Government Development Bank for Puerto Rico

(A Component Unit of the
Commonwealth of Puerto Rico)

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

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

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INDEPENDENT