,000	31,700	26,268	21,492	47,760
2008 ^(p)	5,000	33,200	26,818	21,942	48,760

(p) Projected.

In certain years, emergency repairs to the highway system have been necessary, particularly as a result of storm or flood damage. The cost of these repairs is borne by the Department, except for the cost of repairs to the toll highways, which is borne by the Authority. The Department and the Authority generally have been reimbursed from the Federal Emergency Management Agency for some of the costs of such repairs attributable to federally designated disaster areas. The Legislature of Puerto Rico also appropriates funds from time to time for emergency repairs by the Department in addition to amounts appropriated for maintenance.

The traffic engineers retained by the Authority under the 1968 Resolution and 1998 Resolution conduct an annual evaluation of the level of maintenance of the highway system. In their most recent evaluation completed in July 2003, the traffic engineers found that the current level of maintenance was generally adequate. For fiscal year 2000, the Authority incurred a higher increase in toll highway maintenance expense than what it had experienced in prior years due to the purchase of equipment that was not capitalized. For fiscal 2001 and subsequent years, the Authority has increased the amounts budgeted for toll highway maintenance to reflect an expanded toll highway network and increase levels of maintenance. The projected maintenance budgets for the next five fiscal year periods show an annual rate of growth of 4.3% for both non-toll roads and toll highways. The traffic engineers believe that the Authority's maintenance program represents an adequate level of maintenance to preserve the investment and provide an acceptable level of service. The results of the traffic engineers' most recent maintenance evaluation are summarized in the letter of such traffic engineers included as Appendix V.

Operation and Maintenance - Tren Urbano

The Authority has entered into a Systems and Test Track Turnkey Contract (the "STTT Contract") with the Siemens Transit Team ("STT") covering, among other things, the operations and maintenance of Tren Urbano. The operations portion of the contract is for an initial term of five years with an option by the Authority to extend the term for an additional five years. Under the STTT Contract, STT is responsible for operating and maintaining Tren Urbano and is entitled to receive for such services an annual base compensation, which is subject to an inflation adjustment for changes in the cost of labor (based on the changes to consumer price index) and materials (based on the changes to producer price index). The base compensation does not include the cost of insurance and electricity which is paid separately by the Authority. In addition, STT is entitled to receive incentive compensation, and is subject to penalties, based on meeting or not meeting certain operating and maintenance performance measures.

The Authority also plans to contract the services of over 500 "minibus" drivers and integrate these services with Tren Urbano and with the Metropolitan Bus Authority's services. The costs of this initiative, known as the "Integrated Transportation Alternative" or "ATI," are included in the Tren Urbano's operating costs described below.

The table below shows the Authority's estimate of the annual operating and maintenance expenses of Tren Urbano for the first ten years of service. These estimates are based upon the terms of the STTT Contract and include an inflation adjustment and the Authority's estimate of the cost of insurance and electricity.

Estimated Tren Urbano Annual Operating and Maintenance Expenses (in millions)

Year of Service*	1	2	3	4	5	6	7	8	9	10
Estimated Annual Operation and Maintenance Cost	\$96.1	\$97.5	\$101.1	\$102.8	\$105.3	\$112.2	\$114.9	\$117.2	\$120.3	\$123.4

*Based on twelve full months of operation starting from the date when the system opens for service and includes the cost of van and bus connections to Tren Urbano.

The Authority projects that the annual net operating costs of Tren Urbano, after deducting expected operating revenues from operating and maintenance costs, will increase during the first ten years of operation from \$70.6 million (for the first partial year) to \$83.8 million per year. This estimate is based, among other factors, on an annual average daily ridership of 115,000 passengers by the tenth year of operations, and an initial ridership in the first full year of operation of approximately 64% of the ridership expected for the tenth year, with ridership growing for each year of operation. The costs of operating Tren Urbano will be covered by available moneys in the 1998 Construction Fund.

Construction Improvement Program

As required by the 1968 Resolution and the 1998 Resolution, the Authority has developed a master plan to serve as the basis for the long-term planning of Puerto Rico's transportation facilities, which it supplements as necessary. To

implement the plan, the Authority prepares a five-year Construction Improvement Program which is updated annually. The Authority has focused its current Construction Improvement Program on constructing Tren Urbano and improving the primary and primary urban highway facilities, while also addressing the most essential needs of secondary and tertiary roads. The Authority has also included in its Construction Improvement Program the cost of repairs, renewals and replacements to the highway system bridges in the Puerto Rico strategic network, plans for dealing with urban congestion and for local improvements, and certain capitalized expenditures.

The following table presents the Authority's current Construction Improvement Program for the five fiscal years ending June 30, 2008 and the sources of funds required to finance such program. The Construction Improvement Program is subject to various changing factors, including cost increases, variations in availability of internal and external funds, availability of qualified construction resources, the need for emergency repairs and changing traffic patterns. The Authority's projections assume no changes in the statutory taxes and license fees currently allocated to the Authority, and that the Authority will not be required to assume the payment of the Special Facility Revenue Refunding Bonds, 2003 Series A described in "Teodoro Moscoso Bridge" herein.

CONSTRUCTION IMPROVEMENT PROGRAM

	Fiscal Year Ending June 30, (in thousands)					
	2004	2005	2006	2007	2008	Total
Sources of Funds:						
Internally generated funds ⁽¹⁾	\$155,335	\$50,076	\$55,351	\$45,970	\$47,224	\$353,956
Federal aid for highways	51,000	85,636	79,039	79,035	79,073	373,784
Federal aid for Tren Urbano ⁽²⁾	79,700	139,600	40,000	34,300	20,000	313,600
External financing ⁽³⁾	534,008	229,778	233,185	227,735	283,373	1,508,079
Total	\$820,043	\$505,090	\$407,575	\$387,040	\$429,670	\$2,549,419
Uses of Funds:						
Design	\$ 22,533	\$ 4,104	\$ 2,362	\$ 1,698	\$ 218	\$30,914
Rights of way	95,327	34,312	17,474	7,413	9,990	164,516
Construction	440,446	348,497	276,405	271,732	314,462	1,651,542
Capitalized expenditures	108,000	105,000	105,000	105,000	105,000	528,000
Tren Urbano	153,739	13,178	6,333	1,197	-	174,447
Total	\$820,043	\$505,090	\$407,575	\$387,040	\$429,670	\$2,549,419

⁽¹⁾ Includes funds on hand, current revenues available after provision for debt service and reserve requirements for bonds and toll highway maintenance and operating expenses and investment income. To the extent such funds are held in the 1998 Construction Fund, the holders of the Transportation Revenue Bonds have a claim on such funds in certain circumstances.

⁽²⁾ See the discussion of the Authority's Full Funding Grant Agreement with the United States Department of Transportation in "Tren Urbano" below.

⁽³⁾ Includes short-term financing, net proceeds of borrowing.

In the five-year period from fiscal 1999 through fiscal 2003 the Authority expended approximately \$4.0 billion on the Construction Improvement Program. The current five-year Construction Improvement Program projects an expenditure of approximately \$2.55 billion from fiscal 2004 through fiscal 2008, of which 7% represents the costs of Tren

Urbano. It also includes a \$211.2 million investment attributable to the cost of constructing the Eastern Corridor toll highway, which is subject to certain contingencies discussed below.

The Authority's internally generated funds available to finance its current Construction Improvement Program consist primarily of 1998 Resolution Revenues remaining after payment of debt service for the Highway Revenue Bonds and Transportation Revenue Bonds, provision for reserve requirements for the Highway Revenue Bonds and the Transportation Revenue Bonds, and payment of expenses for operating and maintaining the toll highways as well as Tren Urbano (as to the latter, beginning fiscal 2005 when it is expected to become operational). Such internally generated funds are estimated to aggregate approximately \$354 million during the five-year period from fiscal 2004 through fiscal 2008, including investment income, which is estimated at approximately \$127 million for the five-year period.

The current Construction Improvement Program contemplates new construction borrowings aggregating approximately \$1,213 million of principal to produce \$1,094 million of net proceeds from fiscal 2004 to fiscal 2008.

Tren Urbano. The largest single project included in the Authority's current Construction Improvement Program is Tren Urbano, a new-start mass transit project for the San Juan metropolitan region. The initial phase of Tren Urbano consists of approximately 17 km. of trackway, running from Bayamón to Santurce, via Río Piedras and Hato Rey, and sixteen stations. The project also includes the construction of a maintenance and storage facility and the purchase of 74 rail cars. The initial phase of the project is scheduled to be fully operational in fiscal 2005.

Tren Urbano is being constructed under seven separate design/build contracts. Siemens Transit Team is the contractor under the STTT Contract, the largest of these contracts, with a projected completion cost of approximately \$757 million. The STTT Contract includes: (i) the design and construction of two stations and a 2.6 km. test track; (ii) the design, procurement and installation of all systems for the project, such as the trackway, the train control system, and the communications system; (iii) the design and manufacturing of the vehicles; (iv) the design and construction of the maintenance and storage facility; (v) the responsibility for design and construction coordination among the several civil contracts; and (vi) operating Tren Urbano for a period of five years, with an additional five-year option exercisable by the Authority. The other six design/build contracts for the design and construction of all remaining stations and guideways, as well as other miscellaneous items, had a projected completion cost of \$889 million. Total aggregate costs for the first phase of Tren Urbano including contingency amounts, insurance and right-of-way and administrative costs, is estimated to be \$2.25 billion, of which \$2.071 billion had been incurred through January 31, 2004. As of that date, the construction of the first phase of Tren Urbano was 97% complete based on the percentage of actual monies earned by the contractors against the total contract cost. The monies earned are computed from quantities of work in place versus the total estimated quantities required.

The Authority's estimate of the total cost required to complete the Tren Urbano project includes a contingency for the aggregate amount the Authority estimates, based on its past experience, that may be required to pay to resolve various claims from contractors (mostly related to cost overruns or damages allegedly suffered because of delays in the design and construction of the project). No assurance can be given, however, that these claims will be resolved for the amounts estimated by the Authority or that the estimated cost of completing the Tren Urbano project will not increase as a result of resolving these claims or of the occurrence of other unforeseen contingencies.

To manage the Tren Urbano project, the Authority established the Tren Urbano Office. The Tren Urbano Office includes Authority staff, local and mainland design firms experienced in transit projects and local infrastructure projects, and financial and legal advisors. The Tren Urbano Office provides overall direction and management for the project. The office oversees all engineering and construction activities for the project, and is responsible for scheduling, budgeting, contract administration, risk management and quality assurance. Design review is provided by a consortium of design firms that includes DMJM+Harris, Inc. Construction oversight is provided by experienced Authority personnel and mainland consultants experienced in large transit projects.

Tren Urbano was designated as one of four national turnkey demonstration projects by the FTA. In March 1996, the Authority entered into a Full Funding Grant Agreement with the FTA for the project in the amount of \$307 million. Through February 29, 2004 approximately \$193.6 million had been disbursed under the agreement. The Authority expects to receive the remaining \$113.8 million payable under the agreement as part of the federal government's appropriations for fiscal 2005 and fiscal 2006. On August 4, 2000, the Authority borrowed \$300 million from the United States Department of Transportation to pay eligible project costs incurred and to be incurred in connection with Tren Urbano. This borrowing was repaid with a portion of the proceeds of the Transportation Revenue Bonds issued by the Authority in April, 2003. The balance of federal aid for the Tren Urbano project will come from moneys provided by the FTA and the FHWA under certain formula programs established by federal law. While the Authority cannot assure the amount or timing of federal funds for the project, if federal funds are received slower or in a lesser amount than currently

projected, the Authority will adjust the timing or scope of the remainder of its Construction Improvement Program, utilize lines of credit for interim funding or adjust its borrowing schedule, as necessary, to accommodate any such changes.

The size and complexity of the Tren Urbano project continue to present challenges related to the coordination among the several design/build contractors, as well as traditional construction risk factors. The Authority believes that it has made adequate provision for these factors in estimating the total cost required to complete the project. As with all of the projects contained in the Authority's Construction Improvement Program, the timetable and expenditure forecasts for Tren Urbano are subject to change. Unforeseen circumstances could result in delays or cost escalations not currently provided for in the Authority's projections.

Highway Construction. Highway construction projects included by the Authority in its current Construction Improvement Program are designed to address the transportation needs of the people of Puerto Rico and to enhance the economic development of Puerto Rico. The current Construction Improvement Program includes all the construction projects that the Authority believes are required at the present time to complete the Puerto Rico highway network. Projects include new highway construction, principally of primary roads and toll highways, and construction of improvements designed to alleviate the traffic congestion of the San Juan metropolitan area as well as to provide access to the proposed Port of the Americas, a superport on the southern region of Puerto Rico, which the Governor of Puerto Rico has announced the government intends to commence to construct during the next four years. It also includes reconstruction of existing highways, a bridge program and installation of safety features and other projects.

The Authority's current Construction Improvement Program includes the investment of approximately \$211 million of the total \$241.8 million cost of the construction of a toll highway from Carolina to Río Grande. As formerly conceived, this toll highway was known as PR-66. On April 19, 2000, the construction of PR-66 was permanently halted pursuant to an order of the Puerto Rico Supreme Court issued in an action filed by a group of citizens seeking review of the Puerto Rico Environmental Quality Board decision approving the final environmental impact statement prepared by the Authority for PR-66. As a result of the Court's order, the Authority was forced to terminate all construction contracts relating to PR-66. Prior to it being halted, the Authority had incurred approximately \$130 million in the construction of PR-66. An additional \$42 million in claims have been brought against the Authority by contractors related to the termination of construction contracts which contained liquidated damages clauses.

The Authority has reconceived the original PR-66 project, now re-named the Eastern Corridor, taking into account the environmental and other concerns raised by various citizen groups. On January 15, 2003, the Authority submitted a final environmental impact statement for the complete toll highway. On February 12, 2003, the Environmental Quality Board approved the new environmental impact statement. On February 20, 2003, the Environmental Quality Board published the required notice of such approval. No objections were filed with the Environmental Quality Board or the courts and, after the expiration of a 30-day notice period, the Authority submitted the project for bidding by construction contractors. The Eastern Corridor consists of a nine-mile four lane toll highway from Carolina to Canóvanas. A five-mile extension to Río Grande was added in the new environmental impact statement. The Eastern Corridor is expected to reduce vehicular congestion on highway PR-3 between the San Juan metropolitan area and the eastern region of Puerto Rico. Construction of the Eastern Corridor commenced in the Summer of 2003 and the Authority projects that Phase I of the Eastern Corridor (Carolina to Canóvanas) will be finalized during fiscal 2005.

Other major highway projects which have strategic importance for Puerto Rico's highway network include the construction of sections of PR-53 from Yabucoa to Maunabo and the design of the section that will complete the toll highway from Maunabo to Guayama (which includes the first highway tunnel through a mountain in Puerto Rico), the construction of the section of PR-10 from Utuado to Adjuntas (which will complete the connector between the north and south areas of the island), the conversion into an expressway of the section of PR-2 from Mayagüez to Ponce, which, together with PR-10, will service the proposed transshipment port to be known as "Port of Las Américas," the widening of sections of PR-22, the construction of the PR-5 toll highway connecting PR-2 to Las Cumbres Avenue, and the conversion of a portion of PR-2 in San Juan into an expressway.

The Authority receives aid for highway construction from the FHWA. Such aid is recorded as related costs which are billed to the FHWA, regardless of the year of appropriation. In fiscal years 2000, 2001, 2002 and 2003, such aid from FHWA amounted to \$69.3 million, \$50.0 million, \$34.7 million and \$55.5 million, respectively.

Federal aid for highway construction is received under a number of federal programs, including those directed to construction of new roads and repair and reconstruction of existing roads. The programs provide for matching federal assistance, ranging generally from 80% to 90% of the cost of a project. The level of federal highway aid is dependent upon Congressional authorizations that are apportioned or allocated to the states and the Commonwealth. The U.S. Department of Transportation has broad discretion to release funds for spending within the limits set by Congress. Upon

its approval of a state's program, funds are reserved but not committed. Federal-aid funds are committed when the U.S. Department of Transportation approves the detailed plans for specific projects. Congress has authorized funding for the federal highway programs through April 30, 2004. Federal highway legislation has liberalized certain types of federal highway aid and granted more flexibility to the states and the Commonwealth, in the use of such aid in highway or other transportation projects. No assurance can be given that the level of federal highway aid will be maintained at the levels projected in the above table. In the event of material reductions in such aid, the Construction Improvement Program will be appropriately adjusted in the absence of internally generated funds, external financing or other sources of funds shown in the above table available to offset any such reductions. See "INFORMATION CONCERNING THE FUNDING OF FEDERAL-AID HIGHWAYS."

The federal government conducts periodic audits of the federal aid it provides to the Authority to ascertain that funds are being expended consistently with the federal programs pursuant to which they are provided. Audit findings of a failure by the Authority to expend funds in compliance with federal programs could result in the withholding of federal aid for the project involved or could result in offset claims by the federal government for funds previously received by the Authority.

The traffic engineers retained by the Authority under the 1968 Resolution and the transportation engineers under the 1998 Resolution, if different, annually review the Construction Improvement Program and the Authority's estimates of revenue sources available for its implementation. In their most recent evaluation, the traffic engineers concluded that the Authority's current Construction Improvement Program is a reasonable response to the immediate and short-term transportation needs and is generally consistent with the Authority's long-term transportation master plan. The traffic engineers also concluded that revenue projections have been reasonably accurate and provide a sound basis for determining the size of future programs. The results of that review are summarized in the traffic engineers' letter included as Appendix V.

Teodoro Moscoso Bridge

In furtherance of its expanded powers to enter into concession agreements with private companies, the Authority entered into a concession agreement with Autopistas de Puerto Rico y Compañía, S.E. ("APR") for the design, construction, operation and maintenance of the Teodoro Moscoso Bridge, a bridge spanning the San Jose Lagoon from San Juan to Carolina. Pursuant to the concession agreement, APR is obligated to operate and maintain the bridge for a term of 35 years, subject to extension or to earlier termination. The bridge opened in February 1994 at a cost of approximately \$109.5 million. The bridge does not constitute a Traffic Facility under the 1968 Resolution or a Transportation Facility under the 1998 Resolution.

Construction of the bridge was financed through the issuance by the Authority of the Special Facility Revenue Bonds in the principal amount of \$116,752,769. The proceeds of such bonds were loaned to APR, and APR agreed to repay the loan in amounts sufficient to pay the principal of and interest on the bonds. APR's obligation in respect of the Special Facility Revenue Bonds was payable solely from the net toll revenues of the bridge, after payment of current operating expenses. In October 2003, the Authority refunded the Special Facility Revenue Bonds by issuing its Special Facility Revenue Refunding Bonds, 2003 Series A (the "Special Facility Revenue Refunding Bonds") in the principal amount of \$153,222,270.45. The proceeds derived from the sale of the Special Facility Revenue Refunding Bonds were loaned by the Authority to APR pursuant to a loan agreement, and such proceeds were used to refund the Special Facility Revenue Bonds. Pursuant to the terms of the Special Facility Revenue Refunding Bonds, APR will continue operating the Teodoro Moscoso toll bridge pursuant to the aforementioned concession agreement with the Authority and the bridge will continue being owned by the Authority. The Special Facility Revenue Refunding Bonds will be payable primarily from net toll revenues from the bridge collected by APR, after payment of bridge operating expenses.

Under the Special Facility Revenue Refunding Bonds, the Authority has covenanted that if net toll revenues, together with available reserves, are insufficient to pay the Special Facility Revenue Refunding Bonds, or if the concession agreement is terminated, the Authority will assume APR's obligation to pay the Special Facility Revenue Refunding Bonds. If the Authority assumes the obligation to pay the Special Facility Revenue Refunding Bonds, the Authority will be required to exchange the Special Facility Revenue Refunding Bonds for new bonds issued under the 1998 Resolution, provided it meets the requirements for the issuance of such new bonds. These new bonds would be issued as either Subordinated Transportation Revenue Bonds or Senior Transportation Revenue Bonds, at the option of the Authority, and would have the same interest rates, maturity dates and redemption provisions as the Special Facility Revenue Refunding Bonds. If the Authority cannot issue such new bonds in exchange for the Special Facility Revenue Refunding Bonds, the Special Facility Revenue Refunding Bonds would continue to be payable from revenues available to the Authority after payment of debt service on the Transportation Revenue Bonds.

DEBT

Debt of the Authority

The outstanding debt of the Authority as of January 1, 2004, as adjusted for the issuance of the 2004 Transportation Revenue Bonds and the refunding of the Refunded Bonds is as follows:

	Outstanding as of ⁽¹⁾ January 1, 2004	As Adjusted ⁽²⁾
Highway Revenue Bonds	\$ 1,850,105,000	\$1,850,105,000
Senior Transportation Revenue Bonds ⁽¹⁾	3,015,599,096	3,426,854,096
Subordinated Transportation Revenue Bonds	395,595,000	395,595,000
Outstanding Note	<u>\$ 28,113,774</u>	<u>0</u>
Total⁽³⁾	<u>\$ 5,289,412,870</u>	<u>\$5,672,554,096</u>

(1) Includes accretion on capital appreciation bonds through January 1, 2004.

(2) Adjusted to include the 2004 Transportation Revenue Bonds and to exclude the Refunded Bonds. Does not include the 2004 Grant Anticipation Bonds.

(3) Total does not include \$153,222,270.45 in Special Facility Revenue Refunding Bonds.

Principal and Interest Requirements of 2004 Transportation Revenue Bonds

The Principal and Interest Requirements for the outstanding Highway Revenue Bonds and Transportation Revenue Bonds and for the 2004 Transportation Revenue Bonds for each of the fiscal years 2004 through 2043 (after taking into account the refunding of the Refunded Bonds) are set forth in the following table:

Years Ending June 30,	Unrefunded Revenue Bonds ⁽¹⁾	2004 Transportation Revenue Bonds			Total Debt Service
		Principal	Interest ⁽²⁾	Total	
2004	\$299,066,690.00	\$	\$ 4,822,026.88	\$ 4,822,026.88	\$303,888,716.88
2005	346,496,555.00		24,449,713.76	24,449,713.76	370,946,268.76
2006	349,784,865.01	4,240,000.00	24,449,713.76	28,689,713.76	378,474,578.77
2007	354,420,877.51	4,415,000.00	24,272,588.76	28,687,588.76	383,108,466.27
2008	356,313,122.48	4,600,000.00	24,090,463.76	28,690,463.76	385,003,586.24
2009	356,239,266.22	4,770,000.00	23,921,145.00	28,691,145.00	384,930,411.22
2010	356,298,599.98	4,890,000.00	23,801,895.00	28,691,895.00	384,990,494.98
2011	354,972,787.51	5,125,000.00	23,565,375.00	28,690,375.00	383,663,162.51
2012	354,997,440.04	5,370,000.00	23,316,437.50	28,686,437.50	383,683,877.54
2013	354,959,902.56	5,635,000.00	23,054,437.50	28,689,437.50	383,649,340.06
2014	356,169,282.58	5,910,000.00	22,778,497.50	28,688,497.50	384,857,780.08
2015	356,170,435.10	6,200,000.00	22,488,372.50	28,688,372.50	384,858,807.60
2016	355,007,782.61	6,505,000.00	22,183,712.50	28,688,712.50	383,696,495.11
2017	354,955,707.59	6,825,000.00	21,863,577.50	28,688,577.50	383,644,285.09
2018	351,374,700.12	7,160,000.00	21,527,127.50	28,687,127.50	380,061,827.62
2019	344,690,510.15	7,515,000.00	21,173,627.50	28,688,627.50	373,379,137.65
2020	344,685,302.15	7,885,000.00	20,802,037.50	28,687,037.50	373,372,339.65
2021	322,328,319.27	8,275,000.00	20,411,837.50	28,686,837.50	351,015,156.77
2022	289,265,547.63	21,775,000.00	19,968,523.76	41,743,523.76	331,009,071.39
2023	242,030,974.25	22,900,000.00	18,841,203.76	41,741,203.76	283,772,178.01
2024	242,043,855.24	24,085,000.00	17,655,241.26	41,740,241.26	283,784,096.50
2025	242,012,788.48	25,315,000.00	16,422,706.26	41,737,706.26	283,750,494.74
2026	242,029,837.21	26,585,000.00	15,156,956.26	41,741,956.26	283,771,793.47
2027	259,492,317.70	10,500,000.00	13,827,706.26	24,327,706.26	283,820,023.96
2028	259,506,339.06	11,025,000.00	13,302,706.26	24,327,706.26	283,834,045.32
2029	250,710,982.55	11,580,000.00	12,751,456.26	24,331,456.26	275,042,438.81
2030	253,584,017.53	12,160,000.00	12,172,456.26	24,332,456.26	277,916,473.79
2031	253,585,295.03	12,765,000.00	11,564,456.26	24,329,456.26	277,914,751.29
2032	253,588,612.53	13,405,000.00	10,926,206.26	24,331,206.26	277,919,818.79
2033	253,575,506.27	14,075,000.00	10,255,956.26	24,330,956.26	277,906,462.53
2034	253,581,421.27	14,780,000.00	9,552,206.26	24,332,206.26	277,913,627.53
2035	253,589,531.27	15,515,000.00	8,813,206.26	24,328,206.26	277,917,737.53
2036	232,104,250.01	16,310,000.00	8,018,062.50	24,328,062.50	256,432,312.51
2037	176,736,550.01	17,145,000.00	7,182,175.00	24,327,175.00	201,063,725.01
2038	176,736,512.50	18,025,000.00	6,303,493.76	24,328,493.76	201,065,006.26
2039	111,909,675.00	18,950,000.00	5,379,712.50	24,329,712.50	136,239,387.50
2040	75,136,600.00	19,920,000.00	4,408,525.00	24,328,525.00	99,465,125.00
2041	75,137,612.50	20,940,000.00	3,387,625.00	24,327,625.00	99,465,237.50
2042	33,348,000.00	22,015,000.00	2,314,450.00	24,329,450.00	57,677,450.00
2043	-	23,145,000.00	1,186,181.26	24,331,181.26	24,331,181.26

* Totals may not add up due to rounding.

(1) Includes \$3,120,000 Highway Revenue Bonds sold to the Farmers Home Administration, which mature in the year 2020. Does not include the Special Facility Revenue Refunding Bonds. See "Teodoro Moscoso Bridge" under "TRANSPORTATION SYSTEM REVENUES AND EXPENDITURES." The interest on certain variable rate Highway Revenue Bonds (Series W), issued in August 1993 has been calculated on the basis of the fixed interest rate payable by the Authority under a related interest rate swap agreement as permitted by the 1968 Resolution. The interest on certain variable rate Senior Transportation Revenue Bonds (Series A) has been calculated on the basis of the fixed interest rate payable by the Authority under a related interest rate swap agreement as permitted by the 1998 Resolution. Adjusted to exclude debt service on the Refunded Bonds.

(2) The interest after July 1, 2010 on the Highway Revenue Bonds (Series AA) and the Senior Transportation Revenue Bonds (Series H) which are subject to tender for purchase has been calculated using a rate of 3.08% plus fees of 0.27%.

Upon the issuance of the 2004 Transportation Revenue Bonds, the remaining average life of the Highway Revenue Bonds, the Transportation Revenue Bonds and the 2004 Transportation Revenue Bonds will be approximately 20.4 years.

INFORMATION CONCERNING THE FUNDING OF FEDERAL-AID HIGHWAYS

The Federal-Aid Highway Program

The Federal-Aid Highway Program (“FAHP”) is an “umbrella” term that encompasses most of the federal programs providing highway funds to the states and the Commonwealth, such as the Interstate Maintenance Program, the Bridge Program, the National Highway System Program, and the Surface Transportation Program. The FHWA is the federal agency within the U.S. Department of Transportation responsible for administering the FAHP. The FAHP is financed from the transportation user-related revenues deposited in the federal Highway Trust Fund. The primary source of revenues in the federal Highway Trust Fund is derived from the federal excise taxes on motor fuels. Other taxes include excise taxes on tires, trucks and trailers, and truck use taxes.

Certain FAHP features or requirements are explained or further defined where they appear below but are introduced here for reference:

- *The federal Highway Trust Fund (the “HTF”)*: The HTF is a dedicated federal fund with dedicated revenues held in trust for reimbursement of expenditures by the states and the Commonwealth for costs of eligible transportation projects, including highway projects.
- *Authorization*: “Authorization” is the process by which Congress authorizes the expenditure of federal revenues on federal programs. For the FAHP, authorization historically has been provided on a multi-year basis. However, the current authorization is for several months and ends on April 30, 2004. See “STEPA 2004” below.
- *Apportionment and Allocation*: “Apportionment” is the distribution of authorized funding among the states for each Federal Fiscal Year (“FFY”) according to formulas that are established in authorizing statutes. “Allocation” is the distribution of authorized funding that does not have a statutory formula. The Commonwealth currently receives its authorized funding under the FAHP as an “allocation.”
- *Obligation Authority*: “Obligation” is the commitment of the federal government to pay, through reimbursements to a state or the Commonwealth, its share of the eligible expenditures on an approved project. The amount of such federal revenues that a state or the Commonwealth can obligate in a given FFY is called its “Obligation Authority.”
- *Advance Construction*: The Advance Construction procedure allows states and the Commonwealth to commence eligible projects without first having to obligate the federal government’s share of expenditures. Thus, states and the Commonwealth may begin a project before amassing all of the Obligation Authority needed to cover the federal government’s share. Each of the 2004 Construction Projects will be Advance Construction projects.
- *Partial conversion of Advance Construction*: Under partial conversion of Advance Construction, in a given year a state or the Commonwealth may convert Advance Construction to Obligation Authority and thus be eligible for reimbursement for a portion of the federal share of an Advance Construction project in that or in a subsequent FFY. This removes any requirement for a state or the Commonwealth to wait for reimbursements until the full amount of Obligation Authority needed for the entire project is available.

These features of the FAHP work in a complementary fashion to provide a regular flow of federal reimbursements over the years to state and Commonwealth highway projects. The participation of the Commonwealth in such reimbursements, and the role of such participation in providing payment and security for the 2004 Grant Anticipation Bonds, is discussed in “FEDERAL AID REVENUES.”

It should be noted that the terms and conditions of participation in the FAHP as described herein are subject to change at the discretion of Congress, and there can be no assurance that the laws and regulations now governing the FAHP will not be changed in the future in a manner that may adversely affect the ability of the Commonwealth to receive adequate Federal Transportation Funds to pay the Bond Payments on the 2004 Grant Anticipation Bonds.

Although the FHWA provides funding for eligible highway projects, federal-aid highways are under the administrative control of the state, Commonwealth or local government responsible for their operation and maintenance.

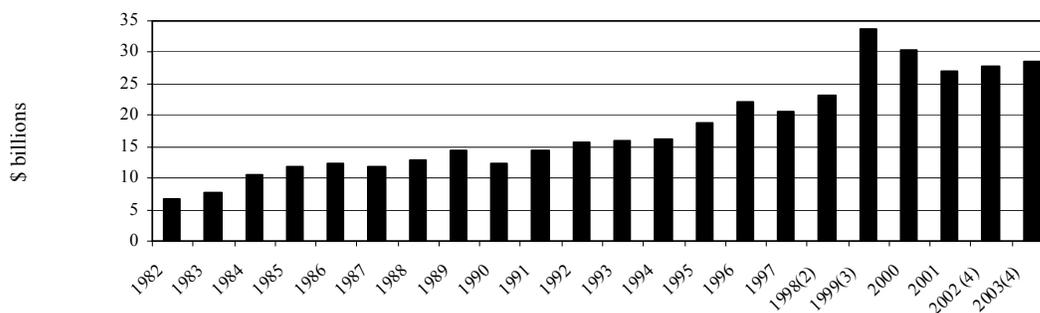
Title 23, United States Code, entitled “Highways,” includes most of the laws that govern the FAHP arranged systematically or codified. Generally, Title 23 embodies those substantive provisions of highway law that Congress considers to be continuing and which need not be reenacted each time the FAHP is reauthorized. Periodically, sections of Title 23 may be amended or repealed through surface transportation acts.

Federal Highway Trust Fund

The FHWA administers payments to states and the Commonwealth under the FAHP through the HTF. Funded by collection of federally-imposed motor vehicle user fees, primarily fuel taxes, the HTF is a dedicated fund with dedicated revenues that are held in trust for reimbursement of the states’ and Commonwealth’s cost of transportation projects, including highway projects. The HTF presently contains the Highway Account and a Mass Transit Account. The Highway Account receives approximately 84% of gasoline tax revenues and 88% of diesel fuel tax revenues, with the remaining share of such revenues deposited in the Mass Transit Account. Using revenues in the Highway Account of the HTF, the FHWA reimburses states and the Commonwealth for expenditures related to approved highway projects. The FHWA distributes these revenues to states and the Commonwealth, based on apportionment and allocation rules prescribed by federal law. Current law requires that the cash balance of the Highway Account, plus projected revenues for the next two years, must suffice to repay all unpaid authorizations before any additional apportionments of revenues can be made from the HTF.

Federal gasoline excise taxes are the largest revenue source for the HTF. The majority of these tax revenues, including 15.4 cents per gallon out of the current 18.4 cents per gallon tax, go to the Highway Account. The following table shows annual and projected HTF collections in the Highway Account for the period FFY 1982 to FFY 2003.

**Payments into the Highway Account of the Highway Trust Fund ⁽¹⁾
Federal Fiscal Years 1982-2003 (in billions)**



SOURCE: FFY 1982-2001, FHWA, Highway Statistics (2001) Table FE-210; FFY 2002-2003, U.S. Treasury Notice PO-3085 (May 9, 2002).

- (1) Exclusive of Interest Earnings
- (2) Reflects the redirection of 03.44 cents of the Gas Tax from deficit reduction to the Highway Account.
- (3) FHWA estimates that \$5.0 billion in FFY 1998 receipts were not received until FFY 1999 due to the Tax Payer Relief Act of 1997. Accordingly, adjusted FFY 1998 receipts would be \$28.1 billion and adjusted FFY 1999 receipts would be \$28.7 billion.
- (4) Estimated.

The HTF Balance. Since 1956, the Highway Account of the HTF has accumulated a surplus of revenues because more revenues have been generated for the account through collections and interest income than have been distributed to states under the FAHP. TEA 21 established an opening balance of \$8.0 billion for the Highway Account effective October 1, 1998. The HTF is required under current federal law to maintain a positive balance to ensure that prior commitments for federal revenues can be met. This requirement allows states, including the Commonwealth, the flexibility to earn and receive reimbursement revenues for up to four years after federal funds first were obligated.

Reauthorization of HTF Collections. Collection of HTF taxes (“HTF collections”), like the FAHP itself, must periodically be reauthorized by Congress. Historically, the HTF and its constituent taxes have been authorized to operate for limited periods of time. Originally, the HTF was authorized through June 1972; it has been reauthorized several times. Most recently, TEA 21 authorized HTF collections through FFY 2005, and the transfer of the taxes to the HTF through June 30, 2006.

History

The modern FAHP originated in the Federal-Aid Highway Act of 1956. The FAHP initially was established as a pay-as-you-go system, meaning that costs of constructing and maintaining the system were to be borne primarily by its users, who would pay a federally-imposed tax on motor fuels. Federal user fees were to provide 90% of the cost of construction, with the remainder paid for by the states.

The Federal-Aid Highway Act of 1956 was the first of a long series of authorizing statutes for the FAHP. TEA 21, which expired on September 30, 2003, and its immediate predecessor, the Intermodal Surface Transportation Efficiency Act of 1991 (“ISTEA”), are the most recent multi-year authorizing statutes. The current authorizing statute, the Surface Transportation Extension Act of 2004 (“STEA 2004”), expires on April 30, 2004 and is seen as an interim reauthorization.

The 1982 Surface Transportation Assistance Act (“STAA”) made notable changes to the FAHP, and began the modern multi-year (*i.e.*, four or more years) authorizing process. STAA also guaranteed each state a minimum 85% return on the money paid in by highway users of the state.

In 1991, ISTEA broadened the focus of the FAHP, changed its structure significantly and created several new funding categories. ISTEA also gave state and local governments far greater flexibility in determining their transportation infrastructure priorities, whether transit or highways, and for the first time allowed significant flexibility to redirect federal revenues among programs. ISTEA also authorized innovative approaches to federal-aid highway funding, including the use of private sector funding sources for transportation improvements. Innovative financing procedures were authorized and encouraged, and states were authorized to augment federal revenues with alternate sources of revenues.

The National Highway System Designation Act of 1995 (the “NHS Act”) designated the National Highway System to include the Interstate System as well as other roads important to the nation’s economy, defense, and mobility. The NHS Act made several changes affecting the financing of federal-aid highway projects, including Advance Construction procedures:

- Standard federal highway financing practices require states and the Commonwealth to have sufficient Obligation Authority before they begin a highway project. If a state or the Commonwealth has many projects or a particularly large project, they may be unable to provide enough Obligation Authority to get federal approval to begin specific projects. To avoid delays in projects that are eligible for federal funding, the FHWA may approve Advance Construction for a project if the state or the Commonwealth can provide 100% of the costs up-front.
- Under Advance Construction procedures prior to the NHS Act, only when a state or the Commonwealth had amassed sufficient Obligation Authority to cover the federal share of a project’s total costs could it convert the project from Advance Construction to Obligation Authority and be reimbursed for the federal share. The NHS Act removed the requirement that states and the Commonwealth must amass Obligation Authority equal to the full federal share before reimbursement could occur. Partial conversion now allows a state or the Commonwealth to be reimbursed for a portion of the federal share of the project’s total costs as Obligation Authority becomes available each year and costs are expended.

In addition, the FHWA has issued guidelines for debt-financed federal-aid highway projects. Key provisions of these guidelines are:

- Debt-financed projects are subject to requirements of Federal Clean Air Act and federal air quality conformity requirements, discussed below under “Regional Planning and Air Conformity.”
- A state or the Commonwealth may make arrangements with the FHWA Division Office regarding the procedures under which it would submit a billing to FHWA for debt-related costs. A request for debt service payment can be timed so that reimbursements could be received shortly before the debt service payment date.
- A state or the Commonwealth may designate a trustee or other depository to receive federal-aid debt service payments directly from FHWA.

TEA 21. TEA 21, which became law on June 9, 1998 and was amended on July 22, 1998, extended the authorization of the FAHP through FFY 2003. TEA 21 expired on September 30, 2003. According to the FHWA, under TEA 21 average annual authorizations for highway aid to the states and the Commonwealth, for FFY 1998 through FFY

2003 are approximately \$28.5 billion, as indicated in the table below (which shows figures by FFY and in billions of dollars):

1998	1999	2000	2001	2002	2003	Average
\$23.8	\$28.2	\$28.7	\$29.5	\$30.0	\$30.6	\$28.5

Source: Financing Federal-Aid Highways, Publication No. FHWA-PL-99-015, August 1999 (available on FHWA website).

TEA 21 increased equity protections for apportionment programs by assuring each state, at least 90.5% of its proportional share of apportioned programs, based on its percentage contribution to HTF receipts which were reauthorized through FFY 2005. Such equity protections currently do not apply to the Commonwealth as a recipient under an allocation program. TEA 21 also included a provision known as Revenue Aligned Budget Authority (“RABA”) which requires that HTF revenues be spent on transportation-related improvements, rather than allowed to accumulate into large surpluses. To this end, TEA 21 set yearly minimum guaranteed funding levels for the authorization period, which are based on annual HTF revenues. TEA 21 also provided that interest will no longer accrue on funds in the Highway Account and that as of October 1, 1998 (the start of FFY 1999), the opening balance of the Highway Account would be set at \$8.0 billion. According to the FHWA Office of Fiscal Services, this amendment reduced the HTF balance by approximately \$7 billion, but will not affect the solvency of the HTF because actual annual funding levels will be based on the previous year’s HTF revenues. TEA 21 allocated to the Commonwealth authorized funding in the amount of \$110 million per FFY for the period commencing with 1999 FFY and ending with the 2003 FFY. Under ISTEA, the Commonwealth had received its authorized funding through a statutory apportionment formula.

STE A 2003. The Surface Transportation Extension Act of 2003 (“STE A 2003”) extended the authorization of the FAHP for a five-month period ending February 29, 2004 at a level of \$14.1 billion for highways. On an annualized basis, should the FAHP be reauthorized through September 30, 2004, this would result in total funding for FFY 2004 at a level of approximately \$33.8 billion. Under STE A 2003, the Commonwealth received an allocation of \$45.8 million for such five month period which was equivalent to the \$110 million per FFY authorized by TEA 21. Congress recently enacted an appropriations act which provides highway funding for FFY 2004 at the FFY 2003 level.

STE A 2004. The Surface Transportation Extension Act of 2004 (“STE A 2004”) further extended the authorization of the FAHP for a two-month period ending April 30, 2004 at the same level authorized by STE A 2003. Under STE A 2004, the Commonwealth has received a total allocation of \$64.2 million for FFY 2004. To date, the FHWA has distributed \$28.5 million of Obligation Authority to the Commonwealth for FFY 2004. There is no guarantee, however, that the FAHP will be reauthorized for the remainder of the current FFY at the same level set forth in STE A 2004.

Operations

The present FAHP continues to reimburse a significant portion of state and Commonwealth expenditures for approved highway projects. The financial assurance provided by the FAHP is unusual among federal programs in that:

- The FAHP is based on dedicated revenues, from a user-tax source, deposited in a dedicated trust fund (the HTF);
- The budget and contract authority of the FHWA is typically established by a multi-year authorization act rather than annually through appropriation acts; and
- Contract authority is not at risk during the annual appropriations process (as budget authority is in most other federal programs).

The process for reimbursing state and Commonwealth expenditures may be summarized in three steps: authorization, obligation and program implementation. The authorization step is the most critical step in establishing overall spending authority for federal highway funding. Authorizing legislation extends the life of the FAHP and the collections that fund the HTF, sets FAHP objectives and provides formulas for determining the distribution or apportionment of available resources among the states and the Commonwealth. The existence of the dedicated revenues in the Highway Account and the existence of multi-year (or under STE A 2004, multi-month) contract authorizations are designed to help to make available a predictable and uninterrupted flow of reimbursements to states and the Commonwealth.

The second step, obligation, is the process through which states and the Commonwealth make use of, or “obligate,” the contract authority that has been apportioned or allocated to them in the authorization process (Step 1). Congress typically limits the amount of Obligation Authority that states and the Commonwealth may use annually.

The third step, program implementation, leads to actual receipt of federal funds by states and the Commonwealth. FAHP implementation methods vary state-by-state. States and the Commonwealth are permitted to make use of Advance Construction and partial conversion of Advance Construction in order to obligate varying amounts of federal funds to an eligible project from FFY to FFY, depending on how much of the state’s or the Commonwealth’s Obligation Authority is available from the FAHP and is desired for such use by the state or the Commonwealth.

Step 1: Authorization

The first step, and the most crucial in financing the FAHP, is the multi-year (or under STEA 2004, multi-month), authorizing legislation. Such highway authorization acts:

- Establish the taxes that fund the HTF and extend their life (reauthorization);
- Establish the specific programs and procedures through which states and the Commonwealth receive federal financial assistance for their highway programs; and
- Set upper limits on funding for specific programs and for the overall FAHP.

Multi-year Authorization Acts. As noted earlier, the FAHP since 1982 has been periodically reauthorized on a multi-year basis by authorization acts, through which Congress influences the level of federal involvement in state or Commonwealth highway program activities. There is no guarantee, however, that reauthorization of the FAHP will occur on a multi-year basis. In fact, STEA 2003, was for a five-month period that ended on February 29, 2004 and the current reauthorization, STEA 2004, ends on April 30, 2004. Annual appropriations acts then establish any limits on the amount of federal funds that the FHWA may obligate to states and the Commonwealth in a given year.

Appropriated Budget Authority and Contract Authority. Most federal programs require appropriated budget authority before revenues may be committed and spent. Normally this authority is provided through a two-step process, with authorizing legislation describing the purposes for a specific program and setting a proposed level of spending, and appropriations acts providing the budget authority or legal ability to spend federal revenues. Appropriations are often for a lower amount than that set by authorizations. The FAHP combines these two steps, with authorizing legislation providing the U.S. Secretary of Transportation with contract authority or the legal ability to enter into binding contracts with state transportation departments (“DOTs”) or the Authority, in the Commonwealth’s case, and other bodies specified in the FAHP without further legislative action.

Contract authority provides state DOTs and the Authority with assurance about the level of future federal revenues that will be available. This, in turn, makes it easier and more cost-effective to plan and execute multi-year construction projects. As a result of contract authority and the collection of user taxes into the dedicated HTF, the formal appropriation by Congress of revenues on an annual basis generally has been non-controversial. Constraints arising from the annual appropriation process are described in Step 2 below.

Annual Distributions. For most components of the FAHP, the authorization acts set the distribution of spending authority among states and the Commonwealth. The primary methods used to distribute authorized federal highway revenues are “apportionment” and “allocation”:

- Apportionments. The contract authority created by authorization acts such as TEA 21 is distributed annually among the 50 states and the District of Columbia using a process called apportionment of revenues. Apportionments indicate the maximum amount of contract authority that each state can expend for eligible projects in specific programs. For each FFY, the FHWA has responsibility for apportioning authorized funding for the various programs among the states according to formulas established in the authorizing statute. Annual apportionments are generally made on the first day of the FFY, which is October 1.
- Allocations. While most highway revenues are distributed to states through apportionments, some funding categories do not contain legislatively-mandated apportionment formulas. Such is the case of the contract authority received by the Commonwealth under TEA 21 and STEA 2004. Distribution of revenues where there are no statutory formulas is called “allocation” or “discretionary allocation.” In most cases, allocated federal funding is divided among states using criteria determined administratively by the federal Department of

Transportation or as provided in a statute, often through competitive grant procedures. In the case of the Commonwealth, TEA 21 and STEA 2004 specifically provided the amounts allocated to the Commonwealth.

Lapsing of Authorization. Though recent multi-year federal surface transportation legislation has authorized the Federal-Aid Highway Act for four to six years at a time, there occasionally have been periods in which the previous authorizing legislation had expired and the subsequent multi-year legislation had yet to be enacted. In most of such instances, however, Congress has enacted short-term authorization legislation.

ISTEA expired on September 30, 1997 and until approval of TEA 21 on June 9, 1998, no new long-term authorization legislation was enacted. Despite the lack of long-term authorizing legislation, states and the Commonwealth were provided an upper limit on Obligation Authority through passage of an appropriations act plus access to their unobligated balances. On November 13, 1997 Congress passed the Surface Transportation Extension Act of 1997 (“STEA”), which provided a six-month authorization for highway funding and established a limit on the amount of new Obligation Authority that states and the Commonwealth could use at funding levels equal to about a quarter of FFY 1997 authorization levels. Similarly, TEA 21 expired on September 30, 2003 and no new long-term authorization has yet to be enacted. As a recipient of an allocation under TEA 21, the Commonwealth does not have unobligated balances to be accessed. However, STEA 2003 and STEA 2004 have reauthorized the FAHP a total of seven months, to April 30, 2004, and several continuing resolutions provided additional funding for the FAHP for interim periods until an appropriations act for FFY 2004 was enacted. A continuing resolution is a joint resolution enacted by Congress and signed by the President, when the new Federal Fiscal Year is about to begin or has begun, to provide budget authority for federal agencies and programs to continue in operation until appropriation acts are enacted. Funds provided for the FHAP through continuing resolutions, however, tend to be used first to provide states with federal aid revenues under apportionment programs.

Matching Requirements. With a few exceptions, the federal government does not pay for the entire cost of construction or improvement of federal-aid highways. Federal reimbursements are typically matched with state and/or local government revenues, and in the case of the Commonwealth, Authority revenues, to account for the necessary dollars to complete the project. The maximum federal share is specified in the legislation authorizing the program. Most projects have an 80% federal share while Interstate Construction and Maintenance projects typically have been funded with a 90% federal share.

Step 2: Obligation

The second step of the federal-aid funding process occurs when revenues that have been authorized by legislation, and either apportioned or allocated to individual states and the Commonwealth, are obligated for a specific purpose. As noted in the previous section, Congress uses annual appropriations acts to control actual annual obligation of funds in the HTF. Appropriations acts limit the amount of federal money that actually will be obligated and thus ultimately spent, and these annual amounts may be less than the authorized amount. This ceiling on the amount of contract authority that states and the Commonwealth may use is called the “annual obligation limit.”

Obligation is the commitment of the federal government to pay, through reimbursement to a state or the Commonwealth, the federal government’s share of an approved project’s eligible costs. This process is important to states and the Commonwealth because it allows them to award contracts with assurance that the federal government will reimburse its share of incurred costs. From the federal perspective, obligations made are the outlays the federal government has committed to make from the HTF in the future. Because of the close relationship between obligations and outlays, Congress and the FHWA play a strong role in determining how much federal funding can be obligated by individual states or the Commonwealth through two primary processes:

- Appropriations acts; and
- Distribution of Obligation Authority.

Appropriations Acts. Congressional appropriations committees use the amount of federal-aid highway revenues that states or the Commonwealth can obligate in a given year, called “Obligation Authority,” as a means of balancing the annual level of highway spending with other federal budgetary priorities. This is accomplished through the establishment of an annual obligation limitation in the annual Department of Transportation and Related Agency Appropriations Act. The annual obligation limitation can be less than the level of funding authorized for the same year, although the creation of budgetary firewalls and RABA in TEA 21 substantially limited the amount of HTF revenues that can be used for non-highway purposes.

Distribution of Obligation Authority. The obligation limitation is the amount of authorized funding that Congress allows states, including the Commonwealth, collectively to obligate in an individual year. Under TEA 21, the annual obligation limitation included two elements – a large portion protected by firewalls and tied to projected HTF receipts through RABA (roughly 90% of total annual contract authority), and a smaller portion that competes with other discretionary budget priorities for funding (less than 10% of total annual contract authority). Beginning in FY 2000, the level of Obligation Authority protected by firewalls is established each year as the guaranteed obligation limitation in TEA 21, adjusted by the difference between HTF revenue estimates made for TEA 21 and new Department of Treasury projections. Additional, discretionary Obligation Authority is determined when annual appropriations bills are developed and is counted under Congress’ annual spending cap, which is the amount of federal dollars that can be spent on all domestic, non-entitlement programs in a given year. The combined total may still be below the authorized annual level, and serves as a limit on the total obligations in that particular year.

Once each state’s or the Commonwealth’s Obligation Authority is determined, the states and the Commonwealth then submit requests to the FHWA to obligate revenues representing the federal share of specific projects throughout the years. (A further description of this process is included in Step 3.) As a state or the Commonwealth obligates revenues, its balance of Obligation Authority is commensurately reduced.

A state’s or the Commonwealth’s Obligation Authority (unlike the apportionments and allocations of authorized funding) must be used before the end of the FFY for which it is made available; if not, it will be distributed to other states. The FHWA closely monitors each state’s plans for use of Obligation Authority. In mid-summer, the FHWA collects any Obligation Authority from states, including the Commonwealth, that do not plan to obligate all of their available Obligation Authority before the end of the FFY, and redistributes it to other states that can obligate the revenues. This reallocation of Obligation Authority is known as the August redistribution.

Step 3: Program Implementation

The third and final step in the overall federal-aid highway funding process—program implementation—occurs after authorized revenues have been distributed to states and the Commonwealth, and after states and the Commonwealth have had the opportunity to obligate those revenues. Once federal-aid highway revenues have been authorized and obligated, states and the Commonwealth must have developed highway programs that describe, at a project-by-project level, exactly how federal reimbursements will be earned. The process of developing and implementing state and Commonwealth highway programs has three broad stages:

- Budgeting;
- Planning and programming; and
- Fiscal management and reimbursement.

Each stage helps to ensure that the states and the Commonwealth develop programs which match funding availability, and that the FHWA is able to distribute federal reimbursements to the states and the Commonwealth in a timely manner. The following paragraphs describe those stages especially in the case of the Commonwealth.

Budgeting. Budgetary information about availability of funding is crucial to the development of Commonwealth highway programs. Projected Commonwealth and federal funding levels are used to budget transportation needs. Consequently, Authority transportation budget officials track the availability of funding and develop forecasts of future Commonwealth and federal revenues. The Authority must estimate the availability of short and long-term Commonwealth and federal funding in order to plan their highway programs. They use this information as a guide during long-range planning, and as a strict constraint on short-term programming. In the Commonwealth, the Office of the Deputy Executive Director for Administration and Finance at the Authority has primary responsibility for budgeting.

Planning and Programming. The budget process—particularly the identification of available funding—provides the context for transportation planning and programming. The long-range planning process provides a perspective of anticipated project needs regionally across the Commonwealth. The STIP follows from the long-range plans and provides a detailed listing of projects that are proposed for implementation in a time-frame of two years. The Department’s Assistant Secretary for Planning, with the support of the Federal Coordination, Strategic Planning and Programming Offices of the Authority, coordinates transportation planning and programming activities for the Department, the designated Metropolitan Planning Organization for the Commonwealth. The Authority actively participates in the planning activities and services as the implementing agency for highway program projects. At the federal level, the

development of state or Commonwealth highway transportation plans is overseen by the FHWA and the FTA and reviewed for conformity with the federal Clean Air Act.

As a condition for receiving federal reimbursements for transportation programs, the Commonwealth must develop comprehensive transportation plans that are based on anticipated long-term Commonwealth and federal funding levels for FAHP categories. The Commonwealth and its urban areas must satisfy these federal requirements in order to remain eligible for federal reimbursements, and specific projects are not eligible unless they are either directly identified in a long-range plan or consistent with policies and objectives identified in long-range plans. Current federal law requires the Commonwealth to develop long-range transportation plans (“LRPs”) that identify long-range Commonwealth policies, objectives and goals, while using realistic projections of available future Commonwealth and federal funding.

In August 2000, the Department completed a long-range plan titled the “Puerto Rico Islandwide Transportation Plan” that generated recommendations to the year 2015, and in August 2001 prepared interim long-range transportation plans for all the Commonwealth’s urbanized and metropolitan areas. The plan’s goals reflect the need for a transportation system that is responsive to local needs, promotes economic development and is environmentally sensitive.

Notwithstanding the above, the Department and the Authority are currently working, with specialized consultants on a Puerto Rico Long Range Multimodal Transportation Plan that will define highway and transit strategies and propose a financially-constrained investment program, based on a year 2030 horizon and vision statement. This long range plan is expected to recommend new strategies to reduce traffic congestion while increasing accessibility, mainly by changing emphasis, from additional highway building, to basic network completion, maintenance and improvement of existing facilities to increase their efficiency and durability, and the reduction of automobile dependency through development of a variety of transit options for mobility throughout the Commonwealth. Transportation System Management (TSM), Transportation Demand Management (TDM), Intelligent Transportation Systems (ITS) and Congestion Management Systems (CMS) type of options will be advanced in the new plan, which is expected to be approved by the Governor in late 2004. Moreover, since the Long Range Plan is required to be financially constrained, if the actions recommended exceed the projected financial resources of the Authority (based on presently available resources), that document will also have to recommend new sources of revenue that could reasonably be expected to provide the needed additional resources.

Current federal law also requires that short-term planning and programming must be conducted at least every two years through the development of a Transportation Improvement Program (“TIP”) for each metropolitan area. Among other requirements, each TIP must include, for each project, the estimated project cost and amount of federal revenues proposed to be obligated during each year.

Federal regulations require that a TIP be prepared for each metropolitan area within a state and also at the statewide level incorporating the metropolitan area TIPs. In the Commonwealth, the Metropolitan Planning Organization is the Department. The Department adopts a TIP for the San Juan metropolitan area and one for the entire Commonwealth, the STIP, which satisfies all requirements for metropolitan and statewide planning under federal law.

Fiscal Management and Federal Highway Reimbursements. Once budgeting, planning and programming are complete, projects move into a fiscal management phase. This fiscal management process is the third element of the implementation step in the overall federal highway funding process. An Authority-led fiscal management system—conducted in accordance with FHWA requirements—is used to determine exactly how much federal funding will be received for each project, to obtain final FHWA authorization before projects are implemented, and to ensure timely federal reimbursement of Authority expenditures on contractor costs. These activities are performed by the Authority’s Programming Office. Also, specified units within the Finance, Accounting and Internal Audit Offices of the Authority intervene during the cost and reimbursement process to insure that both federal and Commonwealth taxes and regulations are strictly followed. In addition, audits of the use of federal funds are periodically conducted by external auditors and submitted to the federal government for review.

The Authority must follow federal fiscal management procedures as it implements projects that have passed through the approval and programming processes. These fiscal management procedures ensure that the FHWA and the Authority are able to manage the process efficiently, from project authorization to actual payment of Federal Highway Reimbursements to the Authority.

In the traditional approach, the Authority simply obligates the full federal share of available funding at the beginning of the project, concurrent with project authorization. The first step in the fiscal management process begins when the Authority requests authorization to use federal funding on a project. The project sponsor (e.g., the Authority) submits plans, specifications and estimates (“PS&Es”) for a project to the FHWA division office, and requests that the

FHWA approve the use of federal funding for the appropriate federal share of the project. The project must be in the STIP and the PS&Es must identify the category of federal funding that will be used.

The FHWA evaluates the PS&Es to ensure that the project is eligible for federal funding and meets a variety of federal requirements (e.g., design standards). Provided that all requirements are satisfied, the FHWA authorizes federal participation in the project, and obligates the federal share of project costs. By obligating the revenues, the FHWA makes a commitment to reimburse the Authority for the federal share of eligible project costs. It sets aside the appropriate amount of the Commonwealth's Obligation Authority, and also sets aside an equivalent amount of apportioned revenues by program (or programs). Accordingly, the Commonwealth must have sufficient Obligation Authority to cover the level of federal participation that the Authority is requesting.

Once authorization for a project has been obtained, the Authority advertises the project and receives bids. Based on actual costs identified in bids, the Authority awards the contract to the lowest qualified bidder and submits a request to the FHWA asking for any necessary adjustments to federal obligations for the project. If approved, the amounts agreed to are included in a project agreement which identifies the revenues that will be encumbered by the Authority (formally applied against the Authority's resources), and the amount that will be reimbursed by the federal government.

Construction begins, and contractors submit bills to the Authority as work is completed. The Authority pays its contractor's bills with cash from the Authority's funds; the Authority bills the FHWA electronically for the federal share of completed work for which payment has been made; and the FHWA makes payment to the Authority via electronic transfer. This FHWA reimbursement to the Authority liquidates its obligation for the federal share of the costs incurred to that point. As project work continues and state expenditures are reported to the FHWA, federal reimbursements are made, generally on a weekly basis. Reimbursement requests are submitted weekly and reimbursements are made by wire transfer generally within one or two days. Much of the Authority's system and management in general, are highly automated, leading to a routine flow of Federal Highway Reimbursements based on actual spending on approved projects.

Innovative variations on this fiscal management approach include Advance Construction and partial conversion of Advance Construction. These variations complement one another to provide the Authority with additional flexibility in managing its Obligation Authority and cash.

The *Advance Construction* approach for authorizing projects allows the Authority to finance projects that are eligible for federal aid without obligating the federal share of costs at the outset of the project. This allows the Authority to begin a project before amassing all of the Obligation Authority needed to cover the federal share of that project. As with the traditional approach, the Authority submits PS&Es to the FHWA and requests project authorization. Under Advance Construction, however, the FHWA is asked to authorize the project without obligating federal revenues. As a result, the Authority will cover the entire cost of the project and later may request the obligation of revenues, when sufficient Obligation Authority is available and is desired by the Authority. Further, the Authority may then take credit for the Authority's expenditures made from project approval to that date, as a basis for earning reimbursements.

Once the FHWA authorizes a project for federal assistance, the Authority follows the same procedure to advertise a project, to award the contract, and to reconcile the level of Authority and federal funding required. The Authority may request that the FHWA convert its Advance Construction amount to an obligation at any time, provided the Commonwealth has sufficient Obligation Authority. This conversion of Advance Construction to Obligation Authority must occur in order for the Authority to be reimbursed for the federal share of the project. The Authority can convert Advance Construction to Obligation Authority long after its expenditures are made.

Under *partial conversion of Advance Construction*, moreover, the Authority follows the steps to apply for Advance Construction but converts, obligates, and receives reimbursement for only a portion of its funding of an Advance Construction project in a given year. This removes any requirement to wait until the full amount of Obligation Authority is available. The Authority can thus obligate varying amounts for the project's eligible cost in each year, depending on how much of the Commonwealth's Obligation Authority is available and desired by the Authority.

The Authority is required to use a detailed accounting system to track project expenditures and reimbursements. In addition, a federal system tracks payments to the Authority. A computer-based project accounting, reporting and billing system is used to track encumbrances and expenditures for all projects, including highway projects, administered by the Authority.

The Federal Aid Agreements

The Authority has entered and will enter into Federal Aid Agreements with the FHWA relating to the design and construction of the 2004 Construction Projects. Under the Federal Aid Agreements, the FHWA has agreed and will agree

to pay Federal Transportation Funds to the Trustee for Bond Payments. Under the Grant Anticipation Resolution, the Authority has covenanted to take all action necessary to ensure that Federal Aid Agreements are maintained in full in full force and effect pursuant to which FHWA has agreed to make payments of Federal Transportation Funds in an amount at least equal to the Bond Payments due on each Bond Payment Date. The Federal Aid Agreements do not constitute a commitment, guarantee or obligation on the part of the United States to provide for the payment of Bond Payments.

STIP and Long Range Plan Conformity with Federal Clean Air Requirements

A section of the municipality of Guaynabo, within the San Juan metropolitan area, has been designated as a PM-10 non-attainment area. The readings of particular matter that produced this designation have been contested as being non-transportation related. Nonetheless, the EPA’s air quality conformity regulations require that in such non-attainment areas the STIP and long range plans be evaluated for emissions impacts. The Commonwealth STIP and long range plans are analyzed to evaluate change in ozone precursors (volatile organic compounds – VOC and oxides of nitrogen – Nox) and carbon monoxide – CO emissions due to implementation. The air quality analysis has demonstrated that implementation of the Commonwealth’s long range transportation plan and STIP is consistent with federal air quality conformity criteria and regulations, and conforms to the air quality goals in the Commonwealth’s air quality implementation plan.

FEDERAL AID REVENUES

Below are tables identifying prior and projected Apportionments, Allocations, Obligation Authority and Receipts of Federal Transportation Funds by the Authority from Federal Fiscal Year 1992 through the Federal Aid authorization ending September 30, 2003. The tables reflect the fact that the Commonwealth’s federal aid revenues were received as “apportionments” under ISTEA and “allocations” under TEA 21. The ability to pay Bond Payments on the 2004 Grant Anticipation Bonds will depend upon the amount of funding provided to the Commonwealth under the FAHP and the Commonwealth’s ability to use such funding. The Authority has been informed by FHWA that its Obligation Authority for the period October 1, 2003 through January 31, 2004 shall be \$28,457,110.

**APPORTIONMENTS, OBLIGATION AUTHORITY AND RECEIPTS
FOR THE PUERTO RICO HIGHWAYS AND TRANSPORTATION AUTHORITY
Under Prior Federal Aid Authorization Period
(Intermodal Surface Transportation Efficiency Act of 1991)
Federal Fiscal Years 1992 Through 1997
(millions of dollars)**

Federal Fiscal Year	Apportionments	Obligation Authority	Actual Receipts
1991-92	\$73.90	\$67.80	\$70.29
1992-93	90.06	74.74	50.59
1993-94	88.01	79.60	53.65
1994-95	87.78	77.02	90.27
1995-96	76.89	79.73	101.24
1996-97	86.78	72.70	73.44
Totals	503.42	451.59	439.48
Annual Average (1992-1997)	\$83.90	\$75.27	\$73.25

**ALLOCATIONS, OBLIGATION AUTHORITY AND RECEIPTS
FOR THE PUERTO RICO HIGHWAYS AND TRANSPORTATION AUTHORITY
Under Prior Federal Aid Authorization Period
(Transportation Equity Act for the 21st Century)
Federal Fiscal Years 1998 Through 2003
(millions of dollars)**

Federal Fiscal Year	Allocations	Obligation Authority ¹	Actual Receipts ²
1997-98	\$110.00	\$92.91	\$99.47
1998-99	110.00	139.89	96.13
1999-00	110.00	81.12	177.46
2000-01	110.00	96.76	90.00
2001-02	110.00	79.25	74.71
2002-03	110.00	84.68	95.52
Totals	660.00	574.61	633.28
Annual Average (1998-2003)	\$110.00	\$95.77	\$105.55

1. Reflects reductions in the original allocations as a result of the Commonwealth not enacting various laws relating to drinking age, open containers, repeat offenders and operation of motor vehicles with a suspended license. Obligation Authority in 1998-1999 includes a special emergency allocation related to Hurricane Georges.
2. The actual receipts for fiscal years 1998 through 2003 include transfers to FTA (1999-\$31.7; 2000-\$108.2; 2001-\$40.0; 2002-\$40.00; 2003-\$40.0) for the Tren Urbano project. Receipts in 1999-2000 includes a special \$68.17 million transfer of funds for the Tren Urbano project.

DEBT SERVICE REQUIREMENTS FOR 2004 GRANT ANTICIPATION BONDS

The following table shows the debt service requirements for the 2004 Grant Anticipation Bonds. In order to issue Additional Bonds the Authority will be required to comply with certain debt service coverage tests. See “SECURITY AND SOURCES OF PAYMENT FOR THE 2004 GRANT ANTICIPATION BONDS – Additional Bonds.”

Year Ending September 30	2004 Grant Anticipation Bonds		
	Principal	Interest	Total
2004		\$2,393,046.77	\$ 2,393,046.77
2005	\$6,090,000.00	5,941,357.50	12,031,357.50
2006	6,235,000.00	5,799,670.00	12,034,670.00
2007	6,375,000.00	5,659,382.50	12,034,382.50
2008	6,590,000.00	5,444,307.50	12,034,307.50
2009	6,770,000.00	5,265,095.00	12,035,095.00
2010	6,935,000.00	5,095,845.00	12,030,845.00
2011	7,240,000.00	4,794,665.00	12,034,665.00
2012	7,540,000.00	4,492,102.50	12,032,102.50
2013	7,900,000.00	4,133,627.50	12,033,627.50
2014	8,275,000.00	3,760,187.50	12,035,187.50
2015	8,630,000.00	3,400,187.50	12,030,187.50
2016	9,045,000.00	2,989,447.50	12,034,447.50
2017	9,490,000.00	2,540,552.50	12,030,552.50
2018	9,935,000.00	2,095,552.50	12,030,552.50
2019	10,420,000.00	1,611,762.50	12,031,762.50
2020	10,935,000.00	1,097,962.50	12,032,962.50
2021	11,470,000.00	560,550.00	12,030,550.00
	\$139,875,000.00	\$67,075,301.77	\$206,950,301.77

TAX EXEMPTION

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 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 Bonds to be included in gross income for Federal income tax purposes retroactive to the date of issue of the Bonds. Pursuant to the 1998 Resolution and the Grant Anticipation Resolution, the Authority has covenanted to comply with the applicable requirements of the Code in order to maintain the exclusion of the interest on the Bonds from gross income for Federal income tax purposes pursuant to Section 103 of the Code. In addition, the Authority has made certain representations and certifications in certain closing documents relating to the Federal income tax analysis of the Bonds, executed in connection with the initial delivery of the Bonds. Bond Counsel will not independently verify the accuracy of those certifications and representations.

In the opinion of Nixon Peabody LLP, Bond Counsel, under existing law and assuming compliance with the aforementioned covenant, and the accuracy of certain representations and certifications made by the Authority described above, interest on the 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 Bonds is, however, included in the adjusted current earnings of certain corporations for purposes of computing the alternative minimum tax imposed on such corporations.

State Taxes

Bond Counsel is also of the opinion that under existing statutes, interest on the Bonds is exempt from personal income taxes imposed by the states, the Commonwealth and any political subdivision thereof.

Original Issue Discount

Bond Counsel is further of the opinion that the difference between the principal amount of the 2004 Grant Anticipation Bonds maturing on September 15 in each of the following years: 2008 and bearing interest at the rate of 2.25%, 2009 and bearing interest at the rate of 2.50%, 2010 and bearing interest at the rate of 2.90%, 2011 and bearing interest at the rate of 3.125%, 2012 and bearing interest at the rate of 3.375%, 2013 and bearing interest at the rate of 3.60%, 2015 and bearing interest at the rate of 3.80%, 2016 and bearing interest at the rate of 3.90%, 2017 and bearing interest at the rate of 4.00%, 2018 and bearing interest at the rate of 4.10%, 2020 and bearing interest at the rate of 4.25%, and 2021 and bearing interest at the rate of 4.30%; the Series I Bonds maturing on July 1, 2007 through July 1, 2021, inclusive; and the Series J Bonds maturing on July 1 in each of the following years: 2008 and bearing interest at the rate of 2.625%, 2009 and bearing interest at the rate of 2.50%, 2021 and bearing interest at the rate of 4.625%, 2022 and bearing interest at the rate of 4.70%, 2023 and bearing interest at the rate of 4.75%, 2024 and bearing interest at the rate of 4.80%, and the term bonds maturing July 1, 2034, July 1, 2039 and July 1, 2043 (collectively, 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 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, Commonwealth and local tax consequences of owning such Discount Bonds.

Original Issue Premium

The 2004 Grant Anticipation Bonds maturing on September 15 in each of the following years: 2005, 2006, 2007, 2008 and bearing interest at the rate of 5.00%, and 2010 through 2021, inclusive, each bearing interest at the rate of 5.00%; the Series I Bonds maturing on July 1, 2006 and July 1, 2022 through July 1, 2026, inclusive; and the Series J Bonds maturing on July 1 in each of the following years: 2006, 2007, 2008 and bearing interest at the rate of 5.00%, 2010 through 2020, inclusive, 2021 through 2024, inclusive and each bearing interest at the rate of 5.50%, and the term bond maturing on July 1, 2029 (collectively, the “Premium Bonds”) are being offered at prices in excess of their principal amounts. 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 bonds. Owners of the Premium Bonds are advised that they should consult with their own advisors with respect to the state, Commonwealth 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 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 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 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 Bonds, and thus on the economic value of the 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 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 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 Bonds may affect the tax status of interest on the Bonds. Bond Counsel expresses no opinion as to any Federal, state, Commonwealth or local tax law consequences with respect to the Bonds, or the interest thereon, if any action is taken with respect to the Bonds or the proceeds thereof upon the advice or approval of other counsel.

UNDERWRITING

The Underwriters have jointly and severally agreed, subject to certain conditions, to purchase the 2004 Grant Anticipation Bonds from the Authority at an aggregate discount of \$834,940.05 from the initial offering prices of the 2004 Grant Anticipation Bonds set forth or derived from information set forth on the inside cover pages hereof. The Underwriters have also jointly and severally agreed, subject to certain conditions to purchase the 2004 Transportation Revenue Bonds from the Authority at an aggregate discount of \$3,385,144.24 from the initial offering prices of the 2004 Transportation Revenue Bonds set forth or derived from information set forth on in the inside cover pages hereof. The obligations of the Underwriters are subject to certain conditions precedent, and they will be obligated to purchase, in each case, all the 2004 Grant Anticipation Bonds and the 2004 Transportation Revenue Bonds if any 2004 Grant Anticipation Bonds or 2004 Transportation Revenue Bonds are purchased. The Bonds may be offered and sold to certain dealers (including dealers depositing Bonds into investment trusts) and institutional purchasers at prices lower than such public offering prices and such offering prices may be changed, from time to time, by the Underwriters.

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

VERIFICATION OF MATHEMATICAL ACCURACY

The Arbitrage Group, Inc. will verify, from the information provided to them, the mathematical accuracy as of the date of delivery of the Series I Bonds of (i) the computations contained in the provided schedules to determine that the anticipated receipts from the securities and cash deposits listed in such schedules, to be held in escrow, will be sufficient to pay, when due, the principal, interest and call premium payment requirements, if any, of the Refunded Bonds (see *Plan of Financing*), and (ii) the computations of yield on both the securities and the Series I Bonds contained in such schedules used by Bond Counsel in its determination that interest on the Series I Bonds is excluded from gross income for federal income tax purposes. The Arbitrage Group, Inc. will express no opinion on the assumptions provided to them, nor as to the exclusion from gross income for Federal income tax purposes of the interest on the Series I Bonds.

LITIGATION

There is no pending litigation of any nature restraining or enjoining or seeking to restrain or enjoin the issuance, sale or delivery of the Bonds or in any way contesting or affecting the validity of the Bonds, the resolutions or the proceedings of the Authority taken with respect to the authorization, issuance or sale thereof, or the pledge or application of any moneys under the 1968 Resolution, the 1998 Resolution or the Grant Anticipation Resolution or the existence or powers of the Authority.

The Authority is involved as defendant in various legal proceedings arising in the normal course of its business. Many of these proceedings involve claims against the Authority based on breach of contract, claims for additional compensation under construction contracts, claims for damages from automobile accidents allegedly caused by alleged defects in highway construction or maintenance and challenges to public bidding procedures conducted by the Authority, among others. The Authority and its General Counsel do not believe that liability from any such legal proceedings, in excess of available insurance coverage and the provision for losses not covered by insurance, as shown on the financial statements, will have a material adverse effect on the financial condition of the Authority.

LEGAL MATTERS

The form of opinions of Nixon Peabody LLP, New York, New York, Bond Counsel, is set forth in Appendix II to this Official Statement. Certain legal matters will be passed upon for the Underwriters by O'Neill & Borges, San Juan, Puerto Rico.

LEGAL INVESTMENT

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

GOVERNMENT DEVELOPMENT BANK

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 Authority in connection with the Bonds offered hereby. As financial advisor, Government Development Bank participated in the selection of the Underwriters of the Bonds. Certain of the Underwriters have been selected by Government Development Bank to serve from time to time as underwriters of its obligations and the obligations of the Commonwealth, its instrumentalities and public corporations. Certain of the Underwriters or their affiliates participate in other financial transactions with Government Development Bank.

RATINGS

The 2004 Grant Anticipation Bonds have been assigned underlying ratings of "A2," by Moody's Investors Service, Inc. ("Moody's") and of "A," by Standard & Poor's Ratings Services ("Standard & Poor's"). Except as noted in the following sentence, the 2004 Transportation Revenue Bonds have been assigned ratings of "Baa1" by Moody's and of "A" by Standard & Poor's. Moody's and Standard & Poor's are expected to give the Insured Bonds ratings of "Aaa" and "AAA," respectively. The ratings reflect only the respective opinions of such rating agencies. Any explanation of the significance of such ratings must be obtained from the respective rating agency. There is no assurance that the ratings will continue for any given period of time or will not be revised downward or withdrawn entirely by any or all of such rating agencies. Any such downward revision or withdrawal of the ratings could have an adverse effect on the market prices of the Bonds.

CONTINUING DISCLOSURE

In order to assist the Underwriters in complying with the requirements of Rule 15c2-12, as amended (the "Rule"), promulgated by the Securities and Exchange Commission ("SEC"), the Authority, as specifically stated hereinbelow, will agree to the following:

1. Each of the Authority and the Commonwealth will agree to file within 305 days after the end of each fiscal year beginning with its fiscal year ending on June 30, 2004, with each NRMSIR and with any Commonwealth state information depository ("SID"), core financial information and operating data for the prior 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 Authority and the Commonwealth, as the case may be, and information as to revenues, expenditures, financial operations and indebtedness of the Authority and the Commonwealth, as the case may be, in each case, generally found or incorporated by reference in this Official Statement; and

2. The Authority will agree to file, in a timely manner, with each NRMSIR or with the MSRB and with any SID, notice of any failure to comply with paragraph 1 above and of the occurrence of any of the following events with respect to the Bonds if, in the judgment of the Authority or its agent, such event is material:

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

- (i) release, substitution, or sale of property securing repayment of the Bonds; and
- (j) rating changes.

With respect to the following events:

Events (c) and (d). For a description of the Bonds, see *The Bonds*. The Authority does not undertake to provide any notice with respect to credit enhancement added after the primary offering of the Bonds, unless the Authority applies for or participates in obtaining the enhancement.

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

Event (g). The Authority does not undertake to provide the above-described event notice of a mandatory scheduled redemption, not otherwise contingent upon the occurrence of an event, if (i) the terms, dates and amounts of redemption are set forth in detail in this Official Statement under “Redemption of the Grant Anticipation Bonds,” “Redemption of the Series I Bonds” and “Redemption of the Series J Bonds” under *The Bonds*, (ii) the only open issue is which Series I Bonds and Series J 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 Bonds and the Grant Anticipation Resolution or 1998 Resolution, and (iv) public notice of the redemption is given pursuant to Securities Exchange Act of 1934 Release No. 3423856 of the SEC, even if the originally scheduled amounts are reduced by prior optional redemptions or purchases of Bonds.

As of the date of this Official Statement, there is no Commonwealth SID, and the nationally recognized municipal securities information repositories are: Bloomberg Municipal Repository, 100 Business Park Drive, Skillman, New Jersey 08558; Standard & Poor’s, Securities Evaluation, Inc., 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 Authority may from time to time choose to provide notice of the occurrence of certain other events in addition to those listed above whether or not, such other events are material with respect to the Bonds, but the Authority does not undertake to provide any such notice of the occurrence of any event, except those events, if material, listed above.

The Commonwealth and the Authority acknowledge that their respective undertakings pursuant to the Rule described above are intended to be for the benefit of the Beneficial Owners of the Bonds, and shall be enforceable by any such Beneficial Owners; provided that the right to enforce the provisions of their respective undertakings shall be limited to a right to obtain specific enforcement of the Authority’s or the Commonwealth’s obligations hereunder.

No Beneficial Owner may institute any suit, action or proceeding at law or in equity (“Proceeding”) for the enforcement of the foregoing covenants (the “Covenants”) or for any remedy for breach thereof, unless such Beneficial Owner shall have filed with the Authority and the Commonwealth written notice of any request to cure such breach, and the Authority or the Commonwealth, as applicable, shall have refused to comply within a reasonable time. All Proceedings shall be instituted only in a Commonwealth court located in the Municipality of San Juan for the equal benefit of all Beneficial Owners of the outstanding Bonds benefited by the Covenants, and no remedy shall be sought or granted other than specific performance of any of the Covenants at issue. Moreover, Proceedings filed by Beneficial Owners against the Commonwealth may be subject to the sovereign immunity provisions of Sections 2 and 2A of Act No. 104, approved June 29, 1955, as amended (32 L.P.R.A. §3077 and §3077a), which governs the scope of legal actions against the Commonwealth, substantially limits the amount of monetary damages that may be awarded against the Commonwealth and provides certain notice provisions, the failure to comply with which may further limit any recovery.

The Covenants may only be amended if:

(1) the amendment is made in connection with a change in circumstances that arises from a change in legal requirements, change in law, or change in the identity, nature, or status of the Authority or the Commonwealth, or type of business conducted; the Covenants, as amended, would have complied with the requirements of the Rule at the time of award of the Bonds, after taking into account any amendments or change in circumstances; and the amendment does not materially impair the interest of Beneficial Owners, as determined by parties unaffiliated with the Authority or the Commonwealth; or

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

APPENDIX I

Puerto Rico Highways and Transportation Authority

Audited Financial Statements

as of

June 30, 2003

Audited Financial Statements

Puerto Rico Highways and Transportation Authority

June 30, 2003

Puerto Rico Highways and Transportation Authority
Audited Financial Statements
June 30, 2003

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Report of Independent Auditors

Hon. Fernando Fagundo Fagundo, Secretary
Department of Transportation and Public Works,
Commonwealth of Puerto Rico

We have audited the accompanying statements of net assets of Puerto Rico Highways and Transportation Authority (the Authority), as of June 30, 2003 and 2002, and the related statements of revenues, expenses and changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Authority's management. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Puerto Rico Highways and Transportation Authority at June 30, 2003 and 2002, and the changes in its net assets and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States.

The Management's Discussion and Analysis on pages 3 through 7, is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued our report, dated September 26, 2003, on our consideration of the Authority's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audits.

Our audits were conducted for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying supplemental schedule listed under "Required Supplemental Information" in the table of contents is presented for the purpose of additional analysis and is not a required part of the financial statements. This schedule is the responsibility of the Authority's management. Such schedule has not been subjected to the auditing procedures applied in our audit of the financial statements and, accordingly, we express no opinion on it.

Ernst + Young LLP

September 26, 2003, except for
Note 9, as to which the
date is October 30, 2003

Stamp No. 1921016
affixed to
original of
this report.

Puerto Rico Highways and Transportation Authority
Year ended June 30, 2003
MANAGEMENT'S DISCUSSION AND ANALYSIS

This Section of the Authority's financial report represents a discussion and analysis of the Authority's financial performance during the fiscal year that ended June 30, 2003. Please read this information in conjunction with the Authority's Financial Statements.

FINANCIAL HIGHLIGHTS

1. Operating revenues for fiscal year 2003 and 2002 were approximately **\$485 million and \$480 million**, respectively.
2. Operating expenses for fiscal year 2003 and 2002 were approximately **\$113 million and \$57 million**, respectively.
3. Total net assets at June 30, 2003 and 2002 amounted to approximately **\$7.61 billion and \$7.64 billion**, respectively.
4. Total capital assets (net of accumulated depreciation) at June 30, 2003 and 2002 were approximately **\$12.3 billion and \$11.8 billion**, respectively.

OVERVIEW OF THE FINANCIAL STATEMENTS

The financial statements provide both long-term and short-term information about the Authority's overall financial status. The financial statements also include notes that explain some of the information in the financial statements and provide more detailed data. The statements are followed by a section of other financial information that further explains and supports the information in the financial statements.

The Authority's financial statements are prepared in conformity with accounting principles generally accepted in the United States as established by the Governmental Accounting Standards Board (GASB). The Authority has implemented the provisions of GASB Statement No. 34, "Basic Financial Statements and Management's Discussion and Analysis for States and Local Governments" (Statement 34) for the fiscal year beginning July 1, 2001. Under Statement 34, the operations of the Authority are accounted for as an Enterprise Fund of the Commonwealth of Puerto Rico and the financial statements are presented on the accrual basis of accounting in order to recognize the flow of economic resources.

The Statements of Net Assets present the Authority's assets and liabilities and any underlying restrictions on such assets and liabilities. Net assets, which is the difference between the Authority's assets and liabilities, is one-way to measure the Authority's financial health or position.

Puerto Rico Highways and Transportation Authority
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

FINANCIAL ANALYSIS OF THE AUTHORITY

Net Assets

Net assets may serve, over time, as a useful indicator of a government's financial position. In the case of the Authority, assets exceeded liabilities by approximately **\$7.61 billion** at the close of the 2003 fiscal year.

The largest portion of the Authority's net assets consists of capital assets (e.g., rights-of-way, roads, bridges, buildings, etc.) less any related debt still outstanding used to acquire those assets, which total approximately **\$7.07 billion**. The Authority uses these capital assets to provide services, and consequently, these assets are not available to liquidate liabilities or cover other spending. In addition, net assets amounting to approximately **\$504 million** are restricted for debt service and construction.

Changes in Net Assets

Net assets at June 30, 2003 declined by approximately **\$29 million** or 0.4% from the restated net assets at June 30, 2002. Major components of the change in net assets consist of the following:

- Total operating revenues increased by 1% during fiscal year 2003 to approximately **\$485 million**. The major component of this increase was related to the increase in toll revenues of 3.7% when compared with fiscal year 2002.
- Total operating expenses increased by 98% to approximately **\$112.6 million** during fiscal year 2003. The increase was mainly caused by the change in the accounting policy of capitalization of costs implemented during 2002 to comply with Statement 34. Before the fiscal year 2002, all expenses and costs, direct and indirect, including administrative expenses, were capitalized as project costs. The new accounting policy consists of including in "General and Administrative Expense" in the Statements of Revenues, Expenses and Changes in Net Assets 20% of expenses attributable to non-technical offices and all project costs not related to bridges and/or roads. Also, those costs invested in small projects that do not qualify as extraordinary repairs and/or do not extend the useful life of an asset, are recorded as "Repair and Maintenance of Roads and Bridges" in the Statements of Revenues, Expenses and Changes in Net Assets. In addition, all projects which are not related to bridges and/or roads will be recorded as "General and Administrative Expense". The effect of this new accounting policy on fiscal year 2002 is presented in the cumulative effect of a change in accounting principle.
- Non-operating expenses were approximately **\$285 million** in 2003, an increase of approximately 34% over the **\$213 million** in 2002. A major component of the change was an increase in interest expense of approximately 30% due to the issuance of additional Transportation Revenue Bonds for capital improvements.
- Contributions, primarily from the US Federal Government, amounted to approximately **\$153 million** during 2003 and **\$201 million** during 2002.

Puerto Rico Highways and Transportation Authority
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

FINANCIAL ANALYSIS OF THE AUTHORITY (continued)

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At June 30, 2003, the Authority had invested approximately **\$12.3 billion** in capital assets (net of related depreciation) including roads, bridges, buildings, land and equipment.

In 1994, the Authority began planning and designing and in 1996 began construction of a new mass transit rail project for the San Juan Metropolitan area known as "Tren Urbano". Through June 30, 2003, the Authority has incurred approximately **\$2.135 billion** in costs for this project. Tren Urbano is the largest single project included in the Authority's current Construction Improvement Program. Its initial phase consists of approximately 17 km. of track running from Bayamón to Santurce. The Authority has contracted with various private parties for the construction of the project and has entered into a five-year contract for the operation and maintenance of the system.

Debt Administration

The Authority's bond sales must be approved by the Secretary of Transportation and Public Works, who exercises the powers of Governing Board of the Authority in coordination with Government Development Bank for Puerto Rico, Fiscal Agent of Commonwealth of Puerto Rico. The Authority must comply with certain rules and regulations of the United States Treasury Department and the United States Securities and Exchange Commission relating to such sales.

Long-term debt includes Highway Revenue Bonds issued pursuant to the 1968 Bond Resolution (No. 68-18) and Transportation Revenue and Subordinated Transportation Revenue Bonds issued pursuant to the 1998 Bond Resolution (No. 98-06). At June 30, 2003, the Authority had approximately **\$5.3 billion** principal amount of Highway and Transportation Revenue Bonds outstanding, net of unamortized discounts and net losses on advance refundings. That amount represents an increase of approximately 21% from June 30, 2002, most of which increase resulted from the issuance of Transportation Revenue Bonds to finance part of the Authority's Construction Improvement Program of **\$2.02 billion** for 2004 through 2008 and to refinance at lower rates other outstanding Highway and Transportation Revenue Bonds.

More detailed information about the Authority's long-term debt is presented in notes 4 and 5 to the financial statements.

Of the approximate **\$5.3 billion** principal amount Highway and Transportation Revenues Bonds outstanding, approximately **\$2.5 billion** is insured and rated Aaa by Moody's Investors Service (Moody's) and AAA by Standard & Poor's (S&P). The remaining uninsured bonds are rated Baa1 by Moody's and A by S&P, except for the Subordinated Transportation Revenue Bonds, which are rated Baa2 and A-, respectively.

Puerto Rico Highways and Transportation Authority
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The economy of Puerto Rico must be analyzed as a region within the U.S. economy, since it is part of the U.S. monetary and banking system, as well as within its territorial boundaries. The main drive of the Puerto Rico economy is a huge external sector closely tied to the flow of merchandise, tourists, and capital between Puerto Rico and the Mainland. Thus, historically, the real growth rates of the Puerto Rico economy have closely followed those of the U.S. economy. In fiscal year 2003, Puerto Rico experienced the consequences of the slowdown in the U.S. economy. However, in spite of the economic slowdown, the consumption of gasoline, which is the main source of recurrent revenues of the Authority, posted just a 0.7% decrease in fiscal year 2003.

The economy of Puerto Rico is expected to resume growing in fiscal year 2004, advancing at a rate of approximately 3.9% in real terms, according to the latest forecast prepared by the Interamerican University of Puerto Rico. The Authority expects this turnaround in economic performance to contribute to achieving the conservative income projections of the Authority for fiscal year 2004.

The Authority adopted the 2004 fiscal year Budget on July 1, 2003. The revenues for fiscal year 2004 are projected to amount to approximately **\$518 million**. The Authority also receives aid for highway construction from the Federal Highway Administration (FHWA) and the Federal Transportation Administration (FTA). This budget includes a total of **\$712 million** for the Construction Improvement Program (CIP), including Tren Urbano. From this total, **\$549 million** is projected to be applied to the strategic network, congestion relief projects and others, which represents an increase of approximately 26 % in fiscal year 2004 from fiscal year 2003.

Highway construction projects included by the Authority in its CIP are designed to enhance the economic development of Puerto Rico. Projects include new highway construction, principally of primary roads and toll ways, and construction improvements designed to alleviate the traffic congestion of the San Juan Metropolitan area. It also includes reconstruction of existing highways, a bridge program and installation of safety features and other projects. The major highway projects include construction of Eastern Corridor, sections of PR-53, Yabucoa-Maunabo and Maunabo-Guayama (which includes the first highway tunnel through a mountain in Puerto Rico) and of PR-10 from Utuado-Adjuntas, conversion to expressway of PR-2 from Mayagüez to Ponce and PR-22 to PR-2 from Arecibo-Aguadilla, the construction of the PR-5 toll way connecting PR-2 to Las Cumbres Avenue (PR-199), the relocation of the PR-167 (PR-148) from Bayamón to Comerío and Naranjito, the relocation of the PR-137 in Vega Baja and PR-156 in Aguas Buenas, Las Cumbres Avenue, from Trujillo Alto to Bayamón, and the conversion to expressway of PR-2.

Puerto Rico Highways and Transportation Authority
MANAGEMENT'S DISCUSSION AND ANALYSIS (continued)

CONTACTING THE AUTHORITY'S FINANCIAL MANAGEMENT

This financial report is designed to provide our bondholders, patrons, and other interest parties with a general overview of the Authority's finances and to demonstrate the Authority's accountability for the money it receives. If you have question or need additional financial information, contact the Puerto Rico Highway and Transportation Authority, Finance Area, P.O. Box 42007, San Juan, Puerto Rico 00940-2007.

Puerto Rico Highways and Transportation Authority
Statements of Net Assets

	June 30	
	2003	2002
Assets:		
Current assets:		
Cash and cash equivalents	\$ 42,525,193	\$ 33,686,851
Accounts receivable, net of allowance for uncollectible accounts of \$41,061,833 in 2003 and \$38,472,421 in 2002	3,641,587	8,233,797
Prepaid expenses and other assets	3,608,106	3,655,200
Total current assets	49,774,886	45,575,848
Restricted assets:		
Cash and cash equivalents	48,861,221	65,104,447
Cash and investments with trustee	762,645,778	867,716,879
Receivables:		
Puerto Rico Treasury Department	199,395	237,829
US Federal government	7,511,371	5,414,197
Accrued interest and other	2,194,242	3,793,700
Total restricted assets	821,412,007	942,267,052
Capital assets:		
Land	1,713,011,071	1,710,911,521
Construction work in progress	5,282,310,698	4,615,205,178
Property and equipment, net of accumulated depreciation of \$5,780,759,049 in 2003 and \$5,518,170,536 in 2002	5,324,028,714	5,504,163,644
Total capital assets	12,319,350,483	11,830,280,343
Revenue bond issuance costs, net of accumulated amortization of \$16,306,885 in 2003 and \$12,549,289 in 2002	89,046,964	57,317,913
Advances to governmental entities for construction projects	20,506,234	17,881,277
Total assets	\$13,300,090,574	\$12,893,322,433

	June 30	
	2003	2002
Liabilities		
Current liabilities:		
Accounts payable	\$ 21,354,664	\$ 10,260,907
Other liabilities	13,598,490	3,553,269
Liabilities payable from restricted assets:		
Accounts payable	188,406,790	300,108,489
Accrued interest payable	108,995,758	112,625,348
Other liabilities	9,485,635	9,738,978
Current portion of bonds payable	10,435,000	81,925,000
Total current liabilities	<u>352,276,337</u>	<u>518,211,991</u>
Long-term debt:		
Accrued legal claims	18,000,000	18,000,000
Accrued vacation and sick leave	16,234,980	19,626,832
Loan payable	-	300,000,000
Bonds payable, net unamortized discount and net loss on advance refundings	5,303,959,351	4,400,490,064
Total long-term debt	<u>5,338,194,331</u>	<u>4,738,116,896</u>
Total liabilities	<u>5,690,470,668</u>	<u>5,256,328,887</u>
Net Assets		
Invested in capital assets, net of related debt	7,070,203,116	7,169,108,191
Restricted for debt service	437,667,218	410,098,060
Restricted for construction	66,421,606	27,771,177
Unrestricted	35,327,966	30,016,118
Total net assets	<u>7,609,619,906</u>	<u>7,636,993,546</u>
Total liabilities and net assets	<u>\$13,300,090,574</u>	<u>\$12,893,322,433</u>

See accompanying notes.

Puerto Rico Highways and Transportation Authority
Statements of Revenues, Expenses and Changes in Net Assets

	Year ended June 30	
	2003	2002
Operating revenues		
Excise taxes:		
Gasoline	\$ 173,506,662	\$ 174,884,874
Diesel oil	15,297,932	18,922,151
Petroleum Tax	120,000,000	120,000,000
Vehicle license fees	31,920,258	30,693,345
Toll fares	135,351,684	130,498,021
Other	8,916,239	5,156,250
Total operating revenues	<u>484,992,775</u>	<u>480,154,641</u>
Operating expenses		
Toll highways administration and maintenance	38,783,798	37,292,706
Repair and maintenance of roads and bridges	40,723,313	-
General and administrative	31,823,722	18,464,417
Other	1,241,077	968,672
Total operating expenses before depreciation and amortization	<u>112,571,910</u>	<u>56,725,795</u>
Operating income before depreciation and amortization	<u>372,420,865</u>	423,428,846
Depreciation and amortization	<u>267,393,484</u>	<u>266,975,070</u>
Operating income	<u>105,027,381</u>	156,453,776
Non-operating revenues (expenses)		
Interest earned on investments	27,605,343	29,051,404
Net (decrease) increase in fair value of investments	(4,402,184)	4,156,272
Interest on TIFIA loan and line of credit	(15,405,341)	(21,104,458)
Interest expense on revenue bonds outstanding	(292,848,341)	(225,282,563)
Net non-operating expenses	<u>(285,050,523)</u>	<u>(213,179,345)</u>
Loss before contributions	<u>(180,023,142)</u>	<u>(56,725,569)</u>
Contributions from US Federal government and other	<u>152,649,502</u>	201,226,940
Change in net assets	<u>(27,373,640)</u>	144,501,371
Net assets at beginning of the year	<u>7,636,993,546</u>	1,832,373,910
Cumulative effect of change in accounting principle	-	5,660,118,265
Net assets at beginning of year (as restated)	<u>7,636,993,546</u>	<u>7,492,492,175</u>
Net assets at end of the year	<u>\$7,609,619,906</u>	<u>\$7,636,993,546</u>

See accompanying notes.

Puerto Rico Highways and Transportation Authority
Statements of Cash Flows

	Year ended June 30	
	2003	2002
Cash flows from operating activities		
Receipts from excise taxes and vehicle licenses fees	\$ 340,763,286	\$ 344,425,170
Receipts from toll fares	135,351,684	130,498,021
Receipts from other sources	8,916,239	2,427,065
Other receipts	4,639,305	43,955,765
Payments to employees	(3,391,852)	(1,749,456)
Payments to others	(203,387,975)	(4,589,929)
Net cash flows provided by operating activities	<u>282,890,687</u>	<u>514,966,636</u>
Cash flows from non-capital financing activities		
Payments to the Department of Transportation and Public Works	(2,624,957)	(6,901,561)
Net cash flows used in non-capital and financing activities	<u>(2,624,957)</u>	<u>(6,901,561)</u>
Cash flows from capital and related financing activities		
Payments of bond issuance costs, including net loss on advance refunding	(97,531,372)	(15,336,634)
Receipts from Federal government and Commonwealth of Puerto Rico grants	150,552,328	202,742,874
Acquisition and construction of capital assets	(756,463,624)	(776,510,081)
Proceeds from bond issuance	1,753,711,608	1,129,864,057
Principal payments to retire revenue bonds	(855,930,000)	(489,035,000)
Payments of line of credit, net of advances	-	(40,787,860)
Interest payments on revenue bonds	(311,883,272)	(234,454,110)
Principal payment to cancel loan payable	(300,000,000)	-
Net cash flows used in capital and related financing activities	<u>(417,544,332)</u>	<u>(223,516,754)</u>
Cash flows from investing activities		
Net sales (purchase) of investments	100,668,917	(320,449,124)
Interest received	29,204,801	28,233,941
Net cash flows provided by (used in) investing activities	<u>129,873,718</u>	<u>(292,215,183)</u>
Net decrease in cash and cash equivalents	<u>(7,404,884)</u>	<u>(7,666,862)</u>
Cash and cash equivalents at beginning of year, including restricted cash and cash equivalents	<u>98,791,298</u>	<u>106,458,160</u>
Cash and cash equivalents at end of year, including restricted cash and cash equivalents	<u>\$ 91,386,414</u>	<u>\$ 98,791,298</u>

Puerto Rico Highways and Transportation Authority
Statements of Cash Flows

	Year ended June 30	
	2003	2002
Reconciliation of operating income to net cash provided by operating activities		
Operating income	\$105,027,381	\$156,453,776
Adjustments to reconcile operating income to net cash provided by operating activities:		
Bad debt provision	2,589,412	2,713,679
Depreciation and amortization	267,393,484	266,975,070
Changes in assets and liabilities:		
Decrease (increase) in accounts receivable	2,041,232	(1,244,373)
Decrease (increase) in prepaid expenses	47,094	(1,753,613)
(Decrease) increase in accounts payable	(90,816,064)	93,571,553
Decrease in accrued vacation and sick leave	(3,391,852)	(1,749,456)
	\$282,890,687	\$514,966,636
Net cash flows provided by operating activities	\$282,890,687	\$514,966,636

See accompanying notes.

Puerto Rico Highways and Transportation Authority

Notes to Financial Statements

June 30, 2003

1. Organization and Summary of Significant Accounting Policies

Puerto Rico Highways and Transportation Authority (the Authority) is a public corporation and instrumentality of the Commonwealth of Puerto Rico, created by Act No. 74 of June 23, 1965, as amended, to provide roads and other facilities for the movement of persons, vehicles and vessels, and for the planning, promotion and feasibility of mass transportation systems. The Authority is a component unit of the Commonwealth of Puerto Rico and accordingly is included in the general-purpose financial statements of the Commonwealth. The powers normally exercised by a Board of Directors are vested with the Secretary of the Department of Transportation and Public Works (DTPW). The Authority is exempt from the payment of any taxes on its revenues and properties.

The accounting policies of the Authority conform to accounting principles generally accepted in the United States as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standards setting body for establishing governmental accounting and financial reporting principles. The following is a summary of the significant accounting policies:

Change in Accounting Principle

Beginning with fiscal year 2002, the Authority is preparing and presenting its financial statements in accordance with the provisions of GASB Statement No. 34, "Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments" (Statement 34) in fiscal year 2002, effective July 1, 2001. Statement 34 established financial and reporting standards for all state and local governments and related entities. Under Statement 34, the Authority is considered an enterprise fund of the Commonwealth of Puerto Rico. The most significant effects of the adoption of Statement 34 relate to the inclusion of general infrastructure assets in the Authority's Statements of Net Assets, net of their corresponding depreciation, the presentation of the Authority's financial statements under the accrual basis of accounting, the inclusion of management's discussion and analysis, and the presentation of the Statements of Cash Flows under the direct method.

The effect of the implementation of Statement 34 in prior fiscal years has been presented in Cumulative Effect of Change in Accounting Principle in the Statements of Revenues, Expenses and Changes in Net Assets as of June 30, 2002. The major components of the Cumulative Effect of Change in Accounting Principle are as follows:

Property and equipment previously recorded in general fixed assets account group and enterprise fund, net of prior years accumulated depreciation	\$5,636,697,965
Long-term debt previously recorded in the general long-term debt account group	61,047,131
Other	(37,626,831)
	<hr/>
	\$5,660,118,265
	<hr/> <hr/>

Puerto Rico Highways and Transportation Authority

Notes to Financial Statements (continued)

1. Organization and Summary of Significant Accounting Policies (continued)

Change in Accounting Policy

During fiscal year 2002, the Authority changed its accounting policy related to the capitalization of project costs to comply with Statement 34. Before the adoption of Statement 34, the Authority capitalized all expenses and costs, direct and indirect, including administrative expenses, as project costs. The new accounting policy of capitalization of project costs consists of including 20% of all non-technical offices as "Operating Expense" in the Statements of Revenues, Expenses and Changes in Net Assets. Also, those costs invested in small projects that do not qualify as extraordinary repairs and/or do not extend the useful life of an asset, are recorded as "Repair and Maintenance of Roads and Bridges" in the Statements of Revenues, Expenses and Changes in Net Assets. In addition, all projects, which are non-related to bridges and/or roads, are recorded as "Operating Expenses". The effect of this new accounting policy on fiscal year 2002 is presented in the cumulative effect of a change in accounting principle.

Basis of Accounting

Under Statement 34, the operations of the Authority are accounted for as an enterprise fund on the accrual basis in order to recognize the flow of economic resources. Under this basis, revenues are recognized in the period in which they are earned, expenses are recognized in the period in which they are incurred, depreciation of assets is recognized, and all assets and liabilities associated with the operation of the Authority are included in the Statements of Net Assets. The principal revenues of the Authority are excise taxes and toll revenues. Operating expenses for the Authority consist of the costs of operating and maintaining Puerto Rico's toll highways and related general and administrative expenses. All other revenues and expenses are reported as non-operating revenues and expenses.

The Authority adopted the provisions of Governmental Accounting Standards Board Statement No. 20 *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting* (GASB No. 20). In adopting GASB No. 20, the Authority elected not to apply all Statements and Interpretations of the Financial Accounting Standards Board, Accounting Principles Board Opinions and Accounting Research Bulletins of the Committee on Accounting Procedure issued after November 30, 1989.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The implementation of Statement 34 involves the use of assumptions and estimates in the determination of the cost of general infrastructure assets, such as roads, highways, bridges and land. The cost of such assets is estimated based on current costs for similar assets deflated using the general price index through the estimated average age of the assets.

Puerto Rico Highways and Transportation Authority

Notes to Financial Statements (continued)

1. Organization and Summary of Significant Accounting Policies (continued)

Cash Equivalents

The Authority considers all highly liquid investments with maturities of three months or less when purchased to be cash equivalents. As of June 30, 2003 and 2002, cash equivalents consisted of time deposits and repurchase agreements.

Investments

The Authority reports investments at fair value in the accompanying Statements of Net Assets and the changes in the fair value of investments in the accompanying Statements of Revenues, Expenditures and Changes in Net Assets.

Restricted Assets

Restricted assets of the Authority represent bond proceeds designated for construction, and other monies required to be restricted for debt service, operations, maintenance, administration, renewal, and replacement.

Advances to the Department of Transportation and Public Works

The Authority periodically advances funds to DTPW to carry out its participation in the construction improvement program of the Authority. These advances are presented as non-current assets in the accompanying Statements of Net Assets.

Capital Assets

Cost Basis

All capital assets are recorded at historical cost or estimated historical cost. The cost of property and equipment includes costs for infrastructure assets (rights-of-way and bridge substructures and highways and bridges), toll facilities, equipment and other related costs (including software), buildings and furniture and equipment. Highways and bridge substructures include road sub-base, grading, land clearing, embankments, and other related costs. Costs for infrastructure assets include construction costs, design and engineering fees and administrative and general expenses paid from construction monies.

Capitalization Policy

Costs to acquire additional capital assets, which replace existing assets or otherwise prolong their useful lives, are capitalized for toll equipment, buildings, toll facilities, and other related costs.

Depreciation is provided using the straight-line method over an estimated useful live of 40 years for roads and highways and 50 years for bridges. Furniture and equipment is stated at cost. Depreciation for furniture and equipment is provided using the straight-line method over an estimated useful life of 10 years.

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

1. Organization and Summary of Significant Accounting Policies (continued)

Capital Assets (continued)

Capitalization Policy (continued)

Project costs incurred on the Tren Urbano, a rail mass transportation project, are recorded at cost and included in Construction in Progress in the accompanying Statements of Net Assets.

Unamortized Losses on Advance Refunding

Losses resulting from current or advance refunding of debt are deferred and amortized over the shorter of the life of the new debt and the remaining life of old debt. The amount deferred is reported as a reduction of the debt and the amount amortized is reported as a component of interest expense.

Vacation and Sick Leave

Employees earn annual vacation leave at the rate of 30 days per year up to a maximum permissible accumulation of 60 days for regular employees. Employees accumulate sick leave at the rate of 18 days per year. Sick leave is only payable if the regular employee resigns and has more than 10 years of employment, or retires and takes a pension. Maximum permissible accumulation for sick leave is 90 days for all employees, and the excess is paid within the next year. The Authority records as a liability and as an expense the vested accumulated vacation and sick leave as benefits accrue to employees.

Bond Premiums/Discounts and Bond Issuance Costs

Bond premiums/discounts are presented in the accompanying Statements of Net Assets as an increase/reduction of the face amount of bonds payable. Bond issuance costs are presented as a deferred asset in the accompanying Statements of Net Assets. The premiums/discounts and issuance costs are amortized over the life of the bonds on a method that approximates the effective interest method. Amortization expense related to bond premium/discounts was approximately \$8,917,000 and \$2,000,000 for the years ended June 30, 2003 and 2002, respectively, and is included as a component of interest expense in the accompanying Statements of Revenues, Expenses and Changes in Net Assets. Depreciation and amortization expense includes amortization of bond issuance costs for the years ended June 30, 2003 and 2002 of approximately \$3,757,000 and \$2,600,000, respectively.

Claims and Judgments

The estimated amount of the liability for claims and judgments is recorded on the accompanying Statements of Net Assets based on the Authority's evaluation of the probability of an unfavorable outcome in the litigation of such claims and judgments. The Authority consults with legal counsel upon determining whether an unfavorable outcome is expected.

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

1. Organization and Summary of Significant Accounting Policies (continued)

Operating Revenues and Expenses

Revenues associated with excise taxes, vehicles license fees, and toll fares are recorded as operating revenues, while expenses related to the administration and maintenance of toll highways, repair and maintenance of roads and bridges, and administrative expenses are recorded as operating expenses. All other revenues and expenses are considered non-operating.

Budgetary Data

The Authority prepares its annual budget following the cash basis of accounting while the financial statements are presented under generally accepted accounting principles (GAAP) and standards established by the GASB. The actual results of operations presented in the Combined Statement of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual - All Governmental Fund Types are in accordance with the budgetary basis of accounting to provide a meaningful comparison of actual with budget.

The Authority uses the following procedures in establishing the budgetary data reflected in the financial statements:

1. The Executive Director submits to the Commonwealth Secretary of Transportation and Public Works (the Secretary) a proposed operating budget for the fiscal year commencing the following July 1. The operating budget includes proposed expenditures and the means of financing them.
2. The budget is approved through a resolution by the Secretary.
3. After the approval of the operating budget, the Secretary is authorized to transfer budgeted amounts within any funds.

The major differences between the budgetary basis of accounting and GAAP are:

1. Revenues are recorded when payments are received (budgetary), as opposed to when earned (GAAP).
2. Expenditures are recorded when payments are made (budgetary) as opposed to when the liability is incurred (GAAP).
3. Advances to governmental entities for construction projects are recorded when paid (budgetary) as opposed to being capitalized as property and equipment when costs are incurred (GAAP).

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

1. Organization and Summary of Significant Accounting Policies (continued)

New Accounting Pronouncement

In May 2002, the GASB issued GAS No. 39 (Statement 39), *Determining Whether Certain Organizations are Component Units*. The objective of Statement 39 is to provide criteria for determining whether certain organizations should be reported as component units based on the nature and significance of their relationship with a primary government and to clarify reporting requirements for those organizations. This statement is effective for financial statements for fiscal years beginning after June 15, 2003. The Authority is currently evaluating its impact on results of operations, financial position and cash flows.

Reclassification

Certain amounts from 2002 have been reclassified to conform with current year's presentation.

2. Cash, Cash Equivalents and Investments

Cash and cash equivalents at June 30, 2003 and 2002 consisted of the following:

	2003	2002
Cash held by the Puerto Rico Department of the Treasury	\$ 21,503,069	\$ 39,777,436
Repurchase agreements	52,927,857	82,357,696
Restricted cash held by escrow agents	18,411,000	17,927,236
Puerto Rico State Infrastructure Bank deposits	3,744,549	2,947,555
Cash on hand and in banks	6,891,967	5,577,395
	103,478,442	148,587,318
Less checks issued in excess of bank balance	12,092,028	49,796,020
	\$ 91,386,414	\$ 98,791,298

Cash with the Department of the Treasury is uninsured and uncollateralized. Repurchase agreements consist of notes from the U.S. and Puerto Rico Governments and collateralized mortgage obligations. These investments are held in the Authority's name.

Restricted cash amounting to \$3,000,000 represents funds held in an escrow fund under an agreement with the U.S. Army Corps of Engineers (the Agreement). Under terms of the Agreement, the Authority is required to maintain escrow funds to secure performance in connection with a mitigation plan related to a construction project. The escrow funds will be released as performance is demonstrated. Restricted cash amounting to \$15,411,000 represents funds held in an escrow account pursuant to a concession agreement with Autopistas de Puerto Rico y Compañía S.E. (see Note 8).

Puerto Rico Highways and Transportation Authority

Notes to Financial Statements (continued)

2. Cash, Cash Equivalents and Investments (continued)

Puerto Rico State Infrastructure Bank (the SIB) deposits represent funds held by Government Development Bank for Puerto Rico (GDB) related to the establishment of a State Infrastructure Bank account, which is dedicated solely to providing loans or other forms of financial assistance consistent with the National Highway System Designation Act of 1995. The SIB was created on June 12, 1998 pursuant to a Cooperative Agreement among the Federal Highway Administration (FHWA) and the Federal Transit Administration of the United States Department of Transportation (FTA), and DTPW. Under the Agreement, DTPW established the SIB and designated the Authority as custodian and GDB as trustee of the SIB funds. The SIB is funded by a matching share agreement whereby on or before the date on which the Authority receives a Federal payment, the Authority must deposit an amount equaling at least 25 percent of such payment. These time deposits are held in the Authority's name.

Cash in banks is covered by federal depository insurance or collateral. The Authority is authorized to deposit funds only in institutions approved by the Department of the Treasury and such deposits should be maintained in separate accounts in the name of the Authority.

Resolutions 68-18 and 98-06 (the Bond Resolutions) require that moneys in the debt service funds be held by the Fiscal Agent (JP Morgan Chase Bank) in trust and applied as provided in the Bond Resolutions. The law governing the Authority does not limit the type of securities in which the Authority may invest. However, funds restricted for debt service must be invested only in direct obligations of the United States government, or obligations unconditionally guaranteed by the United States government, and/or interest bearing time deposits, or other similar arrangements, as provided by the Bond Resolutions. Accordingly, as permitted by the Bond Resolutions, cash and investments with Fiscal Agent restricted for debt service amounting to \$525,131,335 and \$554,112,362 at June 30, 2003 and 2002, respectively, consist of notes from the U.S. Government and Agencies. As per the matching share agreement with FHWA, the SIB reserve consists of \$15,010,735 of principal and \$3,744,549 of interest, which are included as restricted cash and investments with trustee and cash and cash equivalents, respectively at June 30, 2003. These investments are held in the Authority's name.

Investments restricted for capital projects may be made in Investment Obligations, as defined in the Bond Resolutions. Investment Obligations include time deposits of any bank, which are either issued by a bank with combined capital and surplus of at least \$50 million, or collateralized by securities in direct obligations of the United States Government or guaranteed by the United States Government. Accordingly, as permitted by the Bond Resolutions, investments restricted for capital projects, amounting to \$26,264,302 and \$49,257,377 at June 30, 2003 and 2002, respectively, consist of certain U.S. Government Securities maintained pursuant to an investment agreement with Bayerische Landesbank, New York Branch, which expires on April 29, 2005. These investments are held in the Authority's name.

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

2. Cash, Cash Equivalents and Investments (continued)

A summary of changes in the investments restricted for capital projects related to all construction projects except for the SIB funds at June 30, 2003 and 2002 are as follows:

	<u>2003</u>	<u>2002</u>
Balance as of June 30, 2002	\$264,347,139	\$ -
Interest revenue	2,381,414	-
Bonds issuance	332,475,795	318,552,901
Construction expenditures	<u>(387,953,412)</u>	<u>(54,205,762)</u>
Balance as of June 30, 2003	<u>\$211,250,936</u>	<u>\$264,347,139</u>

A summary of changes in the investments restricted for capital projects related to the SIB funds at June 30, 2003 and 2002 are as follows:

	<u>2003</u>	<u>2002</u>
Balance as of June 30, 2002	\$49,257,377	\$53,525,970
Interest revenue	1,280,359	3,544,991
Construction expenditures	<u>(24,273,434)</u>	<u>(7,813,584)</u>
Balance as of June 30, 2003	<u>\$26,264,302</u>	<u>\$49,257,377</u>

A summary of changes in the investments recorded which are restricted for debt service related to Resolution 68-18 at June 30, 2003 and 2002 are as follows:

	<u>2003</u>	<u>2002</u>
Balance of reserve account as of July 1	\$176,432,000	\$164,043,000
Interest revenue	9,716,979	7,310,244
Transferred to Construction Fund	(28,183,146)	(7,310,244)
Transferred to Sinking Fund (for debt service)	<u>-</u>	<u>12,389,000</u>
Balance of reserve account as of June 30	<u>\$157,965,833</u>	<u>\$176,432,000</u>

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

2. Cash, Cash Equivalents and Investments (continued)

A summary of changes in the investments recorded which are restricted for debt service related to Resolution 98-06 (Senior Transportation Revenue Bonds) at June 30, 2003 and 2002 are as follows:

	2003	2002
Balance of reserve account as of July 1	\$165,452,000	\$104,130,000
Interest revenue	8,984,490	8,214,696
Transferred Bond Issuance to Construction Fund	(10,345,293)	(8,480,696)
	36,770,506	61,588,000
Balance of reserve account as of June 30	\$200,861,703	\$165,452,000

A summary of changes in the investments recorded which are restricted for debt service related to Resolution 98-06 (Subordinated Transportation Revenue Bonds) at June 30, 2003 and 2002 are as follows:

	2003	2002
Balance of reserve account as of July 1	\$ -	\$ -
Interest revenue	209,888	-
Transferred to Bond Issuance Construction Fund	(209,888)	-
Bond issuance	26,512,201	-
Balance of reserve account as of June 30	\$26,512,201	\$ -

A summary of changes in the investments recorded which are restricted for debt service related to the SIB funds at June 30, 2003 and 2002 are as follows:

	2003		2002	
	Reserve Account	Interest	Reserve Account	Interest
Balance as of July 1	\$15,010,735	\$2,947,555	\$15,010,735	\$2,112,455
Interest revenue	-	796,994	-	835,100
Balance as of June 30	\$15,010,735	\$3,744,549	\$15,010,735	\$2,947,555

Puerto Rico Highways and Transportation Authority

Notes to Financial Statements (continued)

2. Cash, Cash Equivalents and Investments (continued)

Resolution 68-18 established the Bond Service Account, the Redemption Account, the Reserve Account. All revenues (except the proceeds of the petroleum products tax) under Resolution 68-18 (other than income from investments of moneys in the Construction Fund) are deposited in these accounts (see Note 4). The monies held in these funds are presented as restricted cash and cash equivalents in the balance sheets.

At June 30, 2003, the carrying amount and bank balance of cash deposits held by the Fiscal Agent under Resolution 68-18 are as follows (in thousands):

	2003		2002	
	Carrying Amount	Bank Balance	Carrying Amount	Bank Balance
Restricted:				
Held by the Fiscal Agent	\$49,634	\$49,634	\$88,289	\$88,289

Resolution 98-06 established the Revenue Fund. All revenues under Resolution 98-06 (other than income from investment of moneys in the Construction Fund) are deposited in the Revenue Fund. The monies held in this fund are presented as unrestricted cash and cash equivalents in the balance sheets.

At June 30, 2003, the carrying amount and bank balance of cash deposits held by the Fiscal Agent under Resolution 98-06 are as follows (in thousands):

	2003		2002	
	Carrying Amount	Bank Balance	Carrying Amount	Bank Balance
Restricted:				
Held by the Fiscal Agent	\$104,550	\$104,550	\$ 70,062	\$ 70,062
Held by the Authority	91,386	98,158	98,791	148,703
	\$195,936	\$202,708	\$168,853	\$218,765

At June 30, 2003 and 2002, certain investments and cash deposits of the Authority were restricted to comply with long-term principal and interest debt service requirements (sinking funds). These restricted assets are held by the Fiscal Agent under the Bond Resolutions (see Note 4) in the following funds and accounts:

1968 Reserve Account - Reserve for payment of principal of and interest on Highway Revenue Bonds in the event moneys in Bond Service Account or Redemption Account under Resolution 68-18 are insufficient for such purpose.

Puerto Rico Highways and Transportation Authority

Notes to Financial Statements (continued)

2. Cash, Cash Equivalents and Investments (continued)

1968 Bond Service Account and Redemption Account (Sinking Fund under Resolution 68-18) - Current year requirements for principal of and interest on Highway Revenue Bonds. As of June 30, 2003, cash and cash equivalents in this account amounted to \$45.5 million (2002 - \$121.0 million).

1998 Senior Reserve Account - Reserve for payment of principal of and interest on Senior Transportation Revenue Bonds in the event moneys in Senior Bond Service Account or Senior Bond Redemption Account under Resolution 98-06 are insufficient for such purpose.

1998 Senior Bond Service Account and Senior Bond Redemption Account (Senior Bond Sinking Fund under Resolution 98-06) - Current year requirements for principal of and interest on Senior Transportation Revenue Bonds. As of June 30, 2003, cash and cash equivalents in this account amounted to \$69.5 million (2002 - \$68.9 million).

1998 Subordinated Reserve Fund - Reserve for payment of principal of and interest on Subordinated Transportation Revenue Bonds in the event moneys in Subordinated Bond Service Account or Subordinated Bond Redemption Account under Resolution 98-06 are insufficient for such purpose.

1998 Subordinated Bond Service Account and Subordinated Bond Redemption Account (Subordinated Bond Sinking Fund under Resolution 98-06) - Current year requirements for principal of and interest on Subordinated Transportation Revenue Bonds. As of June 30, 2003, cash and cash equivalents in this account amounted to \$4.8 million (2002 - \$1.3 million).

At June 30, investments held by the Fiscal Agent consist of (in thousands):

	2003	2002
1968 Reserve Account	\$159,020	\$180,237
1968 Sinking Fund	45,518	121,011
1998 Senior Reserve Account	203,676	168,251
1998 Senior Sinking Fund	69,491	68,855
1998 Subordinated Reserve Fund	41,527	15,011
1998 Subordinated Sinking Fund	4,761	1,282
	\$523,993	\$554,647

Investments held by Fiscal Agent under the Bond Resolutions are invested exclusively in securities of the U.S. Government and its agencies.

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

2. Cash, Cash Equivalents and Investments (continued)

The Authority also has cash and investment securities held by the Fiscal Agent restricted for the following purposes:

1998 Construction Fund - Special fund created by the Resolution 98-06. The proceeds of any Transportation Revenue Bonds issued for the purpose of paying the cost of acquiring or constructing transportation facilities, together with the money received from any other source for such purpose, except proceeds which are (i) applied to the repayment of advances, (ii) deposited in the 1998 Senior Bond Reserve Account or 1998 Subordinated Bond Reserve Fund, (iii) deposited in the 1998 Senior or Subordinated Bond Service Account as capitalized interest or (iv) used for the payment of financing expenses, shall be deposited in the 1998 Construction Fund and held by the Fiscal Agent in trust.

At June 30, the 1998 Construction Fund consisted of investment in U.S. Government obligations of approximately \$211,251,000 and \$264,347,000 at June 30, 2003 and 2002, respectively.

3. Capital Assets

The following schedule summarizes property and equipment held by the Authority as of June 30, 2003:

	Ending Balance at June 30, 2002	Additions	Retirements	Reclassification	Ending Balance at June 30, 2003
Land	\$ 1,710,911,521	\$ -	\$ -	\$ 2,099,550	\$ 1,713,011,071
Construction in progress	4,615,205,178	748,040,443	-	(80,934,923)	5,282,310,698
Roads	8,340,286,911	-	-	50,191,346	8,390,478,257
Bridges	2,601,828,410	-	(1,562,439)	28,644,027	2,628,909,998
Property and equipment	80,218,859	5,558,509	(377,860)	-	85,399,508
	<u>17,348,450,879</u>	<u>753,598,952</u>	<u>(1,940,299)</u>	<u>-</u>	<u>18,100,109,532</u>
Accumulated depreciation	(5,518,170,536)	(263,635,888)	1,047,375	-	(5,780,759,049)
Total	<u>\$11,830,280,343</u>	<u>\$ 489,963,064</u>	<u>\$ (892,924)</u>	<u>\$ -</u>	<u>\$12,319,350,483</u>

In 1994, the Authority commenced the planning and design and in 1996 the construction of a rail mass transportation system known as Tren Urbano. The initial phase of Tren Urbano consisted of approximately 17 km of track extending from Bayamón to Santurce. As of June 30, 2003, the Authority has capitalized costs amounting to approximately \$2.1 billion related to this project. Total contributions from the US Federal government and the Authority's funds for this project amount to approximately \$608,159,000 and \$1,412,981,000, respectively. Tren Urbano is expected to be operational during fiscal year 2004.

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

4. Bonds Payable

The Bond Resolutions authorize the issuance of revenue bonds to obtain funds to pay the construction and related costs of transportation facilities. Bonds outstanding under the Bond Resolutions at June 30, 2003 were as follows:

	Issue Date	Original Amount	Maturing July 1	Interest Rate	Outstanding Principal Amount	Unamortized (Discount) Premium	Outstanding Balance
Serial bonds:							
FMHA-C	January 27, 1981	\$ 4,510,000	1983-2020	5.00	\$ 3,120,000	\$ -	\$ 3,120,000
V	June 4, 1992	9,960,000	2000-2005	3.50-5.88	940,000	(13)	939,987
W	July 15, 1993	24,700,000	2009	MCS	24,700,000	(162,464)	24,537,536
X	July 15, 1993	228,695,000	1994-2022	2.85-5.10	65,260,000	(749,601)	64,510,399
Y	April 9, 1996	213,190,000	1997-2022	5.00-6.25	102,165,000	(1,324,620)	100,840,380
Z	April 9, 1996	142,440,000	1996-2016	4.00-6.25	128,545,000	(1,756,932)	126,788,068
AA	April 29, 2003	436,135,000	2005-2023	4.65-6.50	436,135,000	38,098,342	474,233,342
*A	February 15, 1998	271,730,000	1999-2014	2.25-5.50	193,110,000	(2,219,711)	190,890,289
*B	May 15, 2000	174,180,000	2001-2027	5.50-5.75	98,680,000	(1,136,339)	97,543,661
*C	May 15, 2000	14,880,000	2029	6.00	14,880,000	(304,526)	14,575,474
*E	January 1, 2003	284,405,000	2011-2024	5.00-5.75	284,405,000	23,855,237	308,260,237
*F	January 1, 2003	118,615,000	2003-2011	5.00-5.25	118,615,000	4,777,861	123,392,861
*G	April 29, 2003	152,175,000	2011-2023	3.50-5.25	152,175,000	172,142	152,347,142
*H	April 29, 2003	12,630,000	2006-2023	2.25-5.00	12,630,000	200,268	12,830,268
*Subordinated Bonds (1998)	July 15, 1998	16,990,000	2008-2014	2.30-5.75	16,990,000	(139,962)	16,850,038
*Subordinated Bonds (2003)	April 29, 2003	214,560,000	2006-2023	3.90-5.50	214,560,000	9,222,571	223,782,571
Total serial bonds		<u>\$2,319,795,000</u>			<u>\$1,866,910,000</u>	<u>\$ 68,532,253</u>	<u>1,935,442,152</u>
Term bonds:							
W	July 15, 1993	\$ 292,090,000	2013-2020	5.25-5.50	\$ 134,435,000	\$ (1,220,4	133,214,554
X	July 15, 1993	288,565,000	2013-2021	5.25-5.50	79,435,000	(735,7	78,699,255
Y	April 9, 1996	677,045,000	2011-2036	5.00	555,265,000	(14,256,4	541,008,534
Z	April 9, 1996	42,600,000	2018	6.25	42,600,000	(1,041,4	41,558,594
AA	April 29, 2003	281,230,000	2026-2035	5.00	281,230,000	25,023,7	306,253,746
*A	February 15, 1998	818,045,000	2028-2038	4.75-5.00	800,260,000	(14,690,797	785,569,203
*B	May 15, 2000	386,625,000	2026-2039	5.88-6.50	122,665,000	(2,419,5	120,245,462
*D	January 1, 2003	700,855,000	2027-2041	5.00-5.75	700,855,000	(6,828,5	694,026,449
*G	April 29, 2003	411,475,000	2028-2042	5.00	411,475,000	468,9	411,943,947
*H	April 29, 2003	59,405,000	2028-2035	3.50-5.00	59,405,000	998,9	60,403,991
*Subordinated Bonds (1998)	July 15, 1998	58,060,000	2018-2028	5.00	58,060,000	(626,8	57,433,133
*Subordinated Bonds (2003)	April 29, 2003	105,985,000	2028	5.00	105,985,000	4,598,2	110,583,216
Total term bonds		<u>\$4,121,980,000</u>			<u>\$3,351,670,000</u>	<u>\$(10,729,9</u>	<u>3,340,940,084</u>
Less serial bonds payable on July 1, 2003							<u>10,435,000</u>
Bonds payable thereafter							<u>5,265,947,236</u>
Capital appreciation bonds	Feb. 15, 1998	<u>\$ 39,868,740</u>	2015-2018	4.95-5.075			<u>51,814,635</u>
Total bonds payable after July 1, 2003							<u>5,317,761,871</u>
Less net loss on advance refunding							<u>13,802,520</u>
Total bonds payable, net of unamortized premium and net loss on advance refunding							<u>\$5,303,959,351</u>

* Issued under Resolution 98-06. All other bonds issued under Resolution 68-18.

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

4. Bonds Payable (continued)

On April 29, 2003, the Authority issued Highway Revenue Refunding Bonds (Series AA) (the Series AA Bonds), Transportation Revenue Bonds (Series G) (the Series G Bonds), Transportation Revenue Refunding Bonds (Series H) (the Series H Bonds), and Subordinated Transportation Revenue Bonds (Series 2003) (the 2003 Subordinated Bonds). The proceeds of the Series AA Bonds were used to refinance a portion of the Authority's outstanding Highway Revenue Bonds (Series W, Series X, and Series Y) with an outstanding aggregate face amount of \$757,100,000, and pay costs of issuance of the Series AA Bonds. The proceeds of the Series G Bonds were used to finance the cost of various highway projects included in the Authority's current Construction Improvement Program and a portion of the costs of Tren Urbano, make a deposit to the 1998 Senior Bond Reserve Account and pay costs of issuance of the Series G Bonds. The proceeds of the Series H Bonds were used to refund a portion of the Authority's outstanding Transportation Revenue Bonds (Series A and Series B) with an outstanding aggregate face amount of \$45,795,000, and pay costs of issuance of the Series H Bonds. The proceeds of the 2003 Subordinated Bonds were used to repay a loan from the federal government incurred to finance a portion of the costs of Tren Urbano, make a deposit to the 2003 Subordinated Bonds Reserve Account and pay costs of issuance of the 2003 Subordinated Bonds.

A summary of the Series AA Bonds, Series G Bonds, Series H Bonds, and Series 2003 Subordinated Bonds issued during fiscal year 2003 follows:

Serial Bonds	\$ 815,500,000
Term Bonds	<u>858,095,000</u>
Total	<u><u>\$1,673,595,000</u></u>

The Serial Bonds (except for the Mandatory Tender Bonds referred to below) bear fixed interest-rates ranging from 2.25% through of 5.50% and mature from 2005 to 2023. The Term Bonds (except for the Mandatory Tender Bonds referred to below) bear fixed interest rates ranging from 3.50% through 5.00% and mature from 2026 to 2035. Interest on the Serial Bonds and Term Bonds (except for the Mandatory Tender Bonds referred to below) is payable on each January 1 and July 1. The Mandatory Tender Bonds bear interest at a fixed rate of 5% through July 1, 2010 after which the interest rate will float.

Puerto Rico Highways and Transportation Authority

Notes to Financial Statements (continued)

4. Bonds Payable (continued)

A summary of the net proceeds of the Series AA Bonds, Series G Bonds, Series H Bonds, and Series 2003 Bonds and their application follows:

	Series AA	Series G	Series H	Series 2003
Principal amount	\$717,365,000	\$563,650,000	\$72,035,000	\$320,545,000
Less:				
Original issue premium, net	64,261,351	645,491	1,208,340	14,001,426
	781,626,351	564,295,491	73,243,340	334,546,426
Plus:				
Amounts from refunded bonds accounts	51,619,898	-	14,659,776	4,269,616
Net proceeds	\$833,246,249	\$564,295,491	\$87,903,116	\$338,816,042
Application of net proceeds:				
Deposit to construction fund	\$ -	\$522,475,795	\$ -	\$ -
Deposit to debt service reserve	10,884,473	32,603,720	4,166,786	26,512,201
Refunding escrow deposits	799,648,900	-	80,912,992	305,614,192
Costs of issuance	903,185	703,411	94,179	401,662
Underwriters' discount	4,068,066	3,638,325	464,981	2,039,775
Bond insurance premium	17,741,625	4,874,240	2,264,178	4,248,212
Total	\$833,246,249	\$564,295,491	\$87,903,116	\$338,816,042

The Series AA Bonds maturing 2026 and 2035 and a portion of the Series H Bonds maturing in 2035 are subject to mandatory tender (Mandatory Tender Bonds) for purchase on July 1, 2010, subject to a successful remarketing. The purchase price on July 1, 2010 is equal to the principal amount of the Mandatory Tender Bonds, plus accrued interest, if any, to the date of purchase. The Mandatory Tender Bonds may be redeemed on or after July 1, 2010 at the option of the Authority from any available moneys (other than moneys deposited in the 1968 Sinking Fund or the 1998 Senior Bond Sinking Fund, as the case may be, in respect of an Amortization Requirement) on any date, either in whole or in part, at a redemption price equal to the principal amount of the bonds to be redeemed plus accrued interest to the redemption date, without premium.

The Series AA Bonds, except for the Series AA Mandatory Tender Bonds, maturing on July 1, 2028 and 2035 may be redeemed on any date on or after July 1, 2013 at the option of the Authority, either in whole or in part, from any available moneys (other than moneys deposited in the 1968 Sinking Fund in respect of an Amortization Requirement) at a redemption price equal to the principal amount of the bonds to be redeemed plus accrued interest to the redemption date, without premium.

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

4. Bonds Payable (continued)

The Series G Bonds and Series H Bonds, except for the Series H Mandatory Tender Bonds, maturing after July 1, 2013 may be redeemed on any date on or after July 1, 2013 at the option of the Authority, either in whole or in part, from any available moneys (other than moneys deposited in the 1998 Senior Bonds Sinking Fund in respect of an Amortization Requirement) at a redemption price equal to the principal amount of the bonds to be redeemed plus accrued interest to the redemption date, without premium.

The 2003 Subordinated Bonds maturing after July 1, 2013 may be redeemed on any date on or after July 1, 2013 at the option of the Authority, either in whole or in part, from any available moneys (other than moneys deposited in the 1998 Subordinated Bonds Sinking Fund in respect of an Amortization Requirement) at a redemption price equal to the principal amount of the bonds to be redeemed plus accrued interest to the redemption date, without premium.

During fiscal year 2002, the Authority issued the Transportation Revenue Bonds (Series D) (the Series D Bonds), Transportation Revenue Refunding Bonds (Series E) (the Series E Bonds), and Transportation Revenue Refunding Bonds (Series F) (the Series F Bonds). The proceeds of the Series D Bonds were used to finance a portion of the costs of Tren Urbano and various highway projects included in the Authority's current Construction Improvement Program, make a deposit to the 1998 Senior Bond Reserve Account, and pay costs of issuance of the Series D Bonds. The proceeds of the Series E Bonds were used to refund a portion of the Authority's Transportation Revenue Bonds (Series B) with an outstanding aggregate face amount of \$286,765,000 and pay costs of issuance of the Series E Bonds. The proceeds of the Series F Bonds were used to refund a portion of the Authority's Highway Revenue Bonds (Series V) with an outstanding aggregate face amount of \$125,640,000 and pay costs of issuance of the Series F Bonds.

A summary of the Series D Bonds, Series E Bonds, and Series F Bonds issued during fiscal year 2002 follows:

Serial Bonds:	
Various Fixed Rate	\$ 403,020,000
Term Bonds:	
Various Fixed Rate	<u>700,855,000</u>
Total	<u><u>\$1,103,875,000</u></u>

The Term Bonds bear fixed interest rates ranging from 5% to 5.75% and mature in 2027 and 2041. The Serial Bonds bear fixed interest rates ranging from 5.00% to 5.75% and mature from 2003 to 2024. Interest on the Term Bonds and Serial Bonds is payable on each January 1 and July 1.

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

4. Bonds Payable (continued)

A summary of the net proceeds of the Series D Bonds, Series E Bonds, and Series F Bonds and their application follows:

	<u>Series D</u>	<u>Series E</u>	<u>Series F</u>
Principal amount of 2003 Bonds	\$700,855,000	\$284,405,000	\$118,615,000
Less:			
Original issue premium (discount)	(7,123,895)	26,470,787	6,642,165
Plus:			
Amounts from refunded bonds accounts	-	1,423,885	5,937,820
	<u>\$693,731,105</u>	<u>\$312,299,672</u>	<u>\$131,194,985</u>
Net proceeds			
	<u>\$693,731,105</u>	<u>\$312,299,672</u>	<u>\$131,194,985</u>
	<u>Series D</u>	<u>Series E</u>	<u>Series F</u>
Application of net proceeds:			
GDB line of credit repayment	\$300,000,000	\$ -	\$ -
Deposit to construction fund	318,552,901	-	-
Cash deposit to escrow account	-	9,747	251
Cost of escrow securities	-	303,815,597	130,377,117
Deposit to debt service reserve fund	60,336,249	-	-
Costs of issuance	1,216,527	327,601	134,735
Underwriters' discount	5,012,288	1,681,401	682,882
Bond insurance premium	8,613,140	6,465,326	-
	<u>\$693,731,105</u>	<u>\$312,299,672</u>	<u>\$131,194,985</u>
Total			
	<u>\$693,731,105</u>	<u>\$312,299,672</u>	<u>\$131,194,985</u>

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

4. Bonds Payable (continued)

Changes in serial and term bonds during fiscal year 2003, were as follows:

	Outstanding Beginning- of-Year (at face value)	Issued	Refunded	Redeemed	Outstanding End-of-Year (at face value)
Serial	\$1,432,945,000	\$ 874,905,000	\$320,930,000	\$81,925,000	\$1,904,995,000
Term	3,039,460,000	798,690,000	524,565,000	-	3,313,585,000
CABs	49,310,317	2,504,318	-	-	51,814,635
	<u>\$4,521,715,317</u>	<u>\$1,676,099,317</u>	<u>\$845,495,000</u>	<u>\$81,925,000</u>	<u>5,270,394,635</u>
					57,802,236
					13,802,520
					<u>5,314,394,351</u>
					<u>10,435,000</u>
					<u>\$5,303,959,351</u>

The outstanding revenue bonds as of June 30, 2003 require future payments of principal and interest as follows:

<u>Year ending June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
Due on July 1, 2003	\$ 10,435,000	\$ 117,448,099	\$ 127,883,099
2004	29,135,000	272,224,090	301,359,090
2005	83,970,000	270,511,356	354,481,356
2006	88,045,000	266,154,666	354,199,666
2007	97,035,000	261,800,681	358,835,681
2008	103,775,000	256,952,926	360,727,926
Thereafter	<u>4,857,999,635</u>	<u>4,279,339,163</u>	<u>9,137,338,798</u>
	<u>\$5,270,394,635</u>	<u>\$5,724,430,981</u>	<u>\$10,994,825,616</u>

Puerto Rico Highways and Transportation Authority

Notes to Financial Statements (continued)

4. Bonds Payable (continued)

The bonds are secured by a pledge of the gross receipts of the gasoline excise taxes and one half of the diesel oil excise taxes, a maximum of \$11 million monthly (but not more than \$120 million annually) derived from excise taxes over crude oil and its derivatives, \$15 per vehicle per year from certain motor vehicle license fees, the proceeds of any other taxes, fees or charges which the Legislature of Puerto Rico may allocate to the Authority in the future and which the Authority may pledge, proceeds of any tolls or other charges which the Authority may impose for the use of any of its traffic facilities and certain investment earnings. The proceeds of the gasoline tax, the gas oil and diesel oil tax, the crude oil tax and the motor vehicle license fees allocated to the Authority are available taxes and revenues under the Constitution of the Commonwealth of Puerto Rico. Accordingly, if needed, they are subject to being applied first to the payment of debt service on the public debt of the Commonwealth, but such taxes and license fees are to be used for such payments only if and to the extent that all other available revenues of the Commonwealth under the Constitution are insufficient for such purpose. The Commonwealth has never applied these revenues for such payments.

The Bond Resolutions further provide that receipts of pledged revenues (other than investment earnings) be deposited with the Fiscal Agent to the credit of the following accounts in the following order:

Resolution 68-18:

- A. To the Bond Service Account in an amount equal to 1/6 of the amount of interest payable on all bonds on the next succeeding interest payment date and an amount equal to 1/12 of the next maturing installment of any serial bonds (in the case of variable rate bonds, the actual interest on such bonds is deposited monthly with the Fiscal Agent).
- B. To the Redemption Account in an amount equal to 1/12 of the amortization requirements (as defined in Resolution 68-18) for such fiscal year for the term bonds then outstanding plus an amount equal to 1/12 of the premium, if any, which would be payable on the first redemption date in the following fiscal year on a like principal amount of bonds if such principal amount of bonds should be redeemed prior to their maturity from moneys in the applicable Sinking Fund.
- C. To the Reserve Account in an amount equal to the lesser of the maximum principal and interest requirements (as defined in Resolution 68-18) for any fiscal year on all outstanding bonds and 10% of the original principal amount of each series of bonds outstanding (any increase in the applicable reserve requirement on account of bonds issued for construction purposes may be funded from revenues over five years. Excess funds in the Reserve Account can be transferred to the Construction Fund, the Bond Service Account or the Redemption Account, as determined from time to time by the Authority).

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

4. Bonds Payable (continued)

Resolution 98-06:

- D. Virtually identical monthly deposits of pledged revenues to those specified in the paragraphs A through C above are made into the Senior Bond Service Account, the Senior Bond Redemption Account and the Senior Bond Reserve Account in respect of the Senior Transportation Revenue Bonds. After making the required deposits specified in the preceding sentence, remaining pledged revenues shall be deposited to the Subordinated Bond Service Account in an amount equal to 1/6 of the amount of interest payable on all subordinated bonds on the next succeeding interest payment date and an amount equal to 1/12 of the next maturing installment of any serial subordinated bonds.
- E. To the Subordinated Bond Redemption Account in an amount equal to 1/12 of the amortization requirements (as defined in Resolution 98-06) for such fiscal year for the subordinated term bonds then outstanding plus an amount equal to 1/12 of the premium, if any, which would be payable on the first redemption date in the following fiscal year on a like principal amount of such subordinated bonds if such principal amount of bonds should be redeemed prior to their maturity from moneys in the Subordinated Sinking Fund.
- F. Funds remaining after making the deposits described in paragraphs D. and E. above, shall be deposited to each applicable account in the Subordinated Bond Reserve Fund in an amount, if any, needed to restore the respective account balances to the respective deposit requirements corresponding to each such account established by the Authority; provided, that notwithstanding the above, in the event that any Subordinated Reserve requirement shall have increased on account of the issuance of additional series of subordinated bonds issued for construction purposes, the Authority may provide for equal annual deposits and will ensure that the applicable subordinated reserve requirement is met not earlier than the end of a five year period following the issuance of such series of subordinated bonds.
- G. Any revenues remaining after making the deposits referred to above shall be deposited in the Construction Fund under Resolution 98-06 for use by the Authority for any of its authorized purposes.

Under Resolution 68-18 the requirements specified in paragraphs A., B. and C. above are cumulative. Under Resolution 98-06 the requirements specified in paragraphs D., E. and F. above are cumulative.

If funds in the Reserve Account are used to cover any deficiency in the Bond Service Account or the Redemption Account established under the applicable Bond Resolution, the Excise Act provides that the Reserve Account shall be reimbursed, subject to the provisions of the Constitution of the Commonwealth relating to payment of Commonwealth debt, from the first proceeds received by the Commonwealth in the next fiscal year or years derived from (i) any other taxes which may then be in effect on any other fuels or propellants which are used, among other purposes, to propel highway vehicles, and (ii) any remaining portion of the tax on gasoline and gas oil and diesel oil (and in the case of the Senior Bond Reserve Account and Subordinated Bond Reserve Fund under Resolution 98-06, the tax on crude oil and derivatives) then in effect.

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

4. Bonds Payable (continued)

The Authority further covenants that any other funds which it receives from the Commonwealth or any other source to make up any deficiencies in the amounts needed to pay the principal of and interest on any bonds issued under the provisions of the Bond Resolutions will be applied first to any Resolution 68-18 bonds, then to the Senior Transportation Revenue Bonds and Subordinated Transportation Revenue Bonds under Resolution 98-06.

Nothing in the Bond Resolutions is to be construed as preventing the Authority from financing any facilities authorized by the Act that created the Authority, as amended, through the issuance of bonds or other obligations, which are not secured under the provisions of the Bond Resolutions.

The Bond Resolutions permit the Authority (upon satisfaction of certain debt service coverage tests) to issue additional bonds for the purpose of providing funds for completing payment of the cost of any transportation facilities, including Tren Urbano, or for paying all or any part of the cost of any additional transportation facilities, including the payment of any outstanding notes of the Authority which were issued to temporarily finance the costs of the transportation facilities for which such bonds are to be issued, and for refunding at or prior to their maturity or maturities all or a portion of the outstanding Highway or Transportation Revenue Bonds.

The outstanding balances as of June 30, 2003 of the bond issues defeased by the Authority are as follows:

Series A	\$ 27,600,000
Series B	332,560,000
Series W	251,155,000
Series X	349,755,000
Series Y	<u>191,190,000</u>
 Total outstanding defeased Bond issues	 <u><u>\$1,152,260,000</u></u>

As of June 30, 2003 and 2002, the Statements of Net Assets reflect net deferred debits of \$13,802,520 and \$8,068,600, respectively as a component of debt resulting from accounting losses or gains from bonds defeased by the Authority. The Statements of Revenues, Expenses and Changes in Net Assets reflect the amortization of this deferral as a component of interest expense of approximately \$53,770,000 in 2003 and \$5,800,000 in 2002.

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

5. Credit Agreement

On August 4, 2000, the Authority entered into a loan agreement of \$300,000,000 with FTA pursuant to the Transportation Infrastructure Finance and Innovation Act, as amended. The proceeds of the loan were used to cancel the outstanding balance of a line of credit amounting to \$269,999,583 with GDB in connection with the Tren Urbano project. The loan has a fixed interest rate of 5.74%. Interest is payable each July 1 and January 1, beginning January 1, 2001, and principal is payable each July 1, beginning July 1, 2007. On April 29, 2003, the Authority paid the outstanding balance of the loan with the proceeds of the Series 2003 Subordinated Bonds (see Note 4).

6. Changes in Amounts Invested in Capital Assets, Net of Related Debt

The change in amounts invested in capital assets, net of related debt can be summarized as follows:

	2003	2002
Balance at the beginning of the year	\$7,169,108,191	\$7,442,222,069
Change in capital assets	489,070,140	322,203,847
Change in related debt	(587,975,215)	(595,317,725)
	\$7,070,203,116	\$7,169,108,191

7. Retirement Plan

The Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities (ERS) is a cost-sharing, multiple-employer, defined benefit pension plan sponsored by, and reported as a component unit of, the Commonwealth of Puerto Rico. All regular employees of the Authority under age 55 at the date of employment become members of the System as a condition of their employment.

ERS provides retirement, death and disability benefits pursuant to Act No. 447, approved on May 15, 1951, as amended, which became effective on January 1, 1952. Retirement benefits depend upon age at retirement and number of years of credited service. Benefits vest after ten years of plan participation.

Participants who have attained an age of at least fifty-five (55) years and have completed at least twenty-five (25) years of creditable service or members who have attained an age of at least fifty-eight (58) years and have completed at least ten (10) years of creditable service (or who have attained an age of at least sixty five (65) years and have completed at least 10 years of service if hired after April, 1990) are entitled to an annual benefit, payable monthly for life.

Puerto Rico Highways and Transportation Authority

Notes to Financial Statements (continued)

7. Retirement Plan (continued)

The annuity, for which a plan member is eligible, is limited to a minimum of \$200 per month and a maximum of 75% of the average compensation.

Participants who have completed at least thirty (30) years of creditable service are entitled to receive a Merit Annuity. Participants who have not attained fifty-five (55) years of age will receive 65% of such average compensation. Participants who have attained fifty-five (55) years of age will receive 75% of such average compensation. Disability retirement benefits are available to members for occupational and non-occupational disability. However, for non-occupational disability a member must have at least ten (10) years of creditable service.

No benefit is payable if the participant receives a refund of his accumulated contributions.

Commonwealth law requires employees hired on or before March 31, 1990 to contribute to the ERS 5.775 percent for the first \$550 of their monthly gross salary and 8.275 percent for their salary in excess of \$550. The contribution for employees hired after April 1, 1990 is 8.275 percent of their gross salary. The Authority is required to contribute 9.275 percent of the participants' gross salaries to the ERS. The contribution requirement for the years ended June 30, 2003 and 2002 were approximately \$8,890,000 and \$8,498,000, respectively, which consisted of approximately \$4,743,000 from the Authority and \$4,147,000 from its employees. The payroll for employees covered by ERS for the years ended June 30, 2003 and 2002, was approximately \$90,788,000 and \$47,030,000, respectively, and the Authority's total payroll cost was approximately \$54,953,000 and \$73,447,000, respectively. For the two preceding fiscal years the Authority contributed \$4,547,000 and \$4,330,000, respectively, which represented all required contributions.

On September 24, 1999 the law which created ERS was amended for the purpose of establishing a defined contribution plan know as System 2000.

System 2000 became effective on January 1, 2000. Authority employees participating in the defined-benefit plan system at December 31, 1999, had the option to either stay in the defined benefit plan or transfer to System 2000. Persons employed by the Authority on or after January 1, 2000 are only allowed to become members of System 2000.

System 2000 is a hybrid defined contribution plan, also known as a cash balance plan. Under this new plan, there will be a pool of plan assets, which will be invested by ERS, together with those of the defined-benefit plan. Benefits at retirement age will not be guaranteed. The annuity will be based on a formula which assumes that each year the participants' contributions (with a minimum of 8.275% of the participants' salary up to a maximum of 10%) will be invested as instructed by the participant in an account which will either: (1) earn a fixed rate based on the two-year Constant Maturity Treasury Notes; (2) earn a rate equal to 75% of the return of ERS's investment portfolio (net of management fees); or (3) earn a combination of both alternatives.

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

7. Retirement Plan (continued)

Participants receive periodic account statements similar to those of defined contribution plans showing their accrued balances. Disability pensions are not being granted under System 2000. The employers' contributions (9.275% of the employee's salary) will be used to fund the defined benefit plan instead of System 2000.

System 2000 will reduce the retirement age from 65 years to 60 for those employees who joined the current plan on or after April 1, 1990.

Additional information on the System is provided in its financial statements for the year ended June 30, 1998, a copy of which can be obtained from Mrs. Marisol Marchand, Administrator, Employees' Retirement System of the Government of Puerto Rico and its Instrumentalities, PO Box 42003 Minillas Station, Santurce, P.R. 00940.

The Authority has a labor union contract that provides all union employees who work for the Authority upon retirement with the following lump-sum bonus payable at the retirement date computed as follows:

<u>Years worked</u>	<u>Amount</u>
10-15 years	\$140 per year of service
16-20	\$170 per year of service
21-25	\$185 per year of service
26-30	\$195 per year of service

In addition, management employees have similar benefits under the same conditions granted to labor union personnel, as follows:

<u>Years worked</u>	<u>Amount</u>
10-15 years	\$150 per year of service
16-20	\$180 per year of service
21-25	\$200 per year of service
26-30	\$220 per year of service

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

8. Commitments and Contingent Liabilities

Construction

As of June 30, 2003 and 2002, the Authority had commitments for approximately \$886,770,000 and \$1,006,000,000, respectively, related to construction contracts.

Leases

The Authority has various noncancelable operating leases for office space with Puerto Rico Public Buildings Authority and other lessors, the latest of which expires in 2025. The rental expense for the years ended June 30, 2003 and 2002 were approximately \$730,000 and \$1,573,000, respectively. Future rental payments as of June 30, 2003 under these leases are as follows:

2004	\$ 971,400
2005	84,400
2006	84,400
2007	80,200
2008	80,200
Thereafter	<u>3,067,800</u>
Total future rental payments required	<u><u>\$4,368,400</u></u>

Litigation

The Authority is defendant or co-defendant in various lawsuits for alleged damages. Substantially all of these cases are in connection with construction projects, which are generally either fully or partially covered by insurance. The contractors are required, under the terms of the construction agreements, to carry adequate public liability insurance and to hold harmless the Authority from lawsuits brought on account of damages relating to the construction of the projects.

The Authority, based on legal advice, has recorded an adequate provision to cover probable losses on those claims not fully covered by insurance. In the opinion of legal counsel, any liability in excess of the insurance coverage and/or the recorded provision that may arise from such claims would not be significant to affect to the Authority's financial position or results of operations.

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

8. Commitments and Contingent Liabilities (continued)

Special Facility Revenue Bonds

On December 20, 1992, the Authority and Autopistas de Puerto Rico y Compañía S.E. (Autopistas) entered into a concession agreement (the Concession Agreement), amended in 1992, and again in 2003, for the design, construction, operation and maintenance of the Teodoro Moscoso Bridge (the Bridge), a toll bridge, which traverses the San Jose Lagoon between the municipalities of San Juan and Carolina. Autopistas designed and constructed the Bridge and commenced operating the Bridge on February 23, 1994. The initial term of this agreement is 35 years, expiring on April 3, 2027.

In March 1992, the Authority issued Special Facility Revenue Bonds, 1992 Series A, B and C amounting to approximately \$117 million for the purpose of facilitating the construction of the Bridge. The proceeds from the sale of the bonds were transferred by the Authority to Autopistas, the borrower, pursuant to a loan agreement (the Loan Agreement) by and between Autopistas and the Authority.

Under certain circumstances, the Concession Agreement may be terminated and the Authority is then obligated to assume all of the Autopistas's obligations to pay principal of and interest on the bonds, which pursuant to the Loan Agreement will be paid from the net revenues of the use and operation of the Bridge. The Authority does not currently expect the Concession Agreement to terminate. The outstanding bonds (including accrued interest) and the sinking fund balances at June 30, 2003 and 2002 amounted to approximately \$143,948,000 and \$3,875,000, and \$138,444,000 and \$4,326,000, respectively. See Note 4.

Metrobus

In connection with the responsibilities of the Authority for mass transportation systems, the Metrobus project was developed. The project consists of bus operations in part of the San Juan metropolitan area, which operations are conducted by a private company under an agreement, which expired on June 2003, but extended until September 2003.

The contract for the operation of the Metrobus Project provides for fixed payments to the operator. Operators' compensation is based on monthly payments amounting to one-twelfth of the total annual operating costs. Bus fares, which are retained by the operator, reduce such payments. In addition, the Operator has various incentive fees for meeting or exceeding various performance standards.

Puerto Rico Highways and Transportation Authority
Notes to Financial Statements (continued)

8. Commitments and Contingent Liabilities (continued)

Federal Assistance Programs

The Authority participates in a number of federal financial assistance programs. These programs are subject to audits in accordance with the provisions of OMB Circular A-133 "Audits of States, Local Governments, and Non-Profit Organizations" or to compliance audits by grantor agencies. The resolution of certain previously identified questioned costs has not occurred. The amount, if any, of expenditures which may be disallowed by the granting agencies cannot be determined at this time, although the Authority expects such amounts, if any, to be immaterial.

Tren Urbano Project Claims

As part of the Authority's Tren Urbano project, a number of contractors have presented claims related to the project. Claims, which are at various stages of analysis to reach a final resolution, amount to approximately \$79,000,000 and \$60,000,000 as of June 30, 2003 and 2002, respectively.

From these amounts, approximately \$12,000,000 and \$24,000,000 have been categorized as merited claims as of June 30, 2003 and 2002, respectively. These amounts were recorded as accounts payable for restricted assets. The effect of the resolution of these claims, if any, in future years would be to increase the amounts being capitalized for the Tren Urbano project and increase the accounts payable in the accompanying Statements of Net Assets.

9. Subsequent Event

Special Facility Revenue Bonds

On October 30, 2003, the Authority issued Special Facility Revenue Refunding Bonds, 2003 Series A amounting to approximately \$153 million for the purpose of refunding the Authority's Special Facility Revenue Bonds, 1992 Series A, B, and C, which were issued to fund the construction of the Bridge, and to pay the cost of issuance of the bonds. The proceeds from the sale of the bonds were transferred by the Authority to Autopistas, pursuant to a new loan agreement by and between Autopistas and the Authority.

Report of Independent Auditors on Compliance and Internal Control Over Financial Reporting in Accordance with Government Auditing Standards

Hon. Fernando Fagundo Fagundo, Secretary
Department of Transportation and Public Works
Commonwealth of Puerto Rico

We have audited the financial statements of Puerto Rico Highways and Transportation Authority (the Authority) as of and for the year ended June 30, 2003, and have issued our report thereon dated September 26, 2003. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Authority's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses. However, we noted other matters involving the internal control over financial reporting that we have reported to management of the Authority in a separate letter dated September 26, 2003.

This report is intended solely for the information and use of the Authority's management, the U.S. Department of Transportation and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Ernst & Young LLP

September 26, 2003

Stamp No. 1921017
affixed to
original of
this report.

Required Supplemental Information

Puerto Rico Highway and Transportation Authority

Combined Statement of Revenues, Expenditures
and Changes in Fund Balance

Budget and Actual - Budgetary Basis

Year ended June 30, 2003

	Budget (Cash Basis)	Actual (Cash Basis)	Variance Favorable (Unfavorable)
Revenues:			
Excise taxes and vehicle license fees	\$ 344,970,000	\$ 340,763,286	\$ (4,206,714)
Toll fares	135,620,000	135,351,684	(268,316)
Grants:			
Federal Government	245,178,000	150,552,328	(94,547,672)
Interest and other revenue	28,200,000	42,760,344	14,560,344
Total revenues	753,968,000	669,427,642	(84,540,358)
Other financing sources (uses):			
Bond issuance	343,206,000	1,753,711,608	1,410,505,608
Payment to refunded bonds	-	100,668,917	(100,668,917)
Proceeds from SIB bonds	23,037,000	-	(23,037,000)
Total revenues and other financings sources	1,120,211,000	2,523,808,167	1,403,597,167
Expenditures:			
Construction, equipment and administrative	542,495,000	593,541,317	(51,046,317)
Toll highways administration and Metrobus	67,319,000	111,330,833	(44,130,833)
Payment of bonds, including interest	117,842,000	1,265,344,644	(1,147,502,644)
Payment of TIFIA loan	249,168,000	300,000,000	(50,832,000)
Advances to Department of Transportation and Public Works	-	2,624,957	(2,624,957)
Transfers to proprietary fund	440,170,000	257,130,223	183,039,777
Other expenditures	1,250,000	1,241,079	8,921
Total expenditures	1,418,244,000	2,531,213,053	(1,112,969,053)
Excess (deficiency) of revenues and other financing sources over/under expenditures	(298,033,000)	(7,404,885)	\$ (290,628,115)
Funds carried forward from prior year	298,033,000	-	
Fund balance at beginning of year	-	1,427,356,728	
Fund balance at end of year	\$ -	\$1,419,951,843	

Adjustments necessary to convert the revenues and expenses and fund balances at end-of-year from GAAP basis to the budgetary basis are as follows (in thousands):

	<u>Revenues</u>	<u>Excess of Revenues over Expenses</u>
GAAP Basis	\$660,845,436	\$ (27,373,640)
Adjustment:		
Accounts receivable, accrued interest and other	4,180,022	4,180,022
Accounts payable and accrued liabilities	-	147,326,058
Increase in fair value of investments	4,402,184	4,402,184
Proceeds from bond issuance	-	1,753,711,608
Sales of investment	-	100,668,917
Construction costs capitalized on GAAP basis	-	(756,463,624)
Toll highway administration and maintenance	-	(112,571,910)
Payment on redemption of bonds	-	(1,253,461,372)
Depreciation	-	267,393,484
Transfer to proprietary fund	-	(135,216,611)
Per Combined Statements of Revenues, Expenditures and Changes in Fund Balances - Budget and Actual - Budgetary Basis	<u>\$669,427,642</u>	<u>\$ (7,404,884)</u>

NIXON PEABODY LLP

437 Madison Avenue
New York, New York 10022-7001
(212) 940-3000

April 20, 2004

Hon. Fernando E. Fagundo
Secretary of Transportation and Public Works
San Juan, Puerto Rico

Dear Sir:

We have acted as bond counsel in connection with the issuance by the Puerto Rico Highways and Transportation Authority (the "Authority") of \$139,875,000 Puerto Rico Highways and Transportation Authority Grant Anticipation Revenue Bonds (Series 2004) (the "Bonds"). The Bonds are issued pursuant to Act No. 74 of the Legislature of Puerto Rico, approved June 23, 1965, as amended (the "Act"), Resolution No. 04-18 adopted by the Authority on April 7, 2004, authorizing the issuance of grant anticipation revenue bonds (the "2004 Resolution") and a supplemental resolution of the Authority, authorizing the issuance of the Bonds (the "Supplemental Resolution" and together with the 2004 Resolution, the "Resolution").

The Bonds are dated, mature, are payable and bear interest in the manner and upon the terms set forth in the Resolution. The 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 Bonds.

We have examined the law and such certified proceedings and other papers as we deem necessary to render the following opinions.

In rendering the following opinions we have assumed the genuineness of all signatures, the authenticity of all documents tendered to us as originals and the conformity to original documents of all documents submitted to us as certified or photostatic copies. As to questions of fact material to our opinion, we have relied upon the certified proceedings and other certifications of public officials furnished to us without undertaking to verify the same by independent investigation.

Based upon the foregoing, we are of the opinion, under existing law, as follows:

1. The Act is valid.
2. The Authority has the right and power under the Act to adopt the Resolution, and the Resolution has been duly and lawfully adopted by the Authority, is in full force and effect

and is valid and binding. The Resolution creates the valid pledge of and lien on the Trust Estate (as defined in the Resolution), subject to the terms of the Resolution.

3. The Bonds are valid and binding special, limited obligations of the Authority payable solely from the Trust Estate and have been duly authorized and issued in accordance with the Act and the Resolution. The Bonds do not give rise to a pecuniary liability or a charge against the general credit of the Authority or the Commonwealth of Puerto Rico (the "Commonwealth") and are not (and shall not be deemed or construed to be or to create) a debt, liability or obligation of the Commonwealth or any political subdivision of the Commonwealth, nor a pledge of the faith and credit of the Commonwealth or any political subdivision of the Commonwealth, within the meaning of the Constitution or laws of the Commonwealth concerning or limiting the creation of indebtedness by the Commonwealth or any political subdivision of the Commonwealth. Neither the Commonwealth nor any political subdivision thereof shall be obligated to pay the principal of or interest on the Bonds, and the owners of the Bonds shall have no right to make any claim against the Commonwealth or any of its political subdivisions.

4. The proceedings authorizing the issuance of the Bonds have been validly and legally taken.

5. The Act and such proceedings show lawful authority of the issuance and sale of the Bonds.

6. The Internal Revenue Code of 1986, as amended (the "Code") sets forth certain requirements which must be met subsequent to the issuance and delivery of the 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 Bonds to be included in gross income for Federal income tax purposes retroactively to the date of issue of the Bonds. The Authority has covenanted in the Resolution to comply with each provision of the Code applicable to the Bonds necessary to maintain the exclusion from gross income of the interest on the Bonds pursuant to Section 103 of the Code. In addition, the Authority has made certain representations and certifications relating to the Bonds in its "Tax Certificate as to Arbitrage and the Provisions of Sections 103 and 141-150 of the Internal Revenue Code of 1986" of even date herewith.

Under existing law, assuming compliance with the tax covenants described herein and the accuracy of certain representations and certifications made by the Authority described above, interest on the Bonds is excluded from gross income for Federal income tax purposes under Section 103 of the Code. We are 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 Bonds is, however, included in the adjusted current earnings of certain corporations for purposes of computing the alternative minimum tax imposed on such corporations.

7. The interest on the Bonds is exempt from state, Commonwealth and local income taxation.

8. Bond Counsel is further of the opinion that the difference between the principal amount of the Bonds maturing on September 15 in each of the following years: 2008 and bearing interest at the rate of 2.25%, 2009 and bearing interest at the rate of 2.50%, 2010 and bearing interest at the rate of 2.90%, 2011 and bearing interest at the rate of 3.125%, 2012 and bearing interest at the rate of 3.375%, 2013 and bearing interest at the rate of 3.60%, 2015 and bearing interest at the rate of 3.80%, 2016 and bearing interest at the rate of 3.90%, 2017 and bearing interest at the rate of 4.00%, 2018 and bearing interest at the rate of 4.10%, 2020 and bearing interest at the rate of 4.25% and 2021 and bearing interest at the rate of 4.30% (collectively, 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 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.

Except as stated in paragraphs 6, 7 and 8 above, we express no opinion as to any other Federal or state, Commonwealth or local tax consequences of the ownership or disposition of the Bonds. Furthermore, we express no opinion as to any Federal, state, Commonwealth or local tax law consequences with respect to the Bonds, or the interest thereon, if any action is taken with respect to the Bonds or the proceeds thereof upon the advice or approval of other bond counsel.

It is to be understood that the rights of the holders of the Bonds and the enforceability thereof may be subject to bankruptcy, insolvency, reorganization, moratorium and other similar laws affecting creditors' rights heretofore or hereafter enacted to the extent constitutionally applicable and that their enforcement may also be subject to the exercise of judicial discretion in appropriate cases.

Very truly yours,

NIXON PEABODY LLP

437 Madison Avenue
New York, New York 10022-7001
(212) 940-3000

April 20, 2004

Hon. Fernando E. Fagundo
Secretary of Transportation and Public Works
San Juan, Puerto Rico

Dear Sir:

We have acted as bond counsel in connection with the issuance by the Puerto Rico Highways and Transportation Authority (the "Authority") of \$82,340,000 Puerto Rico Highways and Transportation Authority Transportation Revenue Refunding Bonds (Series I) (the "Bonds"). The Bonds are issued pursuant to Act No. 74 of the Legislature of Puerto Rico, approved June 23, 1965, as amended (the "Act") and Resolution No. 98-06 adopted by the Authority on February 26, 1998, as amended (the "1998 Resolution"), together with a resolution adopted on April 7, 2004, with respect to the Bonds (the "Series I Resolution" and together with the 1998 Resolution, the "Authorizing Resolution").

The Bonds are dated, mature, are payable and bear interest in the manner and upon the terms set forth in the Authorizing Resolution. The 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 Bonds.

We have examined (i) the Act, (ii) certified copies of the proceedings of the Authority, including Resolution No. 68-18, adopted on June 13, 1968, as amended (the "1968 Resolution"), (iii) the Puerto Rico Internal Revenue Code of 1994 (Subtitle B of Act No. 120 of the Legislature of Puerto Rico, approved October 31, 1994, as amended among other things by Act No. 34 of the Legislature of Puerto Rico, approved July 16, 1997, as amended), which allocated (A) the proceeds of the sixteen cents per gallon tax imposed on gasoline and four cents of the eight cents per gallon tax on gas oil and diesel oil (the "Allocated Gasoline Tax Proceeds") and (B) the proceeds (up to \$120 million per fiscal year) of the tax imposed on crude oil, unfinished oil and derivative products (the "Allocated Crude Oil Tax Proceeds") to the Authority for use for its corporate purposes, (iv) the Vehicle and Traffic Law of Puerto Rico, approved July 20, 1960, as amended, which allocated the proceeds of the fifteen dollar increase in the motor vehicle license fees for public and private service automobiles imposed by Act No. 9 of the Legislature of Puerto Rico, approved August 12, 1982 (the "Allocated Additional License Fees"), to the Authority for use for its corporate purposes and (v) Reorganization Plan No. 6 of 1971 (Act

No. 113 of the Legislature of Puerto Rico, approved June 21, 1968), which attached the Authority to the Department of Transportation and Public Works.

We have also examined the law and such certified proceedings and other papers as we deem necessary to render the following opinions.

In rendering the following opinions we have assumed the genuineness of all signatures, the authenticity of all documents tendered to us as originals and the conformity to original documents of all documents submitted to us as certified or photostatic copies. As to questions of fact material to our opinion, we have relied upon the certified proceedings and other certifications of public officials furnished to us without undertaking to verify the same by independent investigation.

Based upon the foregoing, we are of the opinion, under existing law, as follows:

1. The Act is valid.
2. The proceedings authorizing the issuance of the Bonds have been validly and legally taken.
3. The Act and such proceedings show lawful authority of the issuance and sale of the Bonds.
4. The Authority has heretofore issued various series of bonds under and in compliance with the provisions of the 1968 Resolution (the "Highway Revenue Bonds"). The 1968 Resolution provides for the issuance of additional Highway Revenue Bonds under the conditions and limitations therein set forth, and the Authority has covenanted in the 1998 Resolution to limit the issuance of such additional Highway Revenue Bonds.
5. The 1998 Resolution provides for the issuance of additional bonds on a parity with the Bonds under the conditions, limitations and restrictions therein set forth (the Bonds and such additional parity bonds being herein called the "Senior Transportation Bonds") for any lawful purpose of the Authority and for the purpose of refunding any bonds issued by the Authority under the 1998 Resolution and any other obligations of the Authority, including outstanding Highway Revenue Bonds. In addition, the 1998 Resolution provides for the issuance of bonds subordinate to the Senior Transportation Revenue Bonds as to their lien on the revenues and other moneys of the Authority, as described below, under the conditions, limitations and restrictions and for the purposes set forth therein (the Senior Transportation Revenue Bonds and such bonds subordinate thereto being herein collectively called the "Transportation Revenue Bonds").
6. The 1998 Resolution provides for the creation of a special fund designated "Puerto Rico Highways and Transportation Authority Transportation Revenue Fund" (the Revenue Fund"), and, subject to the limitations of the next two paragraphs for the deposit to the credit of said special fund of all moneys received by the Authority (i) from the Allocated Crude

Oil Tax Proceeds, (ii) from the Allocated Gasoline Tax Proceeds, (iii) from the Allocated Additional License Fees, (iv) from any tolls or other charges imposed by the Authority for the use of any Toll Facilities and (v) from the proceeds of any other taxes, fees or charges which the Legislature of Puerto Rico may allocate to the Authority and expressly authorizes the Authority to pledge to the payment of the principal of and interest on bonds or other obligations issued by the Authority and which are pledged by the Authority to the payment of the principal of and interest on Transportation Revenue Bonds issued under the provisions of the 1998 Resolution.

The Allocated Gasoline Tax Proceeds, the Allocated Crude Oil Tax Proceeds and the Allocated Additional License Fees, and any other taxes, fees or charges which the Legislature of Puerto Rico may allocate to the Authority, are subject to first being applied to the payment of interest and amortization of public debt in accordance with the provisions of, and to the extent provided by, Section 8 of Article VI of the Constitution of Puerto Rico if needed for such purpose.

The 1968 Resolution provides for the prior deposit to the credit of a special fund designated "Puerto Rico Highways and Transportation Authority Construction Fund" (herein called the "1968 Construction Fund") of the Allocated Gasoline Tax Revenues, the Allocated Additional License Fees and all Existing Toll Facilities Revenues (As such term is defined in the 1998 Resolution), after the required deposits of such moneys have been made to the credit of the Puerto Rico Highways and Transportation Authority Highway Revenue Bonds Interest and Sinking Fund. In the 1998 Resolution, the Authority has covenanted (i) to withdraw monthly from the 1968 Construction Fund and deposit to the credit of the Revenue Fund until the outstanding Highway Revenue Bonds have been paid or provision has been made for their payment and the repeal and cancellation of the 1968 Resolution, all unencumbered moneys held to the credit of the 1968 Construction Fund and (ii) except for the foregoing withdrawal and any encumbrances on the moneys in the 1968 Construction Fund existing on the date of adoption of and as provided in the 1998 Resolution, not further to encumber or otherwise withdraw or pledge any such available moneys in the 1968 Construction Fund.

7. The Bonds are valid and binding special obligations of the Authority payable solely from the special fund created by the 1998 Resolution and designated "Puerto Rico Highways and Transportation Authority Transportation Revenue Bonds Interest and Sinking Fund." The Authority has covenanted to deposit to the credit of said Interest and Sinking Fund a sufficient amount of the moneys held to the credit of the Revenue Fund, together with any other funds of the Commonwealth of Puerto Rico allocated to the Authority and available under the 1998 Resolution for the payment of principal of and interest on the Senior Transportation Revenue Bonds, to pay the principal of and interest on all Senior Transportation Revenue Bonds (including the Bonds) issued under the provisions of the 1998 Resolution as the same may become due and payable and to create and maintain a reserve therefore. Said Interest and Sinking Fund is pledged to and charged with the payment of the principal of the principal and the interest on all Senior Transportation Revenues Bonds (including the Bonds) issued by the Authority under the provisions of the 1998 Resolution.

8. The Bonds do not constitute a debt of the Commonwealth of Puerto Rico or of any of its municipalities or other political subdivisions, and neither the Commonwealth of Puerto Rico nor any such municipality or other political subdivision is liable thereon, and the Bonds are payable only out of the revenues and other moneys of or allocated to the Authority, to the extent provided in the 1998 Resolution.

9. The Internal Revenue Code of 1986, as amended (the "Code") sets forth certain requirements which must be met subsequent to the issuance and delivery of the 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 Bonds to be included in gross income for Federal income tax purposes retroactively to the date of issue of the Bonds. The Authority has covenanted in the Resolution to comply with each provision of the Code applicable to the Bonds necessary to maintain the exclusion from gross income of the interest on the Bonds pursuant to Section 103 of the Code. In addition, the Authority has made certain representations and certifications relating to the Bonds in its "Tax Certificate as to Arbitrage and the Provisions of Sections 103 and 141-150 of the Internal Revenue Code of 1986" of even date herewith.

Under existing law, assuming compliance with the tax covenants described herein and the accuracy of certain representations and certifications made by the Authority described above, interest on the Bonds is excluded from gross income for Federal income tax purposes under Section 103 of the Code. We are 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 Bonds is, however, included in the adjusted current earnings of certain corporations for purposes of computing the alternative minimum tax imposed on such corporations.

10. The interest on the Bonds is exempt from state, Commonwealth and local income taxation.

11. Bond Counsel is further of the opinion that the difference between the principal amount of the Bonds maturing on July 1, 2007 through July 1, 2021, inclusive (collectively, 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 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.

Hon. Fernando E. Fagundo
April 20, 2004
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Except as stated in paragraphs 9, 10 and 11 above, we express no opinion as to any other Federal or state, Commonwealth or local tax consequences of the ownership or disposition of the Bonds. Furthermore, we express no opinion as to any Federal, state, Commonwealth or local tax law consequences with respect to the Bonds, or the interest thereon, if any action is taken with respect to the Bonds or the proceeds thereof upon the advice or approval of other bond counsel.

It is to be understood that the rights of the holders of the Bonds and the enforceability thereof may be subject to bankruptcy, insolvency, reorganization, moratorium and other similar laws affecting creditors' rights heretofore or hereafter enacted to the extent constitutionally applicable and that their enforcement may also be subject to the exercise of judicial discretion in appropriate cases.

Very truly yours,

NIXON PEABODY LLP

437 Madison Avenue
New York, New York 10022-7001
(212) 940-3000

April 20, 2004

Hon. Fernando E. Fagundo
Secretary of Transportation and Public Works
San Juan, Puerto Rico

Dear Sir:

We have acted as bond counsel in connection with the issuance by the Puerto Rico Highways and Transportation Authority (the "Authority") of \$405,895,000 Puerto Rico Highways and Transportation Authority Transportation Revenue Bonds (Series J) (the "Bonds"). The Bonds are issued pursuant to Act No. 74 of the Legislature of Puerto Rico, approved June 23, 1965, as amended (the "Act") and Resolution No. 98-06 adopted by the Authority on February 26, 1998, as amended (the "1998 Resolution"), together with a resolution adopted on April 7, 2004, with respect to the Bonds (the "Series J Resolution" and together with the 1998 Resolution, the "Authorizing Resolution").

The Bonds are dated, mature, are payable and bear interest in the manner and upon the terms set forth in the Authorizing Resolution. The 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 Bonds.

We have examined (i) the Act, (ii) certified copies of the proceedings of the Authority, including Resolution No. 68-18, adopted on June 13, 1968, as amended (the "1968 Resolution"), (iii) the Puerto Rico Internal Revenue Code of 1994 (Subtitle B of Act No. 120 of the Legislature of Puerto Rico, approved October 31, 1994, as amended among other things by Act No. 34 of the Legislature of Puerto Rico, approved July 16, 1997, as amended), which allocated (A) the proceeds of the sixteen cents per gallon tax imposed on gasoline and four cents of the eight cents per gallon tax on gas oil and diesel oil (the "Allocated Gasoline Tax Proceeds") and (B) the proceeds (up to \$120 million per fiscal year) of the tax imposed on crude oil, unfinished oil and derivative products (the "Allocated Crude Oil Tax Proceeds") to the Authority for use for its corporate purposes, (iv) the Vehicle and Traffic Law of Puerto Rico, approved July 20, 1960, as amended, which allocated the proceeds of the fifteen dollar increase in the motor vehicle license fees for public and private service automobiles imposed by Act No. 9 of the Legislature of Puerto Rico, approved August 12, 1982 (the "Allocated Additional License Fees"), to the Authority for use for its corporate purposes and (v) Reorganization Plan No. 6 of 1971 (Act No.

113 of the Legislature of Puerto Rico, approved June 21, 1968), which attached the Authority to the Department of Transportation and Public Works.

We have also examined the law and such certified proceedings and other papers as we deem necessary to render the following opinions.

In rendering the following opinions we have assumed the genuineness of all signatures, the authenticity of all documents tendered to us as originals and the conformity to original documents of all documents submitted to us as certified or photostatic copies. As to questions of fact material to our opinion, we have relied upon the certified proceedings and other certifications of public officials furnished to us without undertaking to verify the same by independent investigation.

Based upon the foregoing, we are of the opinion, under existing law, as follows:

1. The Act is valid.
2. The proceedings authorizing the issuance of the Bonds have been validly and legally taken.
3. The Act and such proceedings show lawful authority of the issuance and sale of the Bonds.
4. The Authority has heretofore issued various series of bonds under and in compliance with the provisions of the 1968 Resolution (the "Highway Revenue Bonds"). The 1968 Resolution provides for the issuance of additional Highway Revenue Bonds under the conditions and limitations therein set forth, and the Authority has covenanted in the 1998 Resolution to limit the issuance of such additional Highway Revenue Bonds.
5. The 1998 Resolution provides for the issuance of additional bonds on a parity with the Bonds under the conditions, limitations and restrictions therein set forth (the Bonds and such additional parity bonds being herein called the "Senior Transportation Bonds") for any lawful purpose of the Authority and for the purpose of refunding any bonds issued by the Authority under the 1998 Resolution and any other obligations of the Authority, including outstanding Highway Revenue Bonds. In addition, the 1998 Resolution provides for the issuance of bonds subordinate to the Senior Transportation Revenue Bonds as to their lien on the revenues and other moneys of the Authority, as described below, under the conditions, limitations and restrictions and for the purposes set forth therein (the Senior Transportation Revenue Bonds and such bonds subordinate thereto being herein collectively called the "Transportation Revenue Bonds").
6. The 1998 Resolution provides for the creation of a special fund designated "Puerto Rico Highways and Transportation Authority Transportation Revenue Fund" (the Revenue Fund"), and, subject to the limitations of the next two paragraphs for the deposit to the credit of said special fund of all moneys received by the Authority (i) from the Allocated Crude

Oil Tax Proceeds, (ii) from the Allocated Gasoline Tax Proceeds, (iii) from the Allocated Additional License Fees, (iv) from any tolls or other charges imposed by the Authority for the use of any Toll Facilities and (v) from the proceeds of any other taxes, fees or charges which the Legislature of Puerto Rico may allocate to the Authority and expressly authorizes the Authority to pledge to the payment of the principal of and interest on bonds or other obligations issued by the Authority and which are pledged by the Authority to the payment of the principal of and interest on Transportation Revenue Bonds issued under the provisions of the 1998 Resolution.

The Allocated Gasoline Tax Proceeds, the Allocated Crude Oil Tax Proceeds and the Allocated Additional License Fees, and any other taxes, fees or charges which the Legislature of Puerto Rico may allocate to the Authority, are subject to first being applied to the payment of interest and amortization of public debt in accordance with the provisions of, and to the extent provided by, Section 8 of Article VI of the Constitution of Puerto Rico if needed for such purpose.

The 1968 Resolution provides for the prior deposit to the credit of a special fund designated "Puerto Rico Highways and Transportation Authority Construction Fund" (herein called the "1968 Construction Fund") of the Allocated Gasoline Tax Revenues, the Allocated Additional License Fees and all Existing Toll Facilities Revenues (As such term is defined in the 1998 Resolution), after the required deposits of such moneys have been made to the credit of the Puerto Rico Highways and Transportation Authority Highway Revenue Bonds Interest and Sinking Fund. In the 1998 Resolution, the Authority has covenanted (i) to withdraw monthly from the 1968 Construction Fund and deposit to the credit of the Revenue Fund until the outstanding Highway Revenue Bonds have been paid or provision has been made for their payment and the repeal and cancellation of the 1968 Resolution, all unencumbered moneys held to the credit of the 1968 Construction Fund and (ii) except for the foregoing withdrawal and any encumbrances on the moneys in the 1968 Construction Fund existing on the date of adoption of and as provided in the 1998 Resolution, not further to encumber or otherwise withdraw or pledge any such available moneys in the 1968 Construction Fund.

7. The Bonds are valid and binding special obligations of the Authority payable solely from the special fund created by the 1998 Resolution and designated "Puerto Rico Highways and Transportation Authority Transportation Revenue Bonds Interest and Sinking Fund." The Authority has covenanted to deposit to the credit of said Interest and Sinking Fund a sufficient amount of the moneys held to the credit of the Revenue Fund, together with any other funds of the Commonwealth of Puerto Rico allocated to the Authority and available under the 1998 Resolution for the payment of principal of and interest on the Senior Transportation Revenue Bonds, to pay the principal of and interest on all Senior Transportation Revenue Bonds (including the Bonds) issued under the provisions of the 1998 Resolution as the same may become due and payable and to create and maintain a reserve therefore. Said Interest and Sinking Fund is pledged to and charged with the payment of the principal of the principal and the interest on all Senior Transportation Revenues Bonds (including the Bonds) issued by the Authority under the provisions of the 1998 Resolution.

8. The Bonds do not constitute a debt of the Commonwealth of Puerto Rico or of any of its municipalities or other political subdivisions, and neither the Commonwealth of Puerto Rico nor any such municipality or other political subdivision is liable thereon, and the Bonds are payable only out of the revenues and other moneys of or allocated to the Authority, to the extent provided in the 1998 Resolution.

9. The Internal Revenue Code of 1986, as amended (the "Code") sets forth certain requirements which must be met subsequent to the issuance and delivery of the 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 Bonds to be included in gross income for Federal income tax purposes retroactively to the date of issue of the Bonds. The Authority has covenanted in the Resolution to comply with each provision of the Code applicable to the Bonds necessary to maintain the exclusion from gross income of the interest on the Bonds pursuant to Section 103 of the Code. In addition, the Authority has made certain representations and certifications relating to the Bonds in its "Tax Certificate as to Arbitrage and the Provisions of Sections 103 and 141-150 of the Internal Revenue Code of 1986" of even date herewith.

Under existing law, assuming compliance with the tax covenants described herein and the accuracy of certain representations and certifications made by the Authority described above, interest on the Bonds is excluded from gross income for Federal income tax purposes under Section 103 of the Code. We are 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 Bonds is, however, included in the adjusted current earnings of certain corporations for purposes of computing the alternative minimum tax imposed on such corporations.

10. The interest on the Bonds is exempt from state, Commonwealth and local personal income taxation.

11. Bond Counsel is further of the opinion that the difference between the principal amount of the Bonds maturing on July 1 in each of the following years: 2008 and bearing interest at the rate of 2.625%, 2009 and bearing interest at the rate of 2.50%, 2021 and bearing interest at the rate of 4.625%, 2022 and bearing interest at the rate of 4.70%, 2023 and bearing interest at the rate of 4.75%, 2024 and bearing interest at the rate of 4.80% and the term bonds maturing July 1, 2034, July 1 2039 and July 1, 2043 (collectively, 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 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

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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.

Except as stated in paragraphs 9, 10 and 11 above, we express no opinion as to any other Federal or state, Commonwealth or local tax consequences of the ownership or disposition of the Bonds. Furthermore, we express no opinion as to any Federal, state, Commonwealth or local tax law consequences with respect to the Bonds, or the interest thereon, if any action is taken with respect to the Bonds or the proceeds thereof upon the advice or approval of other bond counsel.

It is to be understood that the rights of the holders of the Bonds and the enforceability thereof may be subject to bankruptcy, insolvency, reorganization, moratorium and other similar laws affecting creditors' rights heretofore or hereafter enacted to the extent constitutionally applicable and that their enforcement may also be subject to the exercise of judicial discretion in appropriate cases.

Very truly yours,

SUMMARY OF CERTAIN PROVISIONS OF THE GRANT ANTICIPATION RESOLUTION

The following is a general summary of certain provisions of the Grant Anticipation Resolution. The summary is not to be considered a full statement of the terms of the Grant Anticipation Resolution and accordingly is qualified by reference thereto and is subject to the full text thereof. Copies of the Grant Anticipation Resolution may be reviewed upon written request at the offices of the Authority or Trustee.

The following are definitions of certain terms contained in the Grant Anticipation Resolution and used herein

Definitions of Certain Terms

“*Acceptance*” means the Acceptance of the Authority to the Assignment, dated as of March , 2004, pursuant to which the Authority has accepted the Secretary of Transportation’s assignment pursuant to the Assignment of his rights, duties and powers with respect to the receipt of Federal Transportation Funds.

“*Accreted Value*” means any amount defined as such in a Supplemental Resolution for purposes of determining the Redemption Price of, certain rights of the Owner of or certain other matters with respect to a Capital Appreciation Bond.

“*Accretion Date*” means any date defined as such in a Supplemental Resolution for purposes of determining the Accreted Value or Maturity Value of a Capital Appreciation Bond.

“*Act*” means Act No. 74 of the Legislature of Puerto Rico, approved June 23, 1965, as the same shall be amended from time to time or any successor legislation by which the Authority shall be created and from which it shall derive its powers.

“*Assignment Agreement*” means the Assignment Agreement dated as of March , 2004, from the Secretary of Transportation and the Authority, pursuant to which the Secretary of Transportation has irrevocably assigned his rights, duties and powers with respect to the receipt of Federal Transportation Funds to the Authority.

“*Authority Representative*” means (a) the Secretary of Transportation, (b) the Secretary, (c) the Executive Director; or (d) any other officer or employee of the Authority authorized by law or by a writing signed by the Executive Director to act as an Authority Representative under the Grant Anticipation Resolution or any Supplemental Resolution.

“*Bond Counsel*” means (a) as of the date of issuance of the first Series of Bonds, Nixon Peabody LLP, and (b) as of any other date, Nixon Peabody LLP or other attorneys selected by the Authority who have nationally recognized expertise in the issuance of municipal securities, the interest on which is excluded from gross income for federal income tax purposes.

“*Bond Payment Date*” means each date on which Bond Payments are due and includes, but is not limited to, the maturity date of any Bond; each Interest Payment Date on each Current Interest Bond; and the mandatory sinking fund redemption dates of term Bonds that are subject to mandatory sinking fund redemption in accordance with a mandatory sinking fund redemption schedule set forth in a Supplemental Resolution.

“*Bond Payment Fund*” means the special fund created by the Grant Anticipation Resolution.

“*Bond Payments*” means (a) with respect to a Current Interest Bond, the interest due on such Bond on each Interest Payment Date and the principal and interest due on such Bond at maturity; (b) with respect to a Capital Appreciation Bond, the Maturity Value due on such Bond at maturity; and (c) with respect to term Bonds that are subject to mandatory sinking fund redemption in accordance with a schedule set forth in a Supplemental Resolution, the principal and interest or the Accreted Value payable on such Bonds on the date on which they are subject to mandatory sinking fund redemption in accordance with such schedule. “Bond Payments” does not include the Redemption Price of any Bond.

For purposes of this definition:

(i) Bond Payments due on any Interest Payment Date that are payable from accrued interest or capitalized interest held in the Bond Payment Fund pursuant to the Grant Anticipation Resolution will be excluded in determining the amount of Bond Payments due in the Federal Fiscal Year in which such Interest Payment Date occurs for purposes of determining (A) the maximum annual Bond Payments for the certificate required by the Grant Anticipation Resolution; and (B) the amount of Federal Transportation Funds for which Federal Aid Agreements are to be in force and effect pursuant to the Grant Anticipation Resolution.

(ii) If any Bonds bear interest at an adjustable or variable interest rate such that the Bond Payments due in a Federal Fiscal Year or on a Bond Payment Date cannot be determined with certainty on the date on which Federal Transportation Funds are to be paid to the Trustee pursuant to the Grant Anticipation Resolution, or in determining the amount of Bond Payments becoming due during a Federal Fiscal Year for purposes of preparing the certificate required by the Grant Anticipation Resolution, the amount of interest included in the Bond Payments due on such Bonds in such Federal Fiscal Year or on such Bond Payment Date shall be based on the interest rate estimated by the Authority, or as stated in any Supplemental Resolution relating thereto.

(iii) If the Authority purchases or arranges for a Credit Facility or an Interest Rate Exchange Agreement with respect to any Bonds pursuant to the Grant Anticipation Resolution, (A) moneys paid or payable to the provider of the Credit Facility to reimburse the provider for moneys paid by the provider that are used to make Bond Payments (as defined in the first two sentences of this definition) and (B) moneys paid or payable to the provider of the Interest Rate Exchange Agreement for moneys paid by the provider that are used to make Bond Payments (as defined in the first two sentences of this definition) may, but in each case if and to the extent provided in a Supplemental Resolution or in a separate agreement between the Authority and the Credit Facility or Interest Rate Exchange Agreement provider entered into pursuant to the Grant Anticipation Resolution, be treated as Bond Payments on the Bonds to which the Credit Facility or Interest Rate Exchange Agreement relates.

“*Business Day*” means any day other than a Saturday, a Sunday or a day on which banks in New York, New York, San Juan, Puerto Rico or any city identified in a Supplemental Resolution are authorized by law to remain closed.

“*Capital Appreciation Bond*” means a Bond on which no payments are due until maturity or redemption prior to maturity.

“*Code*” means the Internal Revenue Code of 1986, as amended, and regulations thereunder.

“*Construction Costs*” means all costs and expenses paid or incurred or to be paid or incurred (including the reimbursement of the Authority for any of such costs and expenses originally paid or incurred by the Authority) in connection with:

(a) the design of, acquisition of right-of-way for, construction of and improvements made as part of the Construction Projects;

(b) financing costs, including, but not limited to, costs and expenses that the Authority deems necessary or advantageous in connection with the sale of the Bonds and the administration of the Bonds, the Trust Estate, the Grant Anticipation Resolution and any Supplemental Resolution, including, but not limited to, costs and expenses relating to the engagement of consultants, financial advisors, underwriters, bond insurers, letter of credit banks, rating agencies, attorneys, trustees, paying agents, registrars, other agents and other Persons in connection with the issuance of the Bonds, the Trust Estate, the Grant Anticipation Resolution or any Supplemental Resolution;

(c) payment of interest on the Bonds;

(d) restoration of the Debt Service Reserve Fund as contemplated by the Grant Anticipation Resolution;

(e) costs and expenses relating to any Credit Facility entered into in accordance with the Grant Anticipation Resolution, including the reimbursement of the provider of any Credit Facility as provided in the Grant Anticipation Resolution;

(f) costs and expenses relating to any Interest Rate Exchange Agreement entered into in accordance with the Grant Anticipation Resolution; and

(g) amounts required to be deposited into the Rebate Fund pursuant to the Grant Anticipation Resolution and the Tax Certificates.

“*Construction Fund*” means the special fund created by the Grant Anticipation Resolution.

“*Construction Project*” means, any Qualified Federal Aid Transportation Project with respect to which a Federal Aid Agreement is in full force and effect.

“*Credit Facility*” means any letter of credit, insurance, stand-by credit or liquidity agreement or other forms of credit ensuring timely payment of any Bonds, including the Bond Payments on or the Redemption Price or purchase price of such Bonds, that is entered into in accordance with the Grant Anticipation Resolution. References to “*Credit Facility*” with respect to any Series of Bonds shall be ineffective when such Bonds are not supported by a Credit Facility.

“*Current Interest Bond*” means a Bond on which interest is payable on Interest Payment Dates prior to maturity or redemption prior to maturity.

“*Current Payments*” means all payments required to be made from Federal Transportation Funds for the payment of all Bond Payments and Program Costs, which become due during the Federal Fiscal Year for which the Obligation Authority was allocated or apportioned.

“*Debt Service Reserve Fund*” means the special fund created by the Grant Anticipation Resolution.

“*Defeasance Escrow Account*” means any trust account into which money and/or Defeasance Securities are deposited for the purpose of defeasing any Bonds in accordance with the Grant Anticipation Resolution.

“*Defeasance Securities*” means Government Obligations that, at the time they are deposited into a Defeasance Escrow Account either (i) cannot be redeemed prior to maturity at the option of any Person other than the owner thereof or (ii) the redemption date of which has been irrevocably fixed by an irrevocable exercise of an option to redeem on such date or an irrevocable covenant to exercise an option to redeem on such date (in which case the fixed redemption date shall be treated as the maturity date for purposes of the Grant Anticipation Resolution).

“*Earnings Account*” means the earnings account within the Construction Fund created by the Grant Anticipation Resolution.

“*Event of Default*” means an event described in the Grant Anticipation Resolution.

“*Executive Director*” means the Executive Director of the Authority or the Deputy Executive Director of the Authority for the time being, or if there is no Executive Director of the Authority or Deputy Executive Director of the Authority, then any person designated by the Authority to perform the function of the Executive Director.

“*Federal Aid Agreement*” means one or more agreements or memorandum of understanding between the Authority and FHWA pursuant to which FHWA agrees to pay Federal Transportation Funds to pay or to reimburse the Authority or the Trustee for Bond Payments, as such agreement or agreements may be amended or modified or replaced by another agreement or instrument regarding the payment of Federal Transportation Funds by FHWA to pay or to reimburse the Authority or the Trustee for Bond Payments.

“*Federal Aid Authorization*” means, as applicable, (a) Title 23, (b) any extension of Title 23, or (c) any successor to Title 23 authorizing federal funding of state and Commonwealth highways.

“*Federal Fiscal Year*” means the period commencing on October 1 in each calendar year and ending on the last day of September of the next succeeding calendar year, or any other twelve-month period which any appropriate authority may hereafter establish for the federal government as its fiscal year.

“*Federal Transportation Funds*” means federal aid revenues received by or on behalf of, or available to, the Authority pursuant to Title 23 that are legally available for the payment of Bond Payments and Construction Costs. The Title 23 federal aid revenues legally available as Federal Transportation Funds include, but are not limited to, those derived pursuant to Title 23 from the National Highway System, bridges and the federal surface transportation programs and amounts available under the minimum guarantees under, and as described in, Title 23.

“*FHWA*” means the United States Department of Transportation, Federal Highway Administration, its successors and assigns and any other agency or branch of government of the United States which succeeds to the powers of FHWA, which term includes the United States Secretary of Transportation and any other appropriate officer of FHWA with authority to grant approvals or consents or to take other appropriate action as is necessary to approve the Construction Projects, federal grants to finance the Construction Projects and the payment of Bond Payments and to take such other action as is necessary for those purposes under Title 23.

“*FHWA MOA*” means Memorandum of Agreement between the Federal Highway Administration and the Authority dated March , 2004, as such agreement may be amended or modified or replaced by another agreement or instrument regarding the manner in which Federal Transportation Funds will be administered and accounted for.

“*Fitch*” means Fitch Inc. and its successors.

“*Government Obligations*” means (i) direct obligations of, or obligations the principal of and the interest on which are unconditionally guaranteed by, the United States Government, (ii) bonds, debentures or notes issued by any of the following Federal Agencies: Banks for Cooperatives, Federal Intermediate Credit Banks, Federal Home Loan Banks, Export-Import Bank of the United States, Government National Mortgage Association or Federal Land Banks, (iii) obligations issued or guaranteed by an agency of the United States of America or person controlled or supervised by and acting as an instrumentality of the United States of America pursuant to authority granted by the Congress, (iv) municipal obligations, the payment of the principal of and interest and redemption premium, if any on which are irrevocably secured by obligations described in clause (i) of this definition and which obligations are not subject to redemption prior to the date on which the proceeds attributable to the principal of the obligations are to be used and have been deposited in an escrow account which is irrevocably pledged to the payment of the principal of and interest and redemption premium, if any, on such municipal obligations, and (v) evidences of ownership of proportionate interests in future interest or principal payments on obligations specified in clauses (i), (ii), (iii) and (iv) of this definition held by a bank (including the Trustee) or trust company as custodian and which underlying obligations are not available to satisfy any claim of the custodian or any person claiming through the custodian or to whom the custodian may be obligated.

“*Interest Payment Date*” means any date defined as such in a Supplemental Resolution for purposes of paying the interest on a Series of Current Interest Bonds.

“*Interest Rate Exchange Agreement*” means any interest rate exchange agreement authorized by law and entered into with respect to the Bonds or any portion of the Trust Estate that is entered into in accordance with the Grant Anticipation Resolution.

“*Maturity Value*” means any amount defined as such in a Supplemental Resolution for purposes of determining the amount payable to the Owner of a Capital Appreciation Bond at the maturity of such Capital Appreciation Bond.

“*Moody’s*” means Moody’s Investor Service and its successors.

“*New Money Bonds*” means Bonds issued for the purpose of financing the Construction Projects.

“*Obligation Authority*” means the amount of funds apportioned or allocated by FHWA pursuant to Title 23 to the Authority for each Federal Fiscal Year.

“*Operations Center*” means the operations center of the Trustee in San Juan, Puerto Rico or at such other location as the Trustee may designate from time to time by written notice to the Authority.

“*Original Principal Amount*” means any amount defined as such in a Supplemental Resolution for purposes of determining certain rights of the Owner of, or certain other matters with respect to, a Capital Appreciation Bond.

“*Original Purchaser*” means the Person defined as such in a Supplemental Resolution for purposes of purchasing a Series of Bonds from the Authority.

“*Outstanding*” means all Bonds that have been executed and delivered, except:

- (a) any Bond on which all Bond Payments due or to become due have been paid at maturity;
- (b) any Bond on which the Redemption Price due or to become due has been paid in accordance with the redemption provisions applicable to such Bond;
- (c) Bonds in lieu of which other Bonds have been executed and delivered pursuant to the provisions of the Grant Anticipation Resolution or any Supplemental Resolution relating to the transfer and exchange of Bonds or the replacement of mutilated, lost, stolen or destroyed Bonds;
- (d) Bonds that have been canceled by the Trustee or that have been surrendered to the Trustee for cancellation;
- (e) Bonds on which all Bond Payments or the Redemption Price is due and for which the Trustee holds moneys sufficient to pay the Bond Payments or Redemption Price for the benefit of the Owner thereof pursuant to the Grant Anticipation Resolution; and
- (f) Bonds that have been defeased pursuant to the Grant Anticipation Resolution.

“*Owner*” of a Bond means the registered owner of such Bond as shown in the registration records of the Trustee.

“*Permitted Investments*” means:

- (a) Government Obligations;
- (b) direct and general obligations of any state or territory of the United States of America to the payment of the principal of and interest on which the full faith and credit of such state or territory is pledged, provided that such obligations are rated, on the date of investment therein, in any of the three highest rating categories (without regard to any graduations, within any such category) by both Moody’s or any successors thereto and S&P or any successors thereto;
- (c) bankers’ acceptances, certificates of deposit or time deposits of any bank or national banking association (including the Trustee), trust company or savings and loan association (including any investment in pools of such bankers’ acceptances, certificates of deposit or time deposits), which to the extent that such obligations are not insured by the Federal Deposit Insurance Corporation, are either (A) issued by a bank, trust company or savings and loan association having a combined capital and surplus aggregating at least \$50,000,000 or (B) collateralized at all times by such securities as are described in clauses (i) or (ii) above, having a market value at least equal to the principal amount of such bankers’ acceptances, certificates of deposit or time deposits (or portion thereof not so insured); provided that the Trustee has a perfected first security interest in the collateral and that such collateral is held free and clear of claims by third parties;
- (d) any repurchase, reverse repurchase or investment agreement with any bank or trust company organized under the laws of any state of the United States or the Commonwealth or any national banking association (including the Trustee), insurance company, or government bond dealer reporting to, trading with, and recognized as a primary dealer by the Federal Reserve Bank of New York and a member of the Security Investors Protection Corporation, which agreement is secured by any one or more of the

securities described in clauses (i) and (ii) above, provided that the Trustee has a perfected first security interest in the collateral and that such collateral is held free and clear of claims by third parties;

(e) obligations, whether or not insured, issued by any state or territory of the United States, or any political subdivision, agency or instrumentality thereof which are rated, on the date of investment therein, in one of the three highest rating categories (without regard to any gradations within any such category) by both Moody's or any successors thereto and S&P or any successors thereto;

(f) participating shares in a mutual fund or investment pool for local government investment; provided that the investments of such mutual fund or investment pool are rated in one of the three highest rating categories (without regard to any gradations within any such category) by both Moody's or any successors thereto, and S&P or any successors thereto;

(g) (1) shares of stock in a corporation rated in the highest rating category by Moody's or any successors thereto and S&P or any successors thereto (without regard to gradations within such category) that (A) is a regulated investment company within the meaning of Section 851(a) of the Internal Revenue Code of 1986, as amended, and, meets the requirements of Section 852(a) of said Code for the calendar year; (B) invests all of its assets in obligations described in clauses (i) and (ii) above; and (C) has at least 98% of (I) its gross income derived from interest on, or gain from the sale of or other disposition of, such obligations or (II) the weighted average of its assets is represented by investments in such obligations or (2) money market accounts of the Trustee or any state or federally chartered bank, banking associations, trust company or subsidiary trust company that is rated or whose parent state bank is rated in the highest short-term rating category or in one of the two highest long-term rating categories by Moody's or any successors thereto and S&P or any successors thereto (without regard to any gradations within such category); and

(h) any other obligations permitted under the laws of the Commonwealth which are rated, or which are issued by issuers which are rated, on the date of investment therein, in any of the three highest rating categories (without regard to any gradations within any such category) by both Moody's or any successors thereto and S&P or any successors thereto, or which are collateralized by Permitted Investments.

"*Person*" means any natural person, firm, corporation, partnership, limited liability company, state, political subdivision of any state, other public body or other organization or association.

"*principal amount*" means (a) with respect to any Outstanding Current Interest Bond, the principal amount of such Bond; (b) with respect to any Outstanding Capital Appreciation Bond, the Accreted Value of such Bond as of the date on which the Bond is being determined; and (c) with respect to all the Outstanding Bonds together, the sum of the amounts determined pursuant to clauses (a) and (b).

"*Program Costs*" means the costs and expenses set forth in items (b) through (g) included in the definition of Construction Costs.

"*Qualified Federal Aid Transportation Project*" means any project that may be financed, in whole or in part, with Federal Transportation Funds.

"*Rating Agency*" means, with respect to the Bonds, each nationally recognized securities rating service that has, at the request of the Authority, a rating then in effect for the unenhanced Bonds.

"*Rating Confirmation*" means, with respect to the Bonds, written evidence from a Rating Agency that no underlying Bond rating then in effect from such Rating Agency will be withdrawn, reduced or suspended solely as a result of an action to be taken hereunder.

"*Rebate Fund*" means the special fund created by the Grant Anticipation Resolution.

"*Record Date*" means (a) with respect to any Interest Payment Date that is the first day of a month, the fifteenth day of the month (whether or not a Business Day) preceding the month in which the Interest Payment Date occurs; (b) with respect to any Interest Payment Date that is the fifteenth day of a month, the first day of such month (whether or not a Business Day); and (c) with respect to any other Interest Payment Date, the date designated as the Record Date for such Interest Payment Date in a Supplemental Resolution.

“*Redemption Price*” means the amount due on a Bond on the date on which it is redeemed prior to maturity pursuant to the redemption provisions applicable to such Bond. Such term does not include the principal and interest or Accreted Value due on term Bonds on the dates such Bonds are to be redeemed in accordance with a mandatory sinking fund redemption schedule set forth in a Supplemental Resolution.

“*Refunding Bonds*” means Bonds issued for the purpose of refunding, and proceeds of which are used to refund, New Money Bonds or other Refunding Bonds.

“*Reserve Account Credit Facility*” means any letter of credit, surety bond or insurance policy meeting the criteria set forth in a Supplemental Resolution authorizing the issuance of a Series of Bonds.

“*S&P*” means Standard & Poor’s Ratings Services, a division of the McGraw-Hill Companies, Inc., and its successors.

“*Secretary*” means the Secretary or any Assistant Secretary of the Authority for the time being, or if there is no Secretary or Assistant Secretary, then any person designated by the Authority to perform the functions of the Authority.

“*Secretary of Transportation*” means the Secretary of Transportation and Public Works of the Commonwealth from time to time, or such other officer or the board or body succeeding to the powers and principal functions of the Secretary of Transportation and Public Works of the Commonwealth insofar as such powers and principal functions pertain to governance of the Authority.

“*Series*” means the Bonds designated as a separate series in a Supplemental Resolution and any Bonds authenticated and delivered in lieu of or in substitution for such Bonds pursuant to the Grant Anticipation Resolution or any Supplemental Resolution.

“*Series Debt Service Reserve Requirement*” means for each Series of Bonds, the Series Debt Service Reserve Requirement as prescribed in the Supplemental Resolution authorizing such Series of Bonds.

“*Supplemental Resolution*” means any resolution supplementing or amending the Grant Anticipation Resolution that is adopted pursuant to the Grant Anticipation Resolution.

“*Special Record Date*” means a special date fixed to determine the names and addresses of Owners of Bonds for purposes of paying defaulted interest on Current Interest Bonds in accordance with the Grant Anticipation Resolution.

“*Tax Certificate*” means with respect to each Series of Bonds on which the Authority intends the interest to be excluded from gross income for federal income tax purposes, (a) the arbitrage and use of proceeds certificate or other instrument that sets forth the Authority’s expectations regarding the investment and use of proceeds of such Bonds and other matters relating to Bond Counsel’s opinion regarding the federal income tax treatment of interest on such Bonds, including any instructions delivered by Bond Counsel in connection with such certificate, instrument or opinion; and (b) any amendment or modification of any such certificate, instrument or instructions that is accompanied by an opinion of Bond Counsel stating that the amendment or modification will not adversely affect the exclusion of interest on such Bonds from gross income for federal income tax purposes.

“*Title 23*” means Chapter 1 of Title 23, United States Code, Highways, as amended and supplemented from time to time and any successor or replacement provision of law.

“*Trust Estate*” means the property granted to the Trustee pursuant to the Grant Anticipation Resolution.

“*Trustee*” means JPMorgan Chase Bank, acting in its capacity as trustee under the Grant Anticipation Resolution, and any successor thereto appointed thereunder.

“*Trustee Representative*” means any officer in the corporate trust department of the Trustee and any other person authorized by a writing signed by an officer of the Trustee to act as a Trustee Representative under the Grant Anticipation Resolution or any Supplemental Resolution. (*Section 1.01*)

Grant of Trust Estate

The Authority, in consideration of the premises, the purchase of the Bonds by the Owners and other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, in order to secure the payment of the Bond Payments on all Bonds at any time Outstanding hereunder, to secure the performance and observance of all the covenants and conditions set forth in the Bonds, the Grant Anticipation Resolution and any Supplemental Resolution, and to declare the terms and conditions upon and subject to which the Bonds are issued and secured, has adopted the Grant Anticipation Resolution and has granted, assigned, pledged, bargained, sold, alienated, remised, released, conveyed, set over and confirmed, and by these presents does grant, assign, pledge, bargain, sell, alienate, remise, release, convey, set over and confirm unto the Trustee and to its successors and assigns forever, all and singular the following described property, franchises and income, including any title or interest therein acquired after these presents (referred to herein as the "Trust Estate"):

(a) all Federal Transportation Funds that are paid to the Authority or the Trustee, together with the right of the Authority to receive such funds;

(b) all money from time to time held by the Trustee under the Grant Anticipation Resolution or any Supplemental Resolution in any fund or account other than (i) the Rebate Fund, (ii) the Construction Fund, (iii) any Defeasance Escrow Account and (iv) any fund or account created by a Supplemental Resolution that is expressly excluded from the Trust Estate; and

(c) any and all other property, revenues or funds from time to time hereafter by delivery or by writing of any kind specially granted, assigned or pledged as and for additional security hereunder, by the Authority or anyone else, in favor of the Trustee, which is hereby authorized to receive any and all such property at any and all times and to hold and apply the same subject to the terms thereof.

(Section 2.01)

Effect of Pledge

(a) The proceeds from the issuance of Bonds that are pledged pursuant to the Grant Anticipation Resolution shall be used only for the purpose or purposes for which such funds are pledged;

(b) Such pledge of such Federal Transportation Funds shall be valid and binding from the time such funds are transferred to the Trustee or the Authority, and any pledge of the proceeds of any Bonds pursuant to the Grant Anticipation Resolution shall be valid and binding from the date of issuance of such Bonds;

(c) All such pledges shall create a valid security interest, and such revenues shall immediately be subject to the lien of the pledge and security interest without any physical delivery or further act, and the lien of the pledge and security interest shall be valid and binding against all parties having claims of any kind in tort, contract, or otherwise against the pledging party irrespective of whether such claiming party has notice of such lien; and

(d) The instrument by which the pledge and security interest is created need not be recorded or filed in order to perfect such pledge and security interest.

(Section 2.02)

Bonds Secured on a Parity Unless Otherwise Provided

The Trust Estate shall be held by the Trustee for the equal and proportionate benefit of the Owners of all Outstanding Bonds, and any of them, without preference, priority or distinction as to lien or otherwise, except as expressly set forth in the Grant Anticipation Resolution or any Supplemental Resolution.

(Section 2.04)

Limited Obligations

Notwithstanding any other provision of the Grant Anticipation Resolution:

(a) The Bond Payments shall be payable solely from Federal Transportation Funds that are received by the Authority or the Trustee and moneys held in the Bond Payment Fund. The Owners and holders of the Bonds may not look to any other revenues of the Authority for the payment of the Bonds.

(b) All financial obligations of the Authority under the Grant Anticipation Resolution, every Supplemental Resolution and the Bonds (i) are special, limited obligations of the Authority payable solely from the Trust Estate and shall not constitute nor give rise to a pecuniary liability or a charge against the general credit of the Authority or the Commonwealth and (ii) shall not be deemed or construed as creating a debt, liability or obligation of the Commonwealth, or any political subdivision of the Commonwealth, nor a pledge of the faith and credit of the Commonwealth or any political subdivision or municipality of the Commonwealth within the meaning of the Constitution of the Commonwealth or the laws of the Commonwealth concerning or limiting the creation of indebtedness by the Commonwealth or any political subdivision of the Commonwealth.

(c) The provisions of this heading are hereby expressly incorporated into each Supplemental Resolution. The Bonds shall contain statements substantially to the effect of paragraphs (a) and (b) summarized under this heading.

(Section 2.05)

Resolution to Constitute a Contract; Obligation of Resolution and Bonds

In consideration of the purchase and acceptance of any and all of the Bonds authorized from time to time to be issued under the Grant Anticipation Resolution, as amended or supplemented, by those who shall hold the same from time to time: the Grant Anticipation Resolution shall be deemed to be and shall constitute a contract among the Authority, the Trustee and the Owners from time to time of the Bonds; the pledge of certain funds, accounts, revenues and other moneys, rights and interests made in the Grant Anticipation Resolution and the covenants and agreements set forth in the Grant Anticipation Resolution to be performed by and on behalf of the Authority, including the covenants of the Authority therein, shall be for the equal and ratable benefit, protection and security of the Owners of any and all of the Bonds, all of which regardless of the time or times of their issue or maturity shall be of equal rank without preference, priority or distinction of any of such Bonds over any other thereof, except as expressly provided in or permitted by the Grant Anticipation Resolution; and the Bonds shall be special, limited obligations of the Authority payable solely from the Trust Estate as provided therein.

(Section 2.06)

Conditions to Issuance of Bonds

No Series of Bonds may be issued unless each of the following conditions applicable thereto have been satisfied:

(a) Before any Series of Bonds constituting New Money Bonds are issued or incurred, it shall be determined that:

(i) All accumulations required to be made into the Bond Payment Fund or other similar account, and each account in the Debt Service Reserve Fund, for Outstanding Bonds, are current.

(ii) No Event of Default exists in connection with any of the covenants or requirements of the Grant Anticipation Resolution.

(iii) A certificate has been delivered showing compliance with all applicable provisions of Title 23 and any other applicable law necessary on the date of the delivery of a Series of Bonds to receive and continue to receive federal aid highway funds for the payment of the Bonds pursuant to Title 23 without penalty.

(iv) A certificate of an Authority Representative has been delivered, dated the date of issuance, setting forth:

(x) the lowest amount of Federal Transportation Funds received by the Authority in any Federal Fiscal Year during the three Federal Fiscal Year period immediately

preceding the authentication and delivery of the Series of additional Bonds then proposed to be issued;

(y) the maximum annual Bond Payments for the Outstanding Bonds in the current and each future Federal Fiscal Year including the Series of additional Bonds proposed to be issued, but in the case of a Series of additional Bonds for refunding purposes, excluding the Bond Payments on the Bonds to be refunded; and

showing that the Federal Transportation Funds set forth pursuant to (x) above is not less than 400% of the maximum annual Bond Payments set forth in (y) above.

(v) A certificate of the Authority dated the date of delivery shall have been delivered to the Trustee that states in substance that the Authority has no information which indicates that Federal Transportation Funds will not be available to the Authority or will be substantially reduced, during the term of the then current Federal Aid Authorization, and that it is the Executive Director's reasonable belief that sufficient Federal Transportation Funds will continue to be available to the Authority pursuant to Title 23 during that period of time.

(vi) Notwithstanding provisions in the Grant Anticipation Resolution, the requirements of paragraph (a)(iv) under this heading may be revised or deleted in their entirety upon the Authority's receipt of Rating Confirmation from each Rating Agency.

(b) A written certification or opinion by an Authority Representative that the requirements summarized under this heading have been satisfied shall be conclusively presumed to be accurate in determining the right to authorize, issue, sell and deliver the Series of Bonds proposed to be issued.

(c) Until all Bond Payments and Program Costs are paid in full and while any Bonds are Outstanding, no bonds, notes, debentures or other obligations shall be issued or incurred having a lien on the Trust Estate prior and superior to the lien thereon of the Bonds.

(d) Before any Series of Bonds constituting Refunding Bonds are issued, all of the following additional conditions shall be satisfied:

(i) Either the requirements of paragraph (a)(iv) summarized under this heading shall have been met (as and if in effect on such date) or a certificate of an Authority Representative shall state that following the issuance of the Refunding Bonds (including Bond Payments with respect to the Refunding Bonds, but excluding Bond Payments with respect to the refunded Bonds), the aggregate amount of Bond Payments due in any Federal Fiscal Year, through and including the latest maturity of any Bonds then Outstanding, shall be no greater than immediately prior to the issuance of such Refunding Bonds.

(ii) If any of the Bonds to be refunded are to be redeemed prior to their scheduled maturity date, an Authority Representative has directed the Trustee to deliver redemption notices and to redeem the Bonds to be refunded in accordance with the provisions of the Grant Anticipation Resolution and any applicable provisions of any Supplemental Resolution.

(iii) The Federal Aid Agreements pursuant to which Federal Transportation Funds are payable with respect to the Bond Payments on the refunded Bonds have been modified to provide that Federal Transportation Funds will be paid with respect to the Bond Payments on the Refunding Bonds or FHWA has agreed that Federal Transportation Funds will be paid with respect to the Bond Payments on the Refunding Bonds without any modification of such Federal Aid Agreements.

(e) If the additional Series of Bonds are not part of the first Series of Bonds, an Authority Representative certifies that as of the date of issuance of the additional Bonds, either:

(i) there is no Event of Default under the Grant Anticipation Resolution; or

(ii) if there is an Event of Default under the Grant Anticipation Resolution, the Event of Default will be cured upon the issuance of the additional Bonds and the application of the proceeds of the additional Bonds in accordance with the Supplemental Resolution authorizing the issuance of the additional Bonds.

(f) The Authority adopts and the Trustee accepts a Supplemental Resolution authorizing the issuance of each Series of Bonds, which Supplemental Resolution specifies the following:

(i) The Series designation, the name, the aggregate principal amount, the Authorized Denominations, the dated date, the maturity date or dates and the form of the additional Bonds, as bonds or notes, and, if the additional Bonds are Capital Appreciation Bonds, the aggregate Original Principal Amount of each Series and of each Authorized Denomination of such Series.

(ii) If the additional Bonds are Current Interest Bonds, the interest rate or rates, if any, or the method for determining the interest rate or rates on the additional Bonds, which rates may be fixed, adjustable or variable or any combination thereof, and, if any such rate is adjustable or variable, the standard, index, method or formula to be used to determine the interest rate and the maximum interest rate applicable to the additional Bonds; and the Interest Payment Date or Dates for the payment of such interest.

(iii) If the additional Bonds are Capital Appreciation Bonds, the Maturity Value, Accreted Value and Accretion Dates, or the manner of determining the same, for the additional Bonds.

(iv) The redemption provisions, if any, for the additional Bonds.

(v) The form of the additional Bonds.

(vi) The manner in which the proceeds of the additional Bonds are to be applied.

(vii) Any variations from the terms set forth in the Grant Anticipation Resolution with respect to the additional Bonds.

(viii) Any other provisions deemed by an Authority Representative to be advisable or desirable to be included in such Supplemental Resolution that do not violate and are not in conflict with the Grant Anticipation Resolution or any previous Supplemental Resolution.

(g) Bond Counsel has delivered a written opinion to the effect (which may be subject to customary assumptions and limitations) that (i) the additional Bonds have been duly authorized, executed and delivered by the Authority and are valid and binding special, limited obligations of the Authority, payable from the sources provided in the Grant Anticipation Resolution and the applicable Supplemental Resolution; (ii) the Grant Anticipation Resolution creates a valid pledge of and lien on the Trust Estate, subject to the terms thereof; and (iii) if the interest on the additional Bonds is intended by the Authority to be excluded from gross income for federal income tax purposes, interest on the additional Bonds is excluded from gross income for federal income tax purposes.

(Section 3.02)

Bond Payment Fund

(a) ***Creation of Bond Payment Fund.*** A special fund is hereby created with the Trustee to be designated the Puerto Rico Highways and Transportation Authority Grant Anticipation Revenue Bonds Bond Payment Fund (the “Bond Payment Fund”), which shall be used to pay the Bond Payments on and Redemption Price of the Bonds. The Trustee shall create and maintain separate accounts identified by the appropriate Series designation within the Bond Payment Fund to account for the receipt of moneys to pay, and the payment of, the Bond Payments on and Redemption Price of each Series of Bonds, but such separate accounts shall not affect the rights of the Owners of the Bonds with respect to moneys in the Bond Payment Fund.

(b) ***Deposits into Bond Payment Fund.*** There shall be deposited into the Bond Payment Fund (i) all accrued interest received at the time of the issuance of any Bonds; (ii) any capitalized interest from the proceeds of a Series of Bonds unless deposited in the Construction Fund pursuant to a Supplemental Resolution; (iii) to the extent

necessary to make the next Bond Payment, amounts paid to the Trustee pursuant to the Grant Anticipation Resolution from Federal Transportation Funds; (iv) any moneys paid by the Authority with respect to the Redemption Price of Bonds pursuant to the Grant Anticipation Resolution; (v) any moneys transferred to the Bond Payment Fund from the Construction Fund pursuant to the Grant Anticipation Resolution; (vi) moneys deposited into the Bond Payment Fund pursuant to the Grant Anticipation Resolution following an Event of Default; and (vii) all other moneys received by the Trustee accompanied by directions that such moneys are to be deposited into the Bond Payment Fund.

(c) ***Use of Moneys in Bond Payment Fund.*** Moneys in the Bond Payment Fund shall be used, as further provided in the Grant Anticipation Resolution, solely for the payment of the Bond Payments on and Redemption Price of the Bonds and, solely to the extent such payments have been determined to be on a parity with Bond Payments in accordance with the Grant Anticipation Resolution, to make payments to the providers of Credit Facilities and Interest Rate Exchange Agreements; provided that (i) moneys representing accrued interest received at the time of the issuance of any Series of Bonds shall be used to pay the first interest payment due on such Bonds; (ii) moneys paid by the Authority with respect to the Redemption Price of Bonds pursuant to the Grant Anticipation Resolution shall be used to pay the Redemption Price of the Bonds to be redeemed; and (iii) moneys held in the Bond Payment Fund following an Event of Default shall be used as provided in the Grant Anticipation Resolution.
(Section 5.01)

Construction Fund.

(a) ***Creation of Construction Fund.*** A special fund is hereby created with the Trustee to be designated the Puerto Rico Highways and Transportation Authority Grant Anticipation Revenue Bonds Construction Fund (the “Construction Fund”). The Trustee shall create and maintain separate accounts identified by the appropriate Series designation within the Construction Fund to account for the receipt and disbursement of proceeds of each Series of Bonds and shall create and maintain a separate account identified as the Earnings Account (the “Earnings Account”).

(b) ***Deposits into Construction Fund.*** There shall be deposited into the appropriate account of the Construction Fund, proceeds of each Series of Bonds as provided in the applicable Supplemental Resolution.

(c) ***Use of Moneys in Construction Fund.*** Upon the written direction of an Authority Representative, any amounts on deposit in the Construction Fund shall be transferred to or upon the order of the Authority for the payment of, or reimbursement for, costs of issuance relating to any Bonds. So long as no Event of Default described in the Grant Anticipation Resolution then exists, moneys held in the Construction Fund (including the Earnings Account) shall be disbursed to the Authority (or the payee indicated by the Authority) to pay Construction Costs, or reimburse such costs, upon receipt of a requisition signed by the Authority Representative; ***provided, however, that*** requisitions of amounts in the Earnings Accounts shall not require the information set forth in columns (e), (f), (g) and (h). Moneys held in the Construction Fund following such an Event of Default may be transferred at the direction of the Executive Director to the Bond Payment Fund in accordance with the Grant Anticipation Resolution. In the event of a transfer pursuant to the preceding sentence followed by the availability of sufficient amounts to the Trustee from Federal Transportation Funds or other sources in excess of any amount necessary to make any Bond Payments then due, such excess amount up to the amount transferred from the Construction Fund to the Bond Payment Fund shall be transferred to the Construction Fund upon the direction of the Executive Director. Upon the receipt by the Trustee of a certificate from the Executive Director stating that all the Construction Projects have been completed and all required amounts have been deposited into the Rebate Fund, the remaining moneys in the Construction Fund, minus any amount estimated by the Executive Director necessary to pay Construction Costs that have not yet been paid, shall be transferred by the Trustee to the Authority.
(Section 5.02)

Debt Service Reserve Fund

(a) ***Creation of Debt Service Reserve Fund.*** A special fund is hereby created with the Trustee to be designated the Puerto Rico Highways and Transportation Authority Grant Anticipation Revenue Bonds Debt Service Reserve Fund (the “Debt Service Reserve Fund”). Any Supplemental Resolution may establish an account in the Debt Service Reserve Fund related to the Series of Bonds authorized thereby, identified by the appropriate Series designation, which shall be funded pursuant to the terms of such Supplement Resolution. The Series Debt Service Reserve Requirement shall be deposited in the account related to such Series. Amounts in each account in the Debt Service Reserve Fund shall be used to pay debt service on the related Series of Bonds on the date such debt service is due when insufficient funds for that purpose are available in the Bond Payment Fund; provided, however, that all

amounts in an account in the Debt Service Reserve Fund shall be used, together with other amounts available for such purpose under the Grant Anticipation Resolution, to provide for payment of the related Series of Bonds when the aggregate of such amounts is sufficient for such purpose. Amounts in each account of the Debt Service Reserve Fund shall be pledged to Owners of Bonds of the related Series.

(b) ***Reserve Account Credit Facilities.*** In lieu of or in substitution for any moneys on deposit in an account in the Debt Service Reserve Fund, the Authority may, in the manner provided, and in compliance with the conditions set forth in, the Supplemental Resolution authorizing such Series of Bonds, deposit or cause to be deposited with the Trustee a Reserve Account Credit Facility meeting the criteria set forth in such Supplemental Resolution.

(c) ***Restoration of the Debt Service Reserve Fund.*** If after the transfer of moneys on deposit in the Debt Service Reserve Fund to the Bond Payment Fund, the amount left on deposit in any account in the Debt Service Reserve Fund shall be less than the applicable Series Debt Service Reserve Requirement, or, if after a draw under any Reserve Account Credit Facility on deposit in an account in the Debt Service Reserve Fund, the amount available to be paid thereunder shall be less than the applicable Series Debt Service Reserve Requirement, the Authority shall cause to be deposited in the appropriate account in the Debt Service Reserve Fund, in accordance with the Grant Anticipation Resolution, Federal Transportation Funds in an amount necessary to cause the amount of moneys on deposit therein, or the amount available to be paid under any Reserve Account Credit Facility, to be equal to the applicable Series Debt Service Reserve Requirement. Amounts so deposited in the Debt Service Reserve Fund may be used to make payments to any provider of a Reserve Account Credit Facility in order to reinstate such Reserve Account Credit Facility to the applicable Series Debt Service Reserve Requirement.

Investment of Moneys

(a) The Authority and the Trustee agree that all moneys held as part of any other fund or account created hereunder shall be deposited or invested and reinvested by the Trustee, at the written direction of an Authority Representative, in Permitted Investments.

(b) Earnings and losses from the investment of moneys held in the Construction Fund or any account thereof shall be deposited into or charged against the Construction Fund, with any earnings being deposited into the Earnings Account thereof unless, and except to the extent, an Authority Representative directs the Trustee to deposit any such earnings into the Bond Payment Fund.

(c) Earnings and losses from the investment of moneys held in any account in the Debt Service Reserve Fund shall be deposited into or charged against such account, with any earnings being transferred at the direction of an Authority Representative to either the Construction Fund to pay Construction Costs or to the Bond Payment Fund to pay the Bond Payments on the Series of Bonds secured by such account.

(d) Earnings and losses from the investment of moneys held in the Bond Payment Fund or any account thereof shall, except as otherwise provided by a Supplemental Resolution, be deposited into or charged against the fund or account in which realized.

(e) Earnings and losses from the investment of moneys held in any account of the Rebate Fund or any account thereof shall, except as otherwise provided in the Tax Certificates, be deposited into or shall be charged against the account in which realized.

(f) Earnings and losses from the investment of moneys held in any Defeasance Escrow Account shall be deposited or charged as provided in the escrow agreement governing such account.

(g) The Trustee shall, when and as directed by an Authority Representative, sell and reduce to cash a sufficient amount of the investments held in any fund or account whenever the cash balance therein is insufficient to make any payment to be made therefrom.

(h) In computing the amount in any fund or account for any purpose hereunder, investments shall be valued at cost (exclusive of accrued interest) or par, whichever is less.

(Section 5.06)

Application of Federal Transportation Funds

The assignment and pledge of Federal Transportation Funds to the Trustee for the benefit of the Owners of the Bonds pursuant to the Grant Anticipation Resolution is intended to and shall constitute a first priority lien on such Federal Transportation Funds received by the Authority or the Trustee. All Federal Transportation Funds received by the Authority or the Trustee shall constitute Federal Transportation Funds which shall be subject to the assignment and lien thereof upon receipt thereof by the Authority or the Trustee, as applicable.

(i) Each Federal Fiscal Year, Federal Transportation Funds received by the Authority or the Trustee shall be deposited and used only in the manner and order of priority specified below:

(a) Deposits shall be made into the Bond Payment Fund, as summarized in this section and under the heading "Bond Payment Fund." Amounts on deposit in an account of the Bond Payment Fund shall be used only to pay Bond Payments and Redemption Price on the related Series of Bonds and for the purposes permitted by the Grant Anticipation Resolution. Moneys on deposit in the Bond Payment Fund shall be used to make the following payments or for the following purposes:

(i) Interest Component. To pay the next maturing interest payment on the Bonds;

(ii) Principal Payments. To pay the next maturing principal payment or mandatory sinking fund redemption payment on the Bonds; and

(iii) Redemption Price. To pay the Redemption Price of the Bonds next coming due pursuant to redemption prior to maturity;

(b) Federal Transportation Funds shall be deposited, as necessary, in the Debt Service Reserve Fund as required by the Grant Anticipation Resolution;

(c) Federal Transportation Funds shall be deposited, as necessary, in the Rebate Fund as required by the Grant Anticipation Resolution;

(d) Federal Transportation Funds may be used to pay or provide for debt service or any other obligations without a lien on Federal Transportation Funds equal to the lien thereon of Bonds and to fund any reserve requirement for such obligations; and

(e) Subject to the preceding paragraphs in this section and under the heading "Grant of Trust Estate," Federal Transportation Funds may be released to the Authority free and clear of the lien of the Grant Anticipation Resolution, if and to the extent (i) not required for Current Payments and not expected to be needed for any subsequent Bond Payments and (ii) as provided in a certificate of the Executive Director.

Except as summarized in this subsection (i) and for amounts held for the payment of Bonds not then deemed Outstanding, Federal Transportation Funds need not be retained for any use or in any account described in this subsection (i) in excess of the Federal Transportation Funds required for Current Payments if and to the extent such amounts are not expected to be needed for any subsequent Bond Payments.

(ii) Notwithstanding the above, in each Federal Fiscal Year, upon securing Obligation Authority sufficient to pay the Bond Payments and Program Costs coming due in the current Federal Fiscal Year, the Authority need not deposit the Federal Transportation Funds received in the manner and order of priority set forth in subsection (i) above; provided, however, that the Authority shall nevertheless comply with the provisions summarized herein under the heading "Payment of Federal Funds to Trustee"; and provided, further, that the Authority shall forward, or cause to be forwarded, in immediately available funds to the Trustee an amount of Federal Transportation Funds sufficient to pay the Program Costs coming due in such Federal Fiscal Year when such costs are due and payable. (Section 5.07)

Payment of Bond Payments and Program Costs

(a) The Authority covenants to pay, when due, solely from Federal Transportation Funds paid to the Authority or the Trustee or other funds available in the Trust Estate, the Bond Payments. Nothing in the Grant Anticipation Resolution shall be construed as obligating the Authority to pay Bond Payments from any general or other funds of the Authority, or the Commonwealth other than Federal Transportation Funds. Nothing contained in the Grant Anticipation Resolution, however, shall be constituted as prohibiting the Authority in its sole and absolute discretion, from making such payments from any other sources, to the extent legally available for that purpose.

(b) The Authority shall promptly pay, when due any Program Costs not otherwise paid. Any Program Costs payable to the Trustee shall be paid by the Authority to the Trustee on or prior to the due dates thereof. Program Costs are payable solely from Federal Transportation Funds or the proceeds of Bonds. Nothing in the Grant Anticipation Resolution shall be construed as obligating the Authority to pay Program Costs from any general or other fund of the Authority or the Commonwealth, other than Federal Transportation Funds. Nothing contained in the Grant Anticipation Resolution, however, shall be construed as prohibiting the Authority in its sole and absolute discretion, from making such payments from other sources, to the extent legally available for that purpose.

(Section 6.02)

Payment of Federal Funds to Trustee

(a) No later than three Business Days prior to each Bond Payment Date, the Authority shall forward, or cause to be forwarded, in immediately available funds to the Trustee an amount of Federal Transportation Funds equal to the Bond Payment becoming due to the Trustee for receipt by the Trustee three Business Days (or such other date prior to the Bond Payment Date if limited by FHWA) prior to the respective Bond Payment Date. The Trustee shall deposit the Bond Payments and other revenues received by the Trustee as set forth in the Grant Anticipation Resolution.

(b) If and to the extent the entire amount of the Bond Payments due on a Bond Payment Date is not paid to the Trustee as summarized in paragraph (a) of this section, the Trustee shall immediately notify the Authority by telephone confirmed by telecopier and, if and to the extent the Authority has Federal Transportation Funds that are available for such purpose, the Authority shall pay directly to the Trustee, within twenty-four hours after the receipt of such notice by telecopier, Federal Transportation Funds in an amount equal to the amount not so paid.

(Section 6.03)

Other Payments by the Authority

Nothing therein shall be interpreted to restrict the Authority's right, to the extent permitted by law, (a) to make any payment due to the Trustee summarized under the headings "Payment of Federal Funds to Trustee" and "Rebate Payments by the Authority" or any other provision thereof or any provision of any Supplemental Resolution from any Federal Transportation Funds or any other available moneys and (b) to reimburse the Authority or the fund from which such payment is made from moneys that otherwise would have been used to make such payment.

(Section 6.05)

Credit Facilities and Interest Rate Exchange Agreements

(a) The Authority may purchase or arrange for a Credit Facility with respect to any Bonds and may agree to reimburse the provider of such Credit Facility for moneys paid by the provider that are used to make Bond Payments on such Bonds, which reimbursement may be made from any moneys in the Trust Estate that are available for the payment of Bond Payments on such Bonds on a parity with or on a basis subordinate to the payment of such Bond Payments.

(b) To the extent permitted by law the Authority may purchase or arrange for an Interest Rate Exchange Agreement with respect to any Bonds and may agree to make payments to the provider of such Interest Rate Exchange Agreement, which may be made from any moneys in the Trust Estate that are available for payment of Bond Payments on such Bonds on a parity with or on a basis subordinate to the payment of such Bond Payments.

(c) All or any portion of the agreement between the Authority and the provider of any Credit Facility or Interest Rate Exchange Agreement or provisions to put into effect such an arrangement, may be included in any Supplemental Resolution or in a separate agreement between or among the Authority, the Credit Facility or Interest Rate Exchange Agreement provider and/or the Trustee, and the Trustee is hereby directed to agree to the provisions

regarding such Credit Facility or Interest Rate Exchange Agreement contained in any Supplemental Resolution or separate agreement agreed to by the Authority and the Credit Facility or Interest Rate Exchange Agreement provider.

(Section 6.06)

Tax Covenant

The Authority shall not take any action or omit to take any action with respect to the Bonds, the proceeds of the Bonds, the Trust Estate, the Construction Projects or any other funds or property of the Authority and, to the extent within its reasonable control, it will not permit any other Person to take any action or omit to take any action with respect to the Bonds, the Trust Estate, the Construction Projects or any other funds or property of the Authority if such action or omission would cause interest on any of the Bonds to be included in gross income for federal income tax purposes or to be an item of tax preference for purposes of the federal alternative minimum tax imposed on individuals and corporations (except, with respect to corporations, as such interest is required to be taken into account in determining “adjusted net book earnings” for the purpose of computing the alternative minimum tax imposed on such corporations). In furtherance of this covenant, the Authority agrees to comply with the procedures set forth in the Tax Certificates for each Series of Bonds. The covenants summarized under this heading shall remain in full force and effect notwithstanding the payment in full or defeasance of the Bonds until the date on which all of the Authority obligations in fulfilling such covenants have been met. The covenants summarized under this heading shall not, however, apply to any Series of Bonds if, at the time of issuance, the Authority intends the interest on such Series of Bonds to be subject to federal income tax or to the federal alternative minimum tax.

(Section 6.07)

Defense of Trust Estate

The Authority shall at all times, to the extent permitted by law, defend, preserve and protect its title to the Trust Estate, the grant of the Trust Estate to the Trustee under the Grant Anticipation Resolution and all the rights of the Owners under the Grant Anticipation Resolution against all claims and demands of all Persons whomsoever.

(Section 6.08)

Events of Default

Any of the following shall constitute an “Event of Default” under the Grant Anticipation Resolution:

(a) Default in the payment of any portion of the Bond Payments on, or Redemption Price of, any Bond when due.

(b) Failure by the Authority to observe and perform any covenant, condition or agreement on its part to be observed or performed under the Grant Anticipation Resolution, other than as referred to in paragraph (a), for a period of sixty days after written notice specifying such failure and requesting that it be remedied is given to the Authority by the Trustee, unless the Trustee shall agree in writing to an extension of such time prior to its expiration; provided, however, if the failure stated in the notice can be wholly cured within a period of time not materially detrimental to the rights of the owners of Bonds but cannot be cured within the applicable sixty-day period, the Trustee will not unreasonably withhold its consent to an extension of such time if corrective action is instituted by the Authority within the applicable period and diligently pursued until the failure is corrected; and provided, further, that if by reason of force majeure the Authority is unable to carry out the agreements on its part therein contained, the Authority shall not be deemed in default under this paragraph (b) during the continuance of such inability (but force majeure shall not excuse any other Event of Default).

(Section 7.01)

Remedies

(a) Upon the occurrence of any Event of Default summarized in paragraph (a) under the heading “Events of Default,” (i) the Trustee shall, if and to the extent directed by the Executive Director, transfer all or any moneys held in the Construction Fund to the Bond Payment Fund and (ii) any Owner of a Bond on which payment has not been paid when due shall have the right to institute any action permitted under Commonwealth law to enforce such payment as provided in the Grant Anticipation Resolution, as supplemented.

(b) Upon the occurrence of any Event of Default, the Trustee may by mandamus or other action or proceeding or suit at law or in equity to enforce any rights hereunder against the Authority and compel the Authority to perform or carry out its duties under the law and the agreements and covenants required to be performed by it contained therein.

(c) Upon the occurrence of any Event of Default, the Trustee may take whatever action at law or in equity may appear necessary or desirable to enforce the rights of the Owners and shall deposit any moneys received as a result of such action in the Bond Payment Fund.

(d) No right or remedy is intended to be exclusive of any other right or remedy, but each and every such right or remedy shall be cumulative and in addition to any other remedy given hereunder or now or hereafter existing at law or in equity or by statute; provided, however, that neither the Trustee nor any Owners of Bonds shall have the right to declare all Bond Payments to be immediately due and payable.

(e) A judgment requiring a payment of money entered against the Authority in connection with the Bonds and other obligations hereunder may be satisfied only from the Trust Estate.
(Section 7.02)

Use of Moneys Received from Exercise of Remedies

Moneys received by the Trustee resulting from the exercise of remedies following an Event of Default shall be deposited in the Bond Payment Fund and shall, together with other moneys in the Bond Payment Fund and other moneys available for such purpose, be applied in the following order of priority:

(a) *First*, to the payment of the reasonable and proper fees and expenses of the Trustee determined in accordance with the Grant Anticipation Resolution.

(b) *Second*, to the payment of interest due on the Bonds, including interest on past due interest on any Bond at the interest rate borne by such Bond, compounded on each Interest Payment Date. If more than one installment of interest is due on the Bonds, such installments shall be paid in the order in which they were due, with the first installment being paid first. If the amount available is insufficient to pay all of any particular installment of interest due on the Bonds (including interest on the past due interest), the amount available shall be paid ratably, based on the ratio of the amount due on each such Bond to the amount due on all such Bonds. For purposes of this paragraph, the difference between the Original Principal Amount and the Accreted Value of a Capital Appreciation Bond shall be treated as interest, the Accretion Date for a Capital Appreciation Bond shall be treated as an Interest Payment Date and the interest rate determined by straight-line interpolation between Accretion Dates shall be treated as the interest rate on a Capital Appreciation Bond.

(c) *Third*, to the payment of principal due on the Bonds. If principal is due that was to have been paid on more than one date, the amount due on the earliest dates shall be paid first. If the amount available is insufficient to pay all the principal due on any particular date, the amount available shall be paid ratably, based on the ratio of the amount due on each such Bond to the amount due on all such Bonds. For purposes of this paragraph, the Original Principal Amount of a Capital Appreciation Bond shall be treated as principal.

(Section 7.03)

Owners of Majority in Aggregate Principal Amount of Bonds May Control Proceedings

Notwithstanding any other provision thereof, the Owners of a majority in aggregate principal amount of Bonds shall always have the right, at any time, to the extent permitted by law, by an instrument or instruments in writing executed and delivered to the Trustee, to direct the time, method and place of conducting all proceedings to be taken in pursuit of remedies following an Event of Default or otherwise in connection with the enforcement of the terms of the Grant Anticipation Resolution.

(Section 7.04)

Limitations on Rights of Owners Acting Individually

No Owner shall have any right to institute any suit, action or proceeding at law or in equity for the enforcement of any remedy hereunder or for the enforcement of the terms of the Grant Anticipation Resolution, unless an Event of Default under the Grant Anticipation Resolution has occurred and the Owners of not less than a majority in aggregate principal amount of Bonds then Outstanding have made a written request to the Trustee, have offered the Trustee indemnity satisfactory to it against its costs, expenses and liabilities reasonably anticipated to be incurred, and have given the Trustee a reasonable opportunity, to take such action in its capacity as Trustee. The purpose of the preceding sentence is to assure that no Owner or Owners shall have the right to affect, disturb or prejudice the lien of the Grant Anticipation Resolution by his, her, its, or their action or to enforce any right hereunder except in the manner therein provided and that all proceedings at law or in equity shall be instituted and maintained in the manner therein provided and for the equal benefit of the Owners of all Outstanding Bonds. Nothing contained therein shall, however, affect or impair the right of any Owner to enforce the payment of the Bond Payments on or Redemption Price of any Bond at and after the date of such payment is due.

(Section 7.05)

Delay or Omission No Waiver

No delay or omission of the Trustee or of any Owner to exercise any remedy, right or power accruing upon any Event of Default or otherwise shall exhaust or impair any such remedy, right or power or be construed to be a waiver of any such Event of Default, or acquiescence therein; and every remedy, right and power given by the Grant Anticipation Resolution may be exercised from time to time and as often as may be deemed expedient.

(Section 7.08)

Discontinuance of Proceedings on Event of Default; Position of Parties Restored

In case the Trustee or any Owner shall have proceeded to enforce any right under the Grant Anticipation Resolution and such proceedings shall have been discontinued or abandoned for any reason, or shall have been determined adversely to the Trustee or such Owner, then and in every such case the Authority, the Trustee and the Owners shall be restored to their former positions and rights, and all rights, remedies and powers of the Trustee and the Owner shall continue as if no such proceedings had been taken.

(Section 7.09)

Waivers of Events of Default

The Trustee may in its discretion waive any Event of Default and its consequences hereunder, and notwithstanding anything else to the contrary contained in the Grant Anticipation Resolution, shall do so upon the written request of the Owners of a majority in aggregate principal amount of Bonds then Outstanding; provided, however, that there shall not be waived without the consent of the Owners of 100% of the Bonds any Event of Default in the payment of the Bond Payments and Redemption Price when due, unless, prior to such waiver, all such amounts (with interest on amounts past due on any Bond at the interest rate on such Bond or, in the case of a Capital Appreciation Bond, the interest rate determined by straight-line interpolation between Accretion Dates) and all expenses of the Trustee in connection with such Event of Default have been paid or provided for. In case of any such waiver, then and in every such case the Authority, the Trustee and the Owners shall be restored to their former positions and rights hereunder, but no such waiver shall extend to any subsequent or other Event of Default, or impair any right consequent thereon.

(Section 7.10)

Resignation of Trustee

(a) No resignation or removal of the Trustee and no appointment of a successor Trustee pursuant to the Bond Resolution shall become effective until the acceptance of appointment by the successor Trustee under the Bond Resolution.

(b) The Trustee may resign at any time by giving written notice thereof to the Authority. If an instrument of acceptance by a successor Trustee shall not have been delivered to the Trustee within thirty days after the giving of such notice of resignation, the retiring Trustee may petition any court of competent jurisdiction for the appointment of a successor Trustee. *(Section 8.07)*

Removal of Trustee

The Trustee may be removed at any time by an instrument or concurrent instruments in writing, signed by the holders of not less than a majority in principal amount of the Bonds hereby secured and then Outstanding, signed in person by such holders or by their attorneys, legal representatives or agents and delivered to the Trustee, the Authority and the Governmental Development Bank for Puerto Rico (such demand to be effective only when received by the Trustee, the Authority and Government Development Bank for Puerto Rico). The Trustee may also be removed at any time for any breach of trust or for acting or proceeding in violation of, or for failing to act or proceed in accordance with, any provision of the Bond Resolution with respect to the duties and obligations of the Trustee by any court of competent jurisdiction upon the application of the Authority or the holders of not less than five per centum in aggregate principal amount of the Bonds then outstanding hereunder.

(Section 8.08)

Appointment of Successor Trustee

(a) if at any time:

(i) the Trustee shall cease to be eligible under the Bond Resolution and shall fail to resign after written request therefore by the Authority or by any bondholder who shall have been a bona fide bondholder for at least six months, or

(ii) the Trustee shall become incapable of acting or shall be adjudged a bankrupt or insolvent or a receiver of the Trustee or of its property shall be appointed or any public officer shall take charge or control of the Trustee or of its property or affairs for the purpose of rehabilitation, conservation or liquidation,

then in any such case, (i) the Authority may remove the Trustee, or (ii) any bondholder who has been a bona fide bondholder for at least six months may, on behalf of himself and all others similarly situated, petition any court of competent jurisdiction for the removal of the Trustee and the appointment of a successor Trustee.

(b) If the Trustee shall resign, be removed or become incapable of acting, or if a vacancy shall occur in the office of the Trustee for any cause, the Authority shall promptly appoint a successor Trustee.

(c) If, within one year after any resignation, removal or incapability, or the occurrence of any vacancy, a successor Trustee shall be appointed by the Authority, the holders of a majority in principal amount of the Bonds then Outstanding by an instrument or concurrent instruments in writing delivered to the Authority and the Government Development Bank for Puerto Rico and the retiring Trustee, shall appoint a successor Trustee, the successor Trustee so appointed shall, forthwith upon its acceptance of such appointment, become the successor Trustee and supercede the successor Trustee appointed by the Authority. If no successor Trustee shall have been so appointed by the Authority or the bondholders and accepted appointment in the manner thereafter provided, any bondholder who has been a bona fide holder of a Bond for at least six months may, on behalf of himself and all others similarly situated, petition any court of competent jurisdiction for the appointment of a successor Trustee.

(d) The Authority shall give written notice by first-class mail, postage prepaid, of each resignation and each removal of the Trustee and each appointment of a successor Trustee to all bondholders. Each notice shall include the name and address of the principal corporate trust office of the successor Trustee.

Supplemental Resolutions Not Requiring Consent of Owners

The Authority may, without the consent of, or notice to, the Owners, adopt a Supplemental Resolution for any one or more or all of the following purposes:

(a) to add additional covenants to the covenants and agreements of the Authority set forth therein or to add to the limitations and restrictions therein, other limitations and restriction to be observed by the Authority which are not contrary to or inconsistent with the Grant Anticipation Resolution as theretofore in effect;

(b) to add additional revenues, properties or collateral to the Trust Estate;

(c) to cure any ambiguity, or to cure, correct or supplement any defect or omission or inconsistent provision contained therein, provided such action shall not adversely affect the interest of the Owners;

(d) to amend any existing provision thereof or to add additional provisions which, in the opinion of Bond Counsel, are necessary or advisable (i) to qualify, or to preserve the qualification of, the interest on any Bonds for exclusion from gross income for federal income tax purposes or for exclusion from federal alternative minimum tax; (ii) to qualify, or to preserve the qualification of, any Bonds for exemption from taxation and assessment in the Commonwealth; (iii) to qualify, or to preserve the qualification of, the Grant Anticipation Resolution or any Supplemental Resolution under the federal Trust Indenture Act of 1939; or (iv) to qualify, or preserve the qualification of, any Bonds for an exemption from registration or other limitations under the laws of any state or territory of the United States;

(e) to amend any provision thereof relating to the Rebate Fund if in the opinion of Bond Counsel, such amendment does not adversely affect the exclusion of interest on any Bonds from gross income for federal income tax purposes;

(f) to provide for or eliminate book-entry registration of any of the Bonds;

(g) to obtain or maintain a rating of the Bonds by a nationally recognized securities rating agency;

(h) to authorize the issuance of any Series of Bonds in accordance with the Grant Anticipation Resolution;

(i) to facilitate the provision of a Credit Facility or an Interest Rate Exchange Agreement in accordance with the Grant Anticipation Resolution;

(j) to facilitate the receipt or use of Federal Transportation Funds to pay Bond Payments;

(k) to establish additional funds, accounts or subaccounts necessary or useful in connection with any Supplemental Resolution authorized by any other provision summarized in this section;

(l) to make any amendment with Rating Confirmation from each Rating Agency then maintaining an uninsured, underlying rating on the Bonds, that such amendment will not, in itself, result in such uninsured, underlying rating on the Bonds following such amendment being lower than such rating on the Bonds immediately prior to such amendment,

(m) to modify any of the provisions in any other respect whatever, provided that (i) such modification shall be, and be expressed to be, effective only after all Bonds of each Series Outstanding at the date of the adoption of such Supplemental Resolution shall cease to be Outstanding and (ii) such Supplemental Resolution shall be specifically referred to in the text of all Bonds of any Series authenticated and delivered after the date of the adoption of such Supplemental Resolution and of Bonds issued in exchange therefor or in place thereof; or

(n) for any other purpose, provided that Bond Counsel has delivered a written opinion stating that the provisions of the Supplemental Resolution do not materially adversely affect the rights of the Owners of any Bonds. *(Section 9.01)*

Supplemental Resolutions Requiring Consent of Owners.

Except as expressly provided in the Grant Anticipation Resolution, the Authority may not adopt a Supplemental Resolution without the written consent of the Owners of not less than a majority in aggregate principal amount of Bonds then Outstanding; provided, however, that no Supplemental Resolution described below may be adopted without the written consent of the Owner of each Bond affected thereby:

(a) a reduction of the interest rate, Bond Payments or Redemption Price payable on any Bond, a change in the maturity date of any Bond, a change in the Original Principal Amount of any Capital Appreciation Bond, a change in any Interest Payment Date for any Current Interest Bond or any Accretion Date for any Capital Appreciation Bond or a change in the redemption provisions applicable to any Bond;

(b) the deprivation of an Owner to the lien on the Trust Estate granted in the Grant Anticipation Resolution;

(c) the creation of a priority right in the Trust Estate of another Bond over the right of the affected Bond, except as permitted therein; or

(d) a reduction in the percentage of the aggregate principal amount of the Bonds required for consent to any Supplemental Resolution.
(Section 9.02)

Conditions to Effectiveness of Supplemental Resolutions

(e) No Supplemental Resolution shall be effective until (i) it has been duly adopted by the Authority and (ii) Bond Counsel has delivered a written opinion to the effect that the Supplemental Resolution complies with the provisions of the Grant Anticipation Resolution and will not adversely affect the exclusion from gross income for federal income tax purposes of interest on, or the exemption from taxation and assessment in the Commonwealth of the income from, any Outstanding Bonds.

(f) No Supplemental Resolution adopted pursuant to the Grant Anticipation Resolution shall be effective until, in addition to the conditions set forth in paragraph (a) of this section, (i) a notice has been mailed to the Owners of the Outstanding Bonds, at the addresses last shown on the registration records of the Trustee, which notice describes the nature of the proposed Supplemental Resolution and states that copies of it are on file at the office of the Trustee for inspection by the Owners of Outstanding Bonds and (ii) Owners of the required percentage in aggregate principal amount of the Bonds have consented to the Supplemental Resolution. *Notwithstanding anything in this section or the Grant Anticipation Resolution to the contrary, the consent of the Owners of any Series of additional Bonds to be issued hereunder shall be deemed irrevocably given if the Original Purchaser thereof, whether or not for resale, consents in writing to any modification or amendment and, if such Series of additional Bonds is expected to be resold, such modification or amendment, as well as such consent, is disclosed in the official statement or other offering document pursuant to which such Series of additional Bonds is sold.*
(Section 9.03)

Discharge of Resolution

If 100% of the Bond Payments and Redemption Price due, or to become due, on all the Bonds and, all amounts payable to the United States pursuant to the Grant Anticipation Resolution, have been paid, or provision shall have been made for the payment thereof as summarized under the heading "Defeasance of Bonds" and the fees and expenses due to the Trustee and all other amounts payable thereunder have been paid, or provision for such payment shall have been made in a manner satisfactory to the Trustee, then (a) the right, title and interest of the Trustee in and to the Trust Estate shall terminate and be discharged (referred to herein as the "discharge" of the Grant Anticipation Resolution); (b) the Trustee shall transfer and convey to or upon the order of the Authority all property that was part of the Trust Estate, including but not limited to any moneys held in any fund or account hereunder, except any escrow account created as summarized under the heading "Defeasance of Bonds" hereof (which escrow account shall continue to be held in accordance with the agreement governing the administration thereof); and (c) the Trustee shall execute any instrument requested by the Authority to evidence such discharge, transfer and conveyance.

Outstanding Bonds or Bond Payments or Redemption Price or any portions thereof for the payment or redemption of which money shall have been set aside and shall be held in trust by the Trustee shall at the respective maturity or redemption dates thereof be deemed to have been paid within the meaning and with the effect expressed in the first paragraph under this heading.
(Section 10.01)

Defeasance of Bonds

All or any portion of the Outstanding Bonds or Bond Payments shall be deemed to have been paid (referred to herein as “defeased”) prior to their maturity or redemption if:

(a) the defeased Bonds are to be redeemed prior to their maturity, an Authority Representative has irrevocably instructed the Trustee to give notice of redemption of such Bonds in accordance with the Grant Anticipation Resolution and any applicable Supplemental Resolution;

(b) there has been deposited in trust in a Defeasance Escrow Account either moneys in an amount which shall be sufficient, or Defeasance Securities, the principal of and the interest on which when due, and without any reinvestment thereof will provide moneys which, together with the moneys, if any, deposited into or held in the Defeasance Escrow Account, shall be sufficient to pay when due the Bond Payments or Redemption Price, as applicable, due and to become due on the defeased Bonds on and prior to the redemption date or maturity date thereof, as the case may be; and

(c) a certified public accountant or other nationally recognized expert respecting verification of escrows has delivered a verification report verifying the deposit described in paragraph (ii) of this section.

The Defeasance Securities and moneys deposited in a Defeasance Escrow Account summarized in this section and the principal and interest payments on such Defeasance Securities shall not be withdrawn or used for any purpose other than, and shall be held in trust solely for, the payment of the Bond Payments on and Redemption Price of the defeased Bonds; provided, however, that (i) any moneys received from principal and interest payments on such Defeasance Securities that are not required to pay the Bond Payments on or Redemption Price of the defeased Bonds on the date of receipt shall, to the extent practicable, be reinvested in Defeasance Securities maturing at the times and in amounts sufficient to pay when due the Bond Payments on and Redemption Price to become due on the defeased Bonds on or prior to the redemption date or maturity date thereof, as the case may be; and (ii) any moneys or Defeasance Securities may be withdrawn from a Defeasance Escrow Account if (A) the moneys and Defeasance Securities that are on deposit in the Defeasance Escrow Account, including any moneys or Defeasance Securities that are substituted for the moneys or Defeasance Securities that are withdrawn from the Defeasance Escrow Account, satisfy the conditions stated in paragraph (b) of this section, (B) a verification report is delivered that complies with paragraph (c) of this section and (C) an opinion of Bond Counsel is delivered to the effect that such withdrawal or substitution complies with this section and will not of itself adversely affect the federal tax status of interest on either the related Refunding Bonds or the Bonds being refunded.

Any Bonds that are defeased as summarized in this section shall no longer be secured by or entitled to any right, title or interest in or to the Trust Estate, and the Bond Payments on and Redemption Price thereof shall be paid solely from the Defeasance Securities and money held in the Defeasance Escrow Account.

(Section 10.02)

Defeasance of Less than all Bonds of a Particular Series or Maturity.

If less than all the Bonds of any particular Series, any particular maturity of any Series or any particular interest rate within a maturity of a Series are defeased, the Trustee shall institute or cause to be instituted a system to preserve the identity of the individual Bonds or portions thereof that are defeased, regardless of changes in Bond numbers attributable to transfers and exchanges of Bonds.

(Section 10.03)

SUMMARY OF CERTAIN PROVISIONS OF THE 1998 RESOLUTION

The following are brief summaries of certain provisions of the 1998 Resolution. Such statements do not purport to be complete and reference is made to the 1998 Resolution, copies of which are available from the Authority or the 1998 Fiscal Agent. For the purposes of this summary, the term “senior bonds” shall refer to Senior Transportation Revenue Bonds; the term “Subordinated Transportation Revenue Bonds” shall refer to “Subordinated Transportation Revenue Bonds”; and the term “bonds” shall refer to “Transportation Revenue Bonds”; as those terms are used in this Official Statement.

Definition of Certain Terms

“Accreted Value” means, with respect to any Capital Appreciation Bond or Capital Appreciation and Income Bond, an amount equal to the principal amount of such Bond on the date of original issuance plus the interest accrued on such Bond from the date of original issuance to the date of computation or the Interest Commencement Date, as the case may be, such interest to accrue at the rate set forth in the resolution providing for the issuance of said Bond, but not exceeding the maximum rate permitted by law, compounded periodically at the times provided for in such resolution.

“Capital Appreciation Bonds” means any bonds as to which interest is compounded periodically on each of the applicable 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 said resolution, and which may be either serial bonds or term bonds.

“Capital Appreciation and Income Bonds” means any bonds as to which accruing interest is not paid prior to the interest payment date immediately following the Interest Commencement Date specified in the resolution authorizing such Bonds and the interest on which 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.

“Cost of Transportation Facilities” or “cost of Transportation Facilities” means the cost of acquisition and construction of Transportation Facilities and the cost of all labor, materials, machinery and equipment, the cost of all lands, property, rights, easements and franchises acquired, interest prior to and during construction and for any additional period authorized by law if so provided by, and subject to any limitations in, the resolution authorizing the issuance of a Series of bonds, the cost of engineering and legal services, preliminary surveys, or plans and specifications, expenses of administration properly chargeable to such construction or acquisition, legal, architectural and engineering expenses and fees, the cost of audits and of preparing and issuing the bonds, fees and expenses of the 1998 Fiscal Agent and consultants, financing charges, taxes or other governmental charges lawfully assessed during construction, claims arising in connection with construction, premiums on insurance in connection with construction, premiums for bond insurance, interest rate insurance or insurance assuring availability of the amounts required to be on deposit in the Senior Bond Reserve Account or any account in the Subordinated Bond Reserve Fund, any amounts required to be deposited in the Senior Bond Reserve Account or any account in the Subordinated Bond Reserve Fund, initial set-up fees and annual fees for any Credit Facility or Liquidity Facility and tender agent fees and fees payable for remarketing bonds supported by any Credit Facility or Liquidity Facility during such period, as may be specified in the resolution authorizing the issuance of such Series of bonds and all other items of expense not elsewhere in this definition specified, incident to the financing or construction of any Transportation Facilities and the placing of the same in operation.

“Existing Tax and Fee Revenues” means (1) the proceeds of the sixteen cents a gallon tax imposed on gasoline and one-half of the eight cents per gallon tax imposed on gas oil and diesel oil imposed by Subtitle B of Act No. 120, approved October 31, 1994, as amended, and allocated to the Authority by Act No. 223 of November 30, 1995, as amended, and by said Act’s predecessor statutes and (2) the proceeds of the \$15 increase per vehicle of annual motor vehicle license fees imposed by the Commonwealth and allocated to the Authority by Act. No. 9, approved August 12, 1982.

“Existing Toll Facilities Revenues” means the tolls or other charges imposed by the Authority for the use of any Traffic Facilities financed in whole or in part by the issuance of 1968 Resolution Bonds, including any extensions, betterments or improvements to such Facilities however financed or otherwise paid for.

“Fiscal Year” means 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 Authority.

“Government Obligations” means (i) direct obligations of, or obligations the principal of and the interest on which are unconditionally guaranteed by, the United States Government, (ii) bonds, debentures or notes issued by any of the following Federal Agencies: Banks for Cooperatives, Federal Intermediate Credit Banks, Federal Home Loan Banks, Export-Import Bank of the United States, Government National Mortgage Association or Federal Land Banks, (iii) obligations issued or guaranteed by an agency of the United States of America or person controlled or supervised by and acting as an instrumentality of the United States of America pursuant to authority granted by the Congress, (iv) municipal obligations, the payment of the principal of and interest and redemption premium, if any, on which are irrevocably secured by obligations described in clause (i) of this definition and which obligations are not subject to redemption prior to the date on which the proceeds attributable to the principal of the obligations are to be used and have been deposited in an escrow account which is irrevocably pledged to the payment of the principal of and interest and redemption premium, if any, on such municipal obligations, and (v) evidences of ownership of proportionate interests in future interest or principal payments on obligations specified in clauses (i), (ii), (iii) and (iv) of this definition held by a bank (including the 1998 Fiscal Agent) or trust company as custodian and which underlying obligations are not available to satisfy any claim of the custodian or any person claiming through the custodian or to whom the custodian may be obligated.

“Interest Commencement Date” means, with respect to any particular Capital Appreciation and Income Bonds, the date specified in the resolution providing for the issuance of such bonds after which interest accruing on such bonds shall be payable on a periodic basis prior to maturity, with the first such payment date being the applicable interest payment date immediately succeeding such Interest Commencement Date.

“Investment Obligations” means:

(i) Government Obligations,

(ii) direct and general obligations of any state or territory of the United States of America to the payment of the principal of and interest on which the full faith and credit of such state or territory is pledged, provided that such obligations are rated, on the date of investment therein, in any of the three highest rating categories (without regard to any gradations within any such category) by both Moody’s or any successors thereto and S&P or any successors thereto,

(iii) bankers’ acceptances, certificates of deposit or time deposits of any bank or national banking association (including the 1998 Fiscal Agent), trust company or savings and loan association (including any investment in pools of such bankers’ acceptances, certificates of deposit or time deposits), which to the extent that such obligations are not insured by the Federal Deposit Insurance Corporation, are either (A) issued by a bank, trust company or savings and loan association having a combined capital and surplus aggregating at least \$50,000,000 or (B) collateralized at all times by such securities as are described in clauses (i) or (ii) above, having a market value at least equal to the principal amount of such bankers’ acceptances, certificates of deposit or time deposits (or portion thereof not so insured); provided that the 1998 Fiscal Agent has a perfected first security interest in the collateral and that such collateral is held free and clear of claims by third parties,

(iv) any repurchase, reverse repurchase or investment agreement with any bank or trust company organized under the laws of any state of the United States or the Commonwealth or any national banking association (including the 1998 Fiscal Agent), insurance company, or government bond dealer reporting to, trading with, and recognized as a primary dealer by the Federal Reserve Bank of New York and a member of the Security Investors Protection Corporation, which agreement is secured by any one or more of the securities described in clauses

(i) or (ii) above, provided that the 1998 Fiscal Agent has a perfected first security interest in the collateral and that such collateral is held free and clear of claims by third parties,

(v) obligations, whether or not insured, issued by any state or territory of the United States, or any political subdivision, agency or instrumentality thereof which are rated, on the date of investment therein, in one of the three highest rating categories (without regard to any gradations within any such category) by both Moody's or any successors thereto and S&P or any successors thereto,

(vi) participating shares in a mutual fund or investment pool for local government investment; provided that the investments of such mutual fund or investment pool are rated in one of the three highest rating categories (without regard to any gradations within any such category) by both Moody's or any successors thereto, and S&P or any successors thereto,

(vii) (1) shares of stock in a corporation rated in the highest rating category by Moody's or any successors thereto and S&P or any successors thereto (without regard to gradations within such category) that (A) is a regulated investment company within the meaning of Section 851(a) of the Internal Revenue Code of 1986, as amended, and, meets the requirements of Section 852(a) of said Code for the calendar year; (B) invests all of its assets in obligations described in clauses (i) and (ii) above; and (C) has at least 98% of (I) its gross income derived from interest on, or gain from the sale of or other disposition of, such obligations or (II) the weighted average of its assets is represented by investments in such obligations or (2) money market accounts of the 1998 Fiscal Agent or any state or federally chartered bank, banking association, trust company or subsidiary trust company that is rated or whose parent state bank is rated in the highest short-term rating category or in one of the two highest long-term rating categories by Moody's or any successors thereto and S&P or any successors thereto (without regard to any gradations within such category), and

(viii) any other obligations permitted under the laws of the Commonwealth which are rated, or which are issued by issuers which are rated, on the date of investment therein, in any of the three highest rating categories (without regard to any gradations within any such category) by both Moody's or any successors thereto and S&P or any successors thereto, or which are collateralized by such Investment Obligations.

"Mass Transit Facilities" means the equipment, omnibus facilities, rail facilities, and real property, constituting or to constitute part of, or used or reasonably anticipated to be used in connection with the operation of, any mass transportation facility or system, and related services operated by the Authority directly or by contract, lease or other arrangements entered into by the Authority, as the foregoing may from time to time be augmented or diminished.

"1968 Resolution Bonds" means all bonds issued under the 1968 Resolution.

"Principal and Interest Requirements" means for any fiscal year, as applied to the bonds of any Series issued under the provisions of the 1998 Resolution, the sum of:

(i) the amount required to pay the interest on all outstanding bonds of such Series which is payable after July 31 in such fiscal year and on or before July 31 in the following fiscal year,

(ii) the amount required to pay the principal of the serial bonds of such Series then outstanding which is payable after July 31 in such fiscal year and on or before July 31 in the following fiscal year, and

(iii) the Amortization Requirement for the term bonds of such Series for such fiscal year.

The following rules shall apply in determining the amount of the Principal and Interest Requirements for any period:

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

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

(c) the interest rate on bonds issued with a variable, adjustable, convertible or similar rate of interest shall be the greater of (A)(1) the average rate of interest on such bonds for the preceding twelve months or such shorter period that such bonds shall have been outstanding, or (2) if such bonds had not been outstanding prior to the date of calculation, the rate of interest on such bonds on the date of calculation and (B) the lesser of the maximum rate then permitted by law and the maximum rate permitted on such bonds by the resolution authorizing the issuance thereof; provided, however, that if the Authority has notified the 1998 Fiscal Agent that a Swap agreement is in effect in respect of such bonds, then for all purposes of this paragraph, except for the purpose of determining the required deposits to the Senior Bond Sinking Fund or the Subordinated Bond Sinking Fund described in "Sinking Funds" below, the interest rate on such bonds shall be the Swap rate under such Swap agreement; and if such Swap rate is a variable rate, the interest rate on such bonds (except for the purpose specified above in this paragraph) shall be the average Swap rate for the preceding twelve months or such shorter period that the Swap agreement has been in effect, or if such Swap agreement has not been in effect prior to the date of calculation, the Swap rate on the date of calculation;

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

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

(f) in the case of bonds (A) which are expected to be repaid from the proceeds of bonds or other indebtedness or (B) on which interest is payable periodically and for which twenty-five percent (25%) or more of the principal amount matures during any one year and for which no Amortization Requirements have been established, the debt service requirements of the bonds may be excluded and in lieu thereof the bonds shall be treated, for purposes of the computation of Principal and Interest Requirements, as debt securities having a comparable federal tax status as such bonds, maturing in substantially equal annual payments of principal and interest over a period of not more than thirty (30) years from the date of issuance thereof, bearing interest at a fixed rate per annum equal to the average interest rate per annum for such debt securities issued on the date of issuance of the bonds and issued by issuers having a credit rating, issued by Moody's or any successors thereto or S&P or any successors thereto, comparable to that of the Authority, as shown by a certificate of an underwriting or investment banking firm experienced in marketing such securities; and

(g) if all or a portion of the principal of or interest on a Series of bonds is payable from moneys irrevocably set aside or deposited for such purpose, together with projected earnings thereon to the extent such earnings are projected to be from Investment Obligations irrevocably set aside or deposited for such purpose on the date of computation, such principal or interest shall not be included in determining Principal and Interest Requirements; provided that the above computation shall be supported by a verification report from a nationally recognized independent certified public accountant as to the sufficiency of such moneys set aside and projected earnings.

“Reserve Account Insurance Policy” means an insurance policy, surety bond or other acceptable evidence of insurance, which policy, bond or other evidence of insurance constitutes an unconditional senior obligation of a municipal bond insurer whose policy or bond results in the rating of municipal obligations secured by such policy or bond, at the time of deposit to the credit of the Reserve Account, in either of the two highest rating categories (without regard to any gradations within either such category) of either Moody’s or any successors thereto or S&P or any successors thereto.

“Reserve Account Letter of Credit” means an irrevocable, transferable letter of credit, which letter of credit constitutes an unconditional senior obligation of a banking association, bank or trust company or branch thereof whose letter of credit results in the rating of municipal obligations secured by such letter of credit, at the time of deposit to the credit of the Reserve Account, in either of the two highest categories (without regard to any gradations within either such category) of either Moody’s or any successors thereto or S&P or any successors thereto and any agreement of the type referred to in the definition of “Subordinated Reserve Requirement.”

“Revenues” means all moneys received by the Authority on account of the crude oil tax allocated to the Authority by Act No. 34, approved July 16, 1997, as amended, all Existing Tax and Fee Revenues upon the repeal and cancellation of the 1968 Resolution, any tolls or other charges imposed by the Authority for the use of any of the Toll Facilities other than Existing Toll Facilities Revenues received by the Authority prior to the repeal and cancellation of the 1968 Resolution, the proceeds of any other taxes, fees or charges which the Legislature of Puerto Rico may hereafter allocate to the Authority and expressly authorize the Authority to pledge to the payment of the principal of and interest on bonds or other obligations of the Authority and which are pledged by the Authority to the payment of the principal of and interest on bonds or other obligations issued under the provisions of the 1998 Resolution, and investment earnings on deposits to the credit of funds and accounts established under the 1998 Resolution, except for the 1998 Construction Fund.

“Senior Reserve Requirement” with respect to the senior bonds means the lesser of (i) the maximum Principal and Interest Requirements for any fiscal year on account of the outstanding senior bonds and (ii) ten (10%) percent of the original principal amount of each Series of senior bonds outstanding determined on the basis of their initial offering prices to the public.

“Subordinated Reserve Requirement” with respect to any Series of Subordinated Transportation Revenue Bonds means that amount fixed from time to time by resolution of the Authority as the amount required to be held to the credit of a separate account in the Subordinated Bond Reserve Fund corresponding to such Series. For purposes of determining the amount on deposit to the credit of any such separate account, any agreement between the 1998 Fiscal Agent and a financial institution serving as the depository institution of the Commonwealth state infrastructure bank (or other similar fund) created by virtue of Section 350 of the National Highway System Designation Act of 1995, as amended (23 U.S.C. Section 101), or any similar federal legislation, pursuant to which agreement such depository institution irrevocably agrees to provide funds to the 1998 Fiscal Agent for deposit to the credit of any separate account in the Subordinated Bond Reserve Fund shall be treated as satisfying the applicable Subordinated Reserve Requirement to the extent of the maximum amount of funds so available to be provided to the 1998 Fiscal Agent for deposit to the credit of such separate account.

“Swap agreement” means an agreement between the Authority and a Swap party whereby the Swap party agrees to pay to the Authority amounts calculated on the basis of all or a portion of the interest on bonds issued under the 1998 Resolution with a variable, adjustable, convertible or similar rate of interest at or prior to the times such interest is due and payable in consideration of the Authority’s payment to the Swap party of amounts set forth in the Swap agreement.

“Swap party” means a person who is party to a Swap agreement and whose senior obligations are rated at the time of the execution and delivery of such Swap agreement in one of the three highest rating categories (without regard to any gradations within any such category) by (i) S&P or its successors and (ii) Moody’s or its successors.

“Swap rate” means the fixed rate per annum on the principal amount of bonds issued under the 1998 Resolution with a variable, adjustable, convertible or similar rate of interest covered by a Swap

agreement equal to the percentage derived by dividing (i) the sum of the amounts in the last twelve months paid by the Authority in respect of interest on such bonds and to the Swap party less the amount paid to the Authority by the Swap party by (ii) such principal amount of bonds; provided, however, that if such Swap agreement has been in effect for less than twelve months, such percentage shall be multiplied by 360 divided by the number of days between the effective date of such Swap agreement and the date of calculation determined on the basis of 30-day months;

“Toll Facilities” means any Traffic Facilities for the use of which the Authority imposes tolls.

“Traffic Facilities” means any of the following facilities for which 1968 Resolution Bonds or bonds or other obligations shall be issued by the Authority under the provisions of the 1998 Resolution the cost of which facilities paid from the proceeds of such bonds or other obligations shall not have been reimbursed to the Authority from funds not encumbered by the 1998 Resolution or the 1968 Resolution:

(i) roads, avenues, streets, thoroughfares, speedways, bridges, tunnels, channels, stations, terminals and any other land or water facilities necessary or desirable in connection with the movement of persons, freight, vehicles or vessels;

(ii) parking lots and structures and other facilities necessary or desirable in connection with parking, loading or unloading of all kinds of vehicles or vessels; and

(iii) all property rights, easements, and interests therein necessary or desirable for the construction, maintenance, control, operation or development of such traffic facilities.

“Transportation Engineers” means the engineer or engineers or engineering firms or corporations at the time employed by the Authority under the provisions of the 1998 Resolution.

“Transportation Facilities” means all Traffic Facilities, all Mass Transit Facilities, and any other highway, road, transportation or other facilities or undertakings permitted from time to time by the enabling act for which bonds or other obligations shall be issued by the Authority under the provisions of the 1998 Resolution the cost of which facilities paid from the proceeds of such bonds or other obligations shall not have been reimbursed to the Authority from funds not encumbered by the 1998 Resolution.

Sinking Funds

The 1998 Resolution creates the “Puerto Rico Highways and Transportation Authority Transportation Revenue Bonds Interest and Sinking Fund” (the “Senior Bond Sinking Fund”). The “Senior Bond Service Account”, “Senior Bond Redemption Account” and “Senior Bond Reserve Account” are created within the Senior Bond Sinking Fund. (Section 401).

The 1998 Resolution also creates the “Puerto Rico Highways and Transportation Authority Subordinated Transportation Revenue Bonds Interest and Sinking Fund” (the “Subordinated Bond Sinking Fund”). The “Subordinated Bond Service Account,” and “Subordinated Bond Redemption Account” are created within the Subordinated Bond Sinking Fund. (Section 401).

The 1998 Resolution also creates the “Puerto Rico Highways and Transportation Authority Subordinated Transportation Revenue Bonds Reserve Fund” (the “Subordinated Bond Reserve Fund”). The Authority may establish one or more accounts in the Subordinated Bond Reserve Fund to correspond to Series of Subordinated Transportation Revenue Bonds with different Subordinated Reserve Requirements. (Section 401).

The 1998 Resolution also creates the “Puerto Rico Highways and Transportation Authority Transportation Revenue Fund” (the “Revenue Fund”). The Authority has covenanted that all Revenues (except investment earnings on deposits to the credit of the funds and accounts established under the 1998 Resolution) will be deposited when received to the credit of the Revenue Fund. Until the outstanding 1968 Resolution Bonds have been paid or provision has been made for their payment and the repeal and cancellation of the 1968 Resolution, the Authority shall on or before the last day of the month during which the 2003 Bonds shall be issued and on or before the 25th day of each month thereafter withdraw from the 1968 Construction Fund and transfer to the credit of the Revenue Fund all unencumbered moneys held for

the credit of the 1968 Construction Fund (herein “unencumbered 1968 Construction Fund moneys”), such transfer to be made on the books of the Authority as of the close of the preceding month. (Section 401).

The moneys in each Fund or Account are held by the 1998 Fiscal Agent in trust and, pending application, are subject to a lien in favor of the holders of the outstanding bonds and for the further security of such holders until paid out or transferred as provided in the 1998 Resolution. (Section 401).

All Revenues (other than investment earnings), Excess 1968 Resolution Revenues and any other funds of the Commonwealth allocated to the Authority for the payment of principal of and interest on any bonds, are withdrawn monthly from the Revenue Fund and deposited with the 1998 Fiscal Agent as follows:

(1) to the Senior Bond Service Account, an amount equal to 1/6th of the amount of interest payable on all senior bonds of each Series on the next succeeding interest payment date and an amount equal to 1/12th of the next maturing installment of principal of any serial bonds of such Series until the amount in the Senior Bond Service Account equals the amount of interest payable on such interest payment date and the amount of such principal installment; but the amount so deposited on account of the interest in each month after the delivery of the senior bonds of any Series up to and including the month immediately preceding the first interest payment date thereafter of the bonds of such Series shall be that amount which when multiplied by the number of such deposits will be equal to the amount of interest payable on such bonds on such first interest payment date less the amount of any accrued interest paid on such bonds and deposited to the credit of the Senior Bond Service Account;

(2) to the Senior Bond Redemption Account, an amount equal to 1/12th of the Amortization Requirement for such fiscal year for the term bonds of each Series of senior bonds then outstanding plus an amount equal to 1/12th of the premium, if any, which would be payable on the first redemption date in the following fiscal year on a like principal amount of bonds if such principal amount of bonds should be redeemed prior to their maturity from moneys in the Senior Bond Sinking Fund;

(3) to the Senior Bond Reserve Account, such amount as is required to make the amount deposited to the credit of said Account in the then current fiscal year at least equal to 20% of the Senior Reserve Requirement; but such deposits shall only be made to the extent necessary to make the amount then in the Senior Bond Reserve Account equal to the Senior Reserve Requirement; and provided, further, that in the event of an increase in the Senior Reserve Requirement due to the issuance of additional Series of senior bonds, such increase will be funded by deposits in each of the five (5) years, commencing in the fiscal year in which such additional Series of senior bonds is issued, of 20% of such increase in the Senior Reserve Requirement;

(4) to the Subordinated Bond Service Account, an amount equal to one-sixth (1/6) of the amount of interest payable on all Subordinated Transportation Revenue Bonds of each Series on the interest payment date next succeeding and an amount equal to one-twelfth (1/12) of the next maturing installment of principal of such serial bonds of such Series until the amount in the Subordinated Bond Service Account equals the amount of interest payable on such interest payment date and the amount of such principal installment; but the amount so deposited on account of interest in each month after the delivery of the Subordinated Transportation Revenue Bonds of any Series up to and including the month immediately preceding the first interest payment date thereafter of the bonds of such Series shall be that amount which when multiplied by the number of such deposits will be equal to the amount of interest payable on such bonds on such first interest payment date less the amount of any accrued interest paid on such bonds and deposited with the 1998 Fiscal Agent to the credit of the Subordinated Bond Service Account;

(5) to the Subordinated Bond Redemption Account, an amount equal to one-twelfth (1/12) of the Amortization Requirement for such fiscal year for the term bonds of each Series of Subordinated Transportation Revenue Bonds then outstanding plus one-twelfth (1/12) of the premium, if any, which would be payable on the first redemption date in the following fiscal year on a like principal amount of bonds if such principal amount of bonds should be redeemed prior to their maturity from moneys in the Subordinated Bond Sinking Fund;

(6) to each separate account within the Subordinated Bond Reserve Fund, such amount, if any, of any balance remaining after making the deposits described under paragraph (1) through (5) above

(allocated pro rata to each account on the basis of the corresponding Subordinated Reserve Requirements) at least equal to the respective deposit requirements corresponding to each such account established by the Authority; but no such deposits to any such account described under this paragraph will be made in any month if the amount then to the credit of such account shall be equal to the applicable Subordinated Reserve Requirement; and provided, further, that notwithstanding the above, in the event that any Subordinated Reserve Requirement increases on account of the issuance of additional Series of Subordinated Transportation Revenue Bonds, the Authority may provide for equal annual deposits as will ensure that the applicable Subordinated Reserve Requirement will be met not earlier than the end of a five year period following the issuance of such Series of Subordinated Transportation Revenue Bonds; and

(7) the balance remaining after making the deposits referred to above shall be deposited to the credit of the 1998 Construction Fund for use by the Authority for any of its authorized purposes, subject to the provisions of Sections 604 and 605 of the 1998 Resolution. (Section 401).

The requirements specified in paragraphs (1) through (6) above are cumulative. (Section 401).

The Authority further covenants that any other funds which it receives from the Commonwealth or any other source to make up any deficiencies in the amounts needed to pay the principal of and interest on any bonds issued under the provisions of the 1968 Resolution and the 1998 Resolution will be applied for such purpose first to make up any deficiencies in the amounts needed to pay the principal and interest on any 1968 Resolution Bonds and then to make up any such deficiencies needed to pay such principal of and interest on the senior bonds and then the Subordinated Transportation Revenue Bonds. (Section 401).

When the 1968 Resolution is repealed and cancelled, all moneys (other than those held for the redemption or payment of 1968 Resolution Bonds), including obligations purchased as an investment of such moneys will be withdrawn from the 1968 Construction Fund and 1968 Sinking Fund and deposited into the Revenue Fund. (Section 402).

Moneys in the Senior Bond Redemption Account shall be applied to the retirement of senior bonds as follows:

(a) Subject to the provisions of paragraph (c) below, the 1998 Fiscal Agent shall endeavor to purchase outstanding senior bonds, whether or not such bonds shall then be subject to redemption, at the most advantageous price obtainable with reasonable diligence, having regard to interest rate and price, such price not to exceed the principal of such bonds plus the amount of the premium, if any, which would be payable on the next redemption date to the holders of such bonds if such bonds should be called for redemption on such date from moneys in the Senior Bond Sinking Fund. The 1998 Fiscal Agent shall pay the interest accrued on such bonds to the date of delivery thereof from the Senior Bond Service Account and the purchase price from the Senior Bond Redemption Account, but no such purchase shall be made within 45 days next preceding any interest payment date on which such bonds are subject to redemption except from moneys in excess of the amounts set aside or deposited for the redemption of senior bonds.

(b) Subject to the provisions of paragraph (c) below, the 1998 Fiscal Agent shall call for redemption on each date on which senior bonds are subject to redemption from moneys in the Senior Bond Sinking Fund on the forty-fifth day prior to such redemption date such amount of senior bonds then subject to redemption as, with the redemption premium, if any, will exhaust the Senior Bond Redemption Account as nearly as may be; but not less than \$50,000 principal amount of senior bonds shall be called for redemption at any one time.

(c) Moneys in the Senior Bond Redemption Account shall be applied to the purchase or redemption of senior bonds in the following order:

First, the term bonds of each Series of senior bonds, if any, in the order of their issuance, to the extent of the Amortization Requirement, if any, of the then current fiscal year for such term bonds and any deficiency in preceding fiscal years in the purchase or redemption of such term bonds under the provisions of this subdivision; but if none of the term bonds of a Series of senior bonds shall be subject to redemption from moneys in the Senior Bond Sinking Fund and if the 1998 Fiscal Agent shall at any time be unable to exhaust the moneys applicable to the bonds of any such Series in the purchase of such bonds under the provisions of paragraph (a) above, such moneys or the balance of such moneys, as the case may be, shall be

retained in the Senior Bond Redemption Account and, as soon as it is feasible, applied to the retirement of the bonds of such Series;

Second, to the purchase of any outstanding senior bonds, whether or not such bonds shall then be subject to redemption, in accordance with the provisions of paragraph (a) above;

Third, term bonds of each Series of senior bonds in proportion (as nearly as practicable) to the aggregate principal amount of the bonds of each such Series originally issued; and

Fourth, after the retirement of all term senior bonds, any balance shall be applied to the retirement of serial senior bonds of each Series in proportion to the aggregate principal amount of each such Series originally issued.

All expenses in connection with such purchase or redemption shall be paid from the 1998 Construction Fund. (Section 404).

Moneys in the Senior Bond Reserve Account shall be used for the purpose of paying interest on the senior bonds and maturing principal of serial senior bonds whenever and to the extent that the moneys held for the credit of the Senior Bond Service Account shall be insufficient for such purpose and thereafter for the purpose of making deposits to the credit of the Senior Bond Redemption Account whenever and to the extent that the Revenues or other moneys deposited to the credit of the Revenue Fund are insufficient for such purpose; but prior to making any withdrawal from the Senior Bond Reserve Account, the 1998 Fiscal Agent shall withdraw first available unencumbered moneys in the 1998 Construction Fund and then any moneys held to the credit of the Subordinated Bond Redemption Account and then any moneys held to the credit of the Subordinated Bond Service Account in respect of the principal of any Subordinated Transportation Revenue Bonds and finally any other moneys held to the credit of the Subordinated Bond Service Account and transfer all such money so withdrawn to the Senior Bond Service Account or the Senior Bond Redemption Account in the respective amounts necessary to cure any insufficiencies in said Accounts. (Sections 405, 409 and 411).

Moneys held in the Subordinated Bond Service Account and Subordinated Bond Redemption Account will be applied to the payment of Subordinated Transportation Revenue Bonds' debt service in the same manner as moneys in the Senior Bond Service Account and the Senior Bond Redemption Account are applied to the payment of senior bonds' debt service, subject to the provisions employing moneys in the Subordinated Bond Sinking Fund to address insufficiencies in the Senior Bond Sinking Fund described in the previous paragraph. (Sections 406, 407, 411).

Money held for the credit of each account in the Subordinated Bond Reserve Fund shall be used for the purpose of paying interest on each Series of Subordinated Transportation Revenue Bonds and maturing principal of serial Subordinated Transportation Revenue Bonds of each such Series to which such account relates whenever and to the extent that the moneys held for the credit of the Subordinated Bond Service Account shall be insufficient for such purpose and thereafter for the purpose of making deposits to the credit of the Subordinated Bond Redemption Account whenever and to the extent that the Revenues or other moneys deposited to the credit of the Revenue Fund are insufficient for such purpose. (Section 408).

The Authority may deposit into the Senior Bond Reserve Account or any account in the Subordinated Bond Reserve Fund, a Reserve Account Insurance Policy or a Reserve Account Letter of Credit in an amount equal to all or a portion of the applicable reserve requirement, which Reserve Account Insurance Policy or Reserve Account Letter of Credit shall be payable or available to be drawn upon, as the case may be (upon the giving of notice as required thereunder), on any interest payment date on which a deficiency exists in the applicable reserve account which cannot be otherwise cured. If a disbursement is made under the Reserve Account Insurance Policy or the Reserve Account Letter of Credit, the Authority shall be obligated either to reinstate the limits of such Reserve Account Insurance Policy or Reserve Account Letter of Credit following such disbursement, or to deposit into the Senior Bond Reserve Account or any account in the Subordinated Bond Reserve Fund from Revenues, funds in the amount of the disbursement made under such Reserve Account Insurance Policy or Reserve Account Letter of Credit, and any moneys held in any such reserve account may be applied for such purpose. (Sections 401, 405, 408).

1998 Construction Fund

Before any payment or withdrawal shall be made from moneys in the 1998 Construction Fund there shall be filed with the 1998 Fiscal Agent a certificate signed by a designated officer of the Authority setting forth the amount of money to be so disbursed and stating that such money will be used to pay the costs of constructing Transportation Facilities or for other authorized purposes. Upon receipt of such certificate the 1998 Fiscal Agent shall withdraw from the 1998 Construction Fund and deposit to the credit of a special checking account in its commercial department in the name of the Authority the amount so specified in such certificate. The 1998 Fiscal Agent shall also at any time at the written direction of the Authority transfer any part of the unencumbered moneys in the 1998 Construction Fund to the credit of any account in the Senior Bond Sinking Fund and shall make the transfers to the Senior Bond Service Account and Senior Bond Redemption Account to cure deposit deficiencies therein as described above. (Section 409).

Defeasance

If all the outstanding bonds shall have been paid or deemed to have been paid as provided below, then and in that case the rights, title and interest of the 1998 Fiscal Agent under the 1998 Resolution shall cease, terminate and become void, and such bonds shall cease to be entitled to any lien, benefit or security under the 1998 Resolution. In such event, the Authority shall repeal and cancel the 1998 Resolution and may apply any surplus in the Senior Bond Sinking Fund, Subordinated Bond Sinking Fund and all balances remaining in any other fund and accounts other than moneys held for the redemption or payment of bonds to any lawful purposes of the Authority.

Any outstanding bond shall be deemed to have been paid within the meaning and with the effect expressed in the 1998 Resolution when the whole amount of the principal of, redemption premium, if any, and interest on such bond shall have been paid or duly provided for and the conditions set forth in clause (c) below have been satisfied, when (a) in case such bond has been called for redemption or the Authority shall have given to the 1998 Fiscal Agent irrevocable instructions to call such bond for redemption, (b) there shall have been deposited with the 1998 Fiscal Agent Government Obligations the principal of and interest on which are sufficient, without any reinvestment thereof, 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 (c) if such bond does not mature and is not to be redeemed within the next succeeding sixty (60) days, the Authority shall have given the 1998 Fiscal Agent 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 required by clause (b) of this paragraph has been made with the 1998 Fiscal Agent or other appropriate 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 1998 Resolution 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.

Neither the moneys nor Government Obligations deposited with the 1998 Fiscal Agent nor principal or interest payments on any such obligations shall be withdrawn or used for any purpose other than, and shall be held in trust for, the payment of the principal of and redemption premium, if any, and interest on the bonds which have been defeased.

As to Variable Rate Bonds, the amount required for the interest thereon shall be calculated at the maximum rate permitted by the terms of the provisions of the resolution which authorized the issuance of such Variable Rate Bonds. (Section 1001).

Issuance of Additional Bonds

Senior bonds may be issued under and secured by the 1998 Resolution, subject to the conditions hereinafter described, at any time or times for any lawful purpose of the Authority. (Sections 208 and 209).

Before such bonds shall be delivered, there shall be filed with the 1998 Fiscal Agent, among other things, a certificate signed by the Executive Director not earlier than thirty (30) days prior to the delivery date of such bonds setting forth:

(i) the amount of Revenues received by the Authority and until the outstanding 1968 Resolution Bonds have been paid or provision has been made for their payment and the repeal and cancellation of the 1968 Resolution, the amount of Excess 1968 Resolution Revenues deposited to the credit of the Revenue Fund in each of the fifteen (15) months immediately preceding the month in which such certificate is signed, adjusted (I) to give effect to legislation enacted on or prior to the date of delivery of such bonds that would have increased the Revenues or the amounts of Excess 1968 Resolution Revenues deposited to the credit of the Revenue Fund as aforesaid if such legislation (x) had been in effect throughout such fifteen (15) months, (y) allocates additional moneys to the Authority and (z) expressly permits the Authority to pledge to the payment of the bonds issued under the provisions of the 1998 Resolution or the 1968 Resolution until the 1968 Resolution Bonds have been paid or provision has been made for their payment and the repeal and cancellation of the 1968 Resolution and the Authority has expressly pledged such additional moneys to such payment on or prior to such date of delivery and (II) to reflect the moneys which would have been received if (A) the schedule of tolls in effect on the date of delivery of such bonds had been in effect and (B) the Toll Facilities to be financed in whole or part with the proceeds of such bonds had been in operation throughout such fifteen (15) months,

(ii) the amount of the maximum Principal and Interest Requirements for any fiscal year thereafter on account of all senior bonds theretofore issued under the provisions of the 1998 Resolution and then outstanding and the senior bonds then requested to be delivered, and

(iii) the amount of the maximum Principal and Interest Requirements for any fiscal year thereafter on account of all senior bonds and Subordinated Transportation Revenue Bonds theretofore issued under the provisions of the 1998 Resolution and then outstanding and the senior bonds then requested to be delivered; and

(iv) the percentage derived by dividing the amount in item (i) above for any twelve consecutive months by the amount in item (ii) above; and

(v) the percentage derived by dividing the amount in item (i) above for any twelve consecutive months by the amount in item (iii) above. (Section 208).

The 1998 Fiscal Agent may only deliver such additional senior bonds if the percentages shown in item (iv) and item (v) are not less than 150% and 100%, respectively. (Section 208).

The Authority need not deliver said certificate in connection with the issuance of senior bonds issued for the purpose of refunding senior bonds of any Series if the amount of the maximum Principal and Interest Requirements for any fiscal year thereafter on account of the senior bonds to be outstanding after the issuance of such refunding senior bonds shall be equal to or less than the maximum Principal and Interest Requirements for any fiscal year thereafter on account of the senior bonds outstanding prior to the issuance of such refunding senior bonds. (Section 209).

Subordinated Transportation Revenue Bonds may be issued under and secured by the 1998 Resolution, subject to the conditions described below, at any time or times for the purpose of paying the cost of any Transportation Facilities falling within the definition of "Federal-aid highway" or "capital projects" under Section 101 of Title 23 and Section 5302 of Title 49, respectively, of the United States Code, as such definitions may be amended from time to time, or qualifying for any other federal transportation assistance for the defraying (directly or indirectly) of such cost. (Section 210).

Before Subordinated Transportation Revenue Bonds shall be delivered, there shall be filed with the 1998 Fiscal Agent, among other things, a certificate signed by the Executive Director not earlier than thirty (30) days prior to the delivery date of such Subordinated Transportation Revenue Bonds indicating that the percentage derived by dividing (a) the amount of Revenues and Excess 1968 Resolution Revenues determined in the same manner as specified in clause (i) above by (b) the amount of the maximum Principal and Interest Requirements for any fiscal year thereafter on account of all senior bonds and Subordinated Transportation Revenue Bonds theretofore issued under the provisions of the 1998 Resolution and then outstanding and the Subordinated Transportation Revenue Bonds then requested to be delivered is not less than 125%. (Section 210).

Refunding Subordinated Transportation Revenue Bonds may be issued only to refund other Subordinated Transportation Revenue Bonds of any Series. The Authority need not deliver said certificate in connection with the issuance of refunding Subordinated Transportation Revenue Bonds if the amount of the maximum Principal and Interest Requirements for any fiscal year thereafter on account of the Subordinated Transportation Revenue Bonds to be outstanding after the issuance of such refunding Subordinated Transportation Revenue Bonds shall be equal to or less than the maximum Principal and Interest Requirements for any fiscal year thereafter on account of the Subordinated Transportation Revenue Bonds outstanding prior to the issuance of such refunding Subordinated Transportation Revenue Bonds. (Section 211).

Other Indebtedness

The Authority will not incur any indebtedness nor create or suffer to be created any lien, pledge, assignment, encumbrance or charge upon the Revenues ranking equally with or prior to the senior bonds issued under the 1998 Resolution, except the lien and charge of the senior bonds secured by the 1998 Resolution, or ranking equally with the Subordinated Transportation Revenue Bonds except the lien and charge of the Subordinated Transportation Revenue Bonds secured by the 1998 Resolution. Any other indebtedness incurred by the Authority after the effective date of the 1998 Resolution under documents not in effect on the effective date of the 1998 Resolution shall contain a statement that such indebtedness is junior, inferior and subordinate in all respects to the bonds. For purposes of the above limitation on incurrence of indebtedness, indebtedness shall not be deemed to include contracts entered into in the ordinary course of business, agreements to repay advances received from the Federal government or agreements to repay (to the extent drawn) all or a portion of the stated amount drawn under any Credit Facility, Liquidity Facility, Reserve Account Letter of Credit or Reserve Account Insurance Policy. Nothing in the 1998 Resolution shall be deemed to prohibit the Authority from entering into currency swaps, interest rate swaps or other arrangements for hedging of interest rates on any indebtedness. (Section 602).

Nothing in the 1998 Resolution is to be construed as preventing the Authority from financing any facilities authorized by the act creating the Authority, as amended, by the issuance of bonds or other obligations which are not secured under the provisions of the 1998 Resolution. (Section 1101).

Investment of Funds

Moneys held for the credit of the Revenue Fund, Senior Bond Service Account, Senior Bond Redemption Account, Subordinated Bond Service Account, and Subordinated Bond Redemption Account shall, as nearly as may be practicable, be continuously invested and reinvested at the written direction of the Authority in Government Obligations, and moneys held for the credit of the 1998 Construction Fund, Senior Bond Reserve Account and each account in the Subordinated Bond Reserve Fund shall, as nearly as may be practicable, be continuously invested and reinvested at the written direction of the Authority in Investment Obligations, which Government Obligations and Investment Obligations shall mature, or which 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 Fund or Accounts will be required for the purposes intended. Amounts on deposit in the Senior Bond Reserve Account and each account in the Subordinated Bond Reserve Fund shall be invested in Investment Obligations which mature not later than the final maturity date of any senior bonds or Subordinated Transportation Revenue Bonds outstanding, as the case may be. (Section 502).

Investment earnings on moneys on deposit to the credit of the following Funds and Accounts shall be applied as follows:

(a) Investment earnings on moneys on deposit to the credit of the Senior Bond Service Account, the Senior Bond Redemption Account, the Subordinated Bond Service Account, the Subordinated Bond Redemption Account and the 1998 Construction Fund shall be transferred to the credit of or retained in the 1998 Construction Fund; but the Authority may elect to have such investment earnings remain to the credit of the Senior Bond Service Account, the Senior Bond Redemption Account, the Subordinated Bond Service Account or the Subordinated Bond Redemption Account to fund the next payment of principal of, Amortization Requirements for and interest on the senior bonds or the Subordinated Transportation

Revenue Bonds, in which event the Authority shall receive a credit against the amounts required to be deposited in said Accounts as applicable;

(b) Investment earnings on moneys on deposit to the credit of the Senior Bond Reserve Account and each account in the Subordinated Bond Reserve Fund shall be retained in said accounts at any time that the respective amounts on deposit to the credit of said accounts is less than the Senior Reserve Requirement or the corresponding Subordinated Reserve Requirement, as applicable; and

(c) Investment earnings on moneys on deposit to the credit of the Revenue Fund shall be retained therein. (Section 502).

In computing the amount in any Fund or Account created pursuant to the provisions of the 1998 Resolution, obligations purchased as an investment of moneys therein shall be valued at par if purchased at par or at amortized value if purchased at other than par, plus, in each case, accrued interest. Amortized value, when used with respect to an obligation purchased at a premium above or a discount below par, means the value as of any given time obtained by dividing the total premium or discount at which such obligation was purchased by the number of days remaining to maturity on such obligation at the date of such purchase and by multiplying the amount thus calculated by the number of days having passed since such purchase; and (1) in the case of an obligation purchased at a premium by deducting the product thus obtained from the purchase price, and (2) in the case of an obligation purchased at a discount by adding the product thus obtained to the purchase price. Valuation on any particular date shall include the amount of interest then earned or accrued to such date on any moneys or investments in such Fund or Account. The computation of the amount on deposit in or credited to the Fund and Accounts created under the 1998 Resolution and the valuation of the investments of such amount shall be performed by the 1998 Fiscal Agent as of the close of business on the last day of each fiscal year and at such other times as the Authority shall request, and such computation and valuation shall not be required to be performed at other times. (Section 503).

Modifications

The Authority may adopt resolutions supplemental to the 1998 Resolution without the consent of the bondholders to cure any ambiguity, formal defect or omission, or to correct any inconsistent provisions or errors in the 1998 Resolution or any supplemental resolution, or to grant or confer upon the bondholders any additional rights, remedies, powers, authority or security, or to add to the conditions, limitations and restrictions on the issuance of bonds under the provisions of the 1998 Resolution or to add to the covenants and agreements of the Authority in the 1998 Resolution or to surrender any right or power reserved to or conferred upon the Authority, or to amend the conditions, limitations and restrictions on the issuance of Subordinated Transportation Revenue Bonds or the covenants and agreements relating to the Subordinated Transportation Revenue Bonds (as shall not adversely affect the interests of the holders of any senior bonds) as may be required to enable the Authority to comply with the provisions of any federal legislation, rules or regulations or court decisions or orders relating to the receipt by the Authority of grants or other assistance from the United States Government. (Section 801).

The holders of not less than a majority in aggregate principal amount of the senior bonds and of the Subordinated Transportation Revenue Bonds then outstanding and affected thereby shall have the right to consent to and approve the adoption of such resolution or resolutions supplemental to the 1998 Resolution as shall be deemed necessary or desirable by the Authority for the purpose of modifying, altering, amending, adding to or rescinding any of the terms and provisions contained in the 1998 Resolution or in any supplemental resolution; but nothing contained in the 1998 Resolution shall permit, or be construed as permitting, without consent of the holders of all bonds affected thereby, (a) an extension of the maturity of the principal of or the interest on any bond, or (b) a reduction in the principal amount of any bond or the redemption premium or the rate of interest thereon, or (c) the creation of a lien upon or a pledge of Revenues other than the lien and pledge created by the 1998 Resolution, or (d) a preference or priority of any bond or bonds over any other bond or bonds, or (e) a reduction in the aggregate principal amount of the bonds required for consent to such supplemental resolution, or (f) a change in the subordination provisions. (Section 802).

If at any time the Authority determines that it is necessary or desirable to adopt any supplemental resolution for any of the purposes of the above paragraph, the 1998 Fiscal Agent at the expense and request

of the Authority shall cause notice of the proposed adoption of such supplemental resolution to be mailed, first class, postage prepaid, to all bondholders and to Government Development Bank for Puerto Rico. Such notice shall briefly set forth the nature of the proposed supplemental resolution and shall state that copies thereof are on file at the office of the 1998 Fiscal Agent for inspection by all bondholders. The 1998 Fiscal Agent shall not, however, be subject to any liability to any bondholder by reason of its failure to cause such notice to be mailed, and any such failure shall not affect the validity of such supplemental resolution when consented to and approved. (Section 802).

Whenever, at any time within one year after the date of the mailing of such notice, the Authority shall obtain an instrument or instruments in writing purporting to be executed by the holders of not less than a majority in aggregate principal amount of the senior bonds and of the Subordinated Transportation Revenue Bonds then Outstanding, which instrument or instruments shall refer to the proposed supplemental resolution described in such notice and shall specifically consent to and approve the adoption thereof in substantially the form of the copy thereof referred to in such notice, and the Authority shall deliver to the 1998 Fiscal Agent a certificate signed by the Executive Director that the holders of such required percentages of bonds have filed such consents, thereupon, but not otherwise, the Authority may adopt such supplemental resolution in substantially such form, without liability or responsibility to any holder of any bond, whether or not such holder shall have consented thereto. (Section 802).

If the holders of not less than a majority in aggregate principal amount of the affected senior bonds and of the affected Subordinated Transportation Revenue Bonds outstanding at the time of the adoption of such supplemental resolution shall have consented to and approved the adoption thereof, no holder of any bond shall have any right to object to the adoption of such supplemental resolution, or to object to any of the terms and provisions contained therein or the operation thereof, or in any manner to question the propriety of the adoption thereof, or to enjoin or restrain the Authority from adopting the same or from taking any action pursuant to the provisions thereof and such consent shall be binding on the holder giving such consent and upon any subsequent holder whether or not he has notice thereof. (Section 802).

Upon the adoption of any supplemental resolution pursuant to the provisions of the 1998 Resolution, the 1998 Resolution shall be and be deemed to be modified and amended in accordance therewith, and the respective rights, duties and obligations under the 1998 Resolution of the Authority, the 1998 Fiscal Agent and all holders of bonds then outstanding shall thereafter be determined, exercised and enforced in all respects under the provisions of the 1998 Resolution as so modified and amended. (Section 803).

Miscellaneous Covenants

Master Plan. The Authority covenants that the master plan for the construction of required Transportation Facilities in the Commonwealth will be supplemented periodically as necessary and that the five-year Construction Improvement Program will be updated each year to cover the Transportation Facilities to be constructed by the Authority in the ensuing five-year period. (Section 603).

Costs of Maintenance, Repair and Operation of Traffic Facilities. The Authority covenants that, if and to the extent funds for the purpose of maintaining, repairing and operating all Traffic Facilities financed by the Authority in whole or in part by 1968 Resolution Bonds and all Transportation Facilities financed by the Authority in whole or in part by bonds under the provisions of the 1998 Resolution are not provided by the Commonwealth, the Authority will pay such costs from unencumbered funds then on deposit in the 1998 Construction Fund or from the Revenues or unencumbered 1968 Construction Fund moneys thereafter deposited to the credit of the 1998 Construction Fund pursuant to the 1998 Resolution and not from funds then on deposit or thereafter deposited to the credit of the 1968 Construction Fund. (Section 604).

The Authority further covenants that it will cause an annual general evaluation to be made by the Transportation Engineers of the level of maintenance of all Traffic Facilities and Transportation Facilities financed in whole or in part by the issuance of bonds under the provisions of, respectively, the 1968 Resolution and the 1998 Resolution, which Facilities shall be, in the judgment of the Authority and of the Traffic Engineers, material to the overall system of Transportation Facilities of the Authority. (Section 604).

The Authority further covenants that it will operate or cause to be operated the Toll Facilities, any Mass Transit Facilities and all other Transportation Facilities that it may from time to time operate or cause to be operated in an efficient and economical manner, that it will at all times maintain or cause to be maintained such Transportation Facilities in good repair and in sound operating condition and that it will make or cause to be made all necessary repairs, renewals and replacements thereto. (Section 604).

Annual Report of Traffic Engineers. The Authority covenants that it will cause the Transportation Engineers to prepare a report each year promptly after the completion of their general evaluation of the level of maintenance, repair and operating condition of the Transportation Facilities setting forth (i) their comments with respect to any supplements or revisions made by the Authority in the master plan or in the five-year Construction Improvement Program referred to above under “Master Plan” and their recommendations as to any supplements or revisions which should be made in such plan or in the Construction Improvement Program, and (ii) their findings as to whether those Traffic Facilities have been maintained in good repair, working order and sound operating condition and their recommendations as to necessary repairs, renewals or replacements. (Section 605).

If it appears from such report that repairs, renewals or replacements of any such Facilities are necessary, the Authority shall promptly cause the same to be restored to a condition of good repair and to sound operating condition, and if and to the extent that funds for such purpose have not been made available by the Commonwealth, moneys on deposit to the credit of the 1998 Construction Fund which have not theretofore been encumbered for other purposes, and moneys which are thereafter deposited to the credit of the 1998 Construction Fund pursuant to the 1998 Resolution shall first be applied for such purpose. No funds then on deposit or thereafter deposited to the credit of the 1968 Construction Fund shall be applied for such purpose. (Section 605).

Relating to the 1968 Resolution. The Authority covenants that immediately upon the repeal and cancellation of the 1968 Resolution, all Existing Tax and Fee Revenues and Existing Toll Revenues shall be pledged to the payment of the principal of and premium, if any, and interest on the bonds issued under the provisions of the 1998 Resolution to the same extent and with the same effect as the pledge of Revenues and other moneys deposited to the credit of the Revenue Fund. (Section 601).

The Authority further covenants that it will cause the 1968 Resolution to be repealed and cancelled at the earliest practicable date. The Authority further covenants that, except for the proposed supplemental resolution described in *Summary of Certain Provisions of the Proposed Supplemental Resolution*, it will not adopt any resolution supplemental to the 1968 Resolution for the purpose of granting to or conferring upon the 1968 Fiscal Agent for the benefit of the holders of the bonds issued under the 1968 Resolution any additional rights, remedies, powers, authority or security that may lawfully be granted to or conferred upon such holders or the 1968 Fiscal Agent, or for the purpose of modifying, altering, amending, adding to or rescinding, in any particular, any of the terms or provisions contained in the 1968 Resolution, or for the purpose of extending the maturity of any 1968 Resolution Bond or creating a lien upon or a pledge of revenues ranking prior to or on a parity with the lien or pledge created by the 1968 Resolution. Nothing shall prevent the Authority from adopting a resolution supplemental to the 1968 Resolution to cure any ambiguity or formal defect or omission in the 1968 Resolution. (Section 609).

The Authority covenants that so long as any 1968 Resolution Bonds are outstanding under the provisions of the 1968 Resolution it will cause to be made the deposits to the credit of the 1968 Construction Fund required by the 1968 Resolution. The Authority further covenants that except for any withdrawals required to be made as set forth in the third sentence of the fourth paragraph of “Sinking Funds” above, it will not withdraw, expend, pledge or otherwise encumber moneys held to the credit of the 1968 Construction Fund whether for the purpose of satisfying the Authority’s Construction Improvement Program or otherwise, except for the satisfying the Authority’s obligations under Section 513 of that certain trust agreement, dated as of April 1, 1992, by and between the Authority and Banco Santander Puerto Rico, successor trustee. See, “Teodoro Moscoso Bridge” under *Transportation System Revenues and Expenditures* above in this Official Statement (Section 610).

Use of Revenues. The Authority covenants and agrees that, so long as any of the bonds secured by the 1968 Resolution shall be outstanding, none of the Revenues will be used for any purpose other than as provided in the 1968 Resolution and the 1998 Resolution, and that no contract or contracts will be entered

into or any action taken by which the rights of the 1998 Fiscal Agent or of the bondholders might be impaired or diminished. (Section 611).

Additional 1968 Resolution Bonds. The Authority covenants that so long as any bonds shall be outstanding under the provisions of the 1998 Resolution it will not issue additional 1968 Resolution Bonds which mature after July 1, 2036 and except for (a) Series I Bonds and (b) bonds issued for the purpose of meeting the obligations of the Authority under Section 11.4(b) of that certain Concession Agreement for the Final Design, Construction, Operation and Maintenance of a Privatized Transportation Facility, dated December 20, 1991, as amended, by and between the Authority and Autopistas de Puerto Rico y Compañía, S.E. relating to its obligations in respect of the Teodoro Moscoso Bridge. See, "Teodoro Moscoso Bridge" under *Transportation System Revenues and Expenditures* above in this Official Statement.

Swap Agreements. The Authority covenants that it will not enter into a Swap agreement unless it first delivers copies of the proposed Swap agreement to S&P and Moody's and any other rating agency then rating the bonds. (Section 613).

Level of Tolls and Other Charges. Notwithstanding any provisions in the 1968 Resolution enabling the Authority to reduce tolls or other charges, the Authority covenants that it will not reduce the tolls or other charges imposed by it for the use of its Toll Facilities unless, as of the effective date of such reduction, the Authority delivers to the 1998 Fiscal Agent a certificate, signed by the Executive Director of the Authority not earlier than thirty (30) days prior to the effective date of such reduction, setting forth:

(i) the amount of Revenues received by the Authority and, until the outstanding 1968 Resolution Bonds have been paid or provision has been made for their payment and the repeal and cancellation of the 1968 Resolution, the amount of Excess 1968 Resolution Revenues deposited to the credit of the Revenue Fund in each of the fifteen (15) months immediately preceding the month in which such certificate is signed, adjusted (I) to give effect to legislation enacted on or prior to the effective date of such reduction that would have increased the Revenues or the amounts deposited to the credit of the Revenue Fund from the 1968 Construction Fund as aforesaid if such legislation (x) had been in effect throughout such fifteen (15) months, (y) allocates additional moneys to the Authority and (z) expressly permits the Authority to pledge to the payment of the bonds issued under the provisions of the 1998 Resolution or the 1968 Resolution until the 1968 Resolution Bonds have been paid or provision has been made for their payment and the repeal and cancellation of the 1968 Resolution and the Authority has expressly pledged such additional moneys to such payment on or prior to such date of delivery and (II) to reflect the moneys which would have been received if (A) the schedule of tolls in effect on such effective date had been in effect and (B) any Toll Facilities which have commenced operation or been removed from operation during such fifteen (15) months either had been in operation or not operating, throughout such fifteen (15) months,

(ii) the amount of the maximum Principal and Interest Requirements for any fiscal year thereafter on account of all senior bonds theretofore issued under the provisions of the 1998 Resolution and then outstanding, and

(iii) the amount of the maximum Principal and Interest Requirements for any fiscal year thereafter on account of all senior bonds and all Subordinated Transportation Revenue Bonds theretofore issued under the provisions of the 1998 Resolution and then outstanding and it shall appear from such certificate that the percentages derived by dividing the sum of the amounts shown in item (i) of such certificate for any twelve (12) consecutive months by the amount shown in item (ii) of said certificate and by the amount shown in item (iii) of said certificate, shall not be less than one hundred fifty per centum (150%) and one hundred per centum (100%), respectively. (Section 614).

SUMMARY OF CERTAIN PROVISIONS OF THE PROPOSED SUPPLEMENTAL RESOLUTION

The following is a summary of certain provisions of a resolution proposing to amend the 1998 Resolution, which resolution will be adopted when the consent of owners of a majority in aggregate principal amount of the Transportation Revenue Bonds and of the Subordinated Transportation Revenue Bonds has been obtained. Such statements do not purport to be complete and reference is made to the

proposed supplemental resolution, copies of which are available from the Authority or the 1998 Fiscal Agent. See "Modifications" in *Summary of Certain Provisions of the 1998 Resolution* for limitations as to the ability of the Authority to modify the 1998 Resolution further.

The proposed supplemental resolution will provide as follows:

(iii) the interest rate on bonds issued with a variable, adjustable, convertible or similar rate of interest shall be in the case of (A) in the case of such bonds outstanding on and before the date of calculation the greater of the average interest rate on such bonds during the sixty months or twelve months ending in either case with the month preceding the date of calculation (or such shorter period (ending with the same month as aforesaid) that such bonds shall have been Outstanding), and (B) in the case of such bonds first being delivered on such date of calculation and are being issued (1) on the basis that interest on such bonds would be excludible from gross income of the owners thereof for federal income tax purposes, the greater of the average of the Bond Market Association Swap Index (the "BMA Index") (i) for the twelve month period and (ii) the sixty month period in either case ending seven days before the date of calculation plus 100 basis points, or (2) as bonds not described in clause (B)(1), the greater of the average of the London Interbank Offered Rate ("LIBOR") for the time period most closely resembling the reset period for such bonds (i) for the twelve month period and (ii) for the sixty month period in either case ending seven days before the date of calculation plus 100 basis points (if the BMA Index or LIBOR shall cease to be published, the index to be used shall be that index which the Authority, in consultation with Government Development Bank for Puerto Rico, determines most closely replicates such index, as set forth in a certificate of the Executive Director filed with the Fiscal Agent); provided, however, that if the Authority has notified the Fiscal Agent that a Swap agreement is in effect in respect of such bonds, then for all purposes of this paragraph, except for the purpose of determining the required deposits to the Senior Bond Sinking Fund or the Subordinated Bond Sinking Fund pursuant to Section 401 hereof, the interest rate on such bonds shall be the Swap rate under such Swap agreement; and if such Swap rate is a variable rate, the interest rate on such bonds (except for the purpose specified above in this paragraph) shall be the average Swap rate for the preceding sixty months (or such shorter period that the Swap agreement has been in effect), or if such Swap agreement has not been in effect prior to the date of calculation, the Swap rate on the date of calculation.

APPENDIX V

Letter From The Traffic Engineers

JORGENSEN

Roy Jorgensen Associates, Inc.

Corporate Offices

3735 Buckeystown Pike
Post Office Box 70
Buckeystown, MD 21717-0070

Telephone: 1-301-831-1000
Facsimile: 1-301-874-2876

April 7, 2004

Dr. Jack T. Allison, Executive Director
Puerto Rico Highway and Transportation Authority
P.O. Box 42007
San Juan, Puerto Rico 00940-2007

Dear Dr. Allison:

This letter summarizes the results of our evaluation of the level of maintenance of the Puerto Rico Highway and Transportation Authority's Traffic Facilities and our review of the Construction Improvement Program. Our study was conducted in accordance with Resolution No. 68-18, adopted June 13, 1968, as amended, and Resolution No. 98-06, adopted February 26, 1998. Results of the study are documented in our Final Report, entitled "Maintenance Evaluation and Program Review – 2002-2003", dated July 2003.

Based on our field inspections, we find that the overall level of maintenance has generally been adequate to preserve the investment and provide an acceptable level of service to road users. Maintenance work methods and levels of service have been in general conformance to widely accepted maintenance practices in transportation and public works agencies in North America.

We have reviewed the 5-year Construction Improvement Program for Fiscal Years 2004-2008. In our opinion, the program is a reasonable response to the immediate and short-term transportation needs of the Commonwealth and is generally consistent with the Authority's long-range transportation master plan. Funding for the program appears to be adequate, based on revenue projections that have been reasonably accurate in the past and provide a sound basis for determining the size of future programs.

Please let us know if you need any additional information.

Sincerely,



William C. Grenke
Senior Consultant

APPENDIX VI

**SPECIMEN OF MBIA INSURANCE CORPORATION'S
BOND INSURANCE POLICY**

FINANCIAL GUARANTY INSURANCE POLICY

MBIA Insurance Corporation Armonk, New York 10504

Policy No. [NUMBER]

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

[PAR]
[LEGAL NAME OF ISSUE]

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

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

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

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

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

COUNTERSIGNED:

Resident Licensed Agent

City, State

STD-RCS-6
4/95

MBIA Insurance Corporation

President

Attest:

Assistant Secretary

APPENDIX VII

**SPECIMEN OF FINANCIAL GUARANTY INSURANCE COMPANY'S
BOND INSURANCE POLICY**



Financial Guaranty Insurance Company
 125 Park Avenue
 New York, NY 10017
 T 212-312-3000
 T 800-352-0001

Municipal Bond New Issue Insurance Policy

Issuer:	Policy Number:
	Control Number: 0010001
Bonds:	Premium:

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

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

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

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

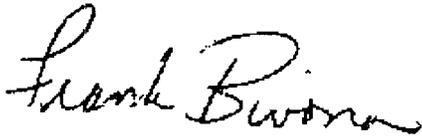


Financial Guaranty Insurance Company
125 Park Avenue
New York, NY 10017
T 212-312-3000
T 800-352-0001

Municipal Bond New Issue Insurance Policy

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

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



President

Effective Date:

Authorized Representative

U.S. Bank Trust National Association, acknowledges that it has agreed to perform the duties of Fiscal Agent under this Policy.



Authorized Officer



Financial Guaranty Insurance Company
 125 Park Avenue
 New York, NY 10017
 T 212-312-3000
 T 800-352-0001

Endorsement
To Financial Guaranty Insurance Company
Insurance Policy

Policy Number: _____ **Control Number:** 0010001

It is further understood that the term "Nonpayment" in respect of a Bond includes any payment of principal or interest made to a Bondholder by or on behalf of the issuer of such Bond which has been recovered from such Bondholder pursuant to the United States Bankruptcy Code by a trustee in bankruptcy in accordance with a final, nonappealable order of a court having competent jurisdiction.

NOTHING HEREIN SHALL BE CONSTRUED TO WAIVE, ALTER, REDUCE OR AMEND COVERAGE IN ANY OTHER SECTION OF THE POLICY. IF FOUND CONTRARY TO THE POLICY LANGUAGE, THE TERMS OF THIS ENDORSEMENT SUPERSEDE THE POLICY LANGUAGE.

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

President

Effective Date:

Authorized Representative

Acknowledged as of the Effective Date written above:

Authorized Officer
U.S. Bank Trust National Association, as Fiscal Agent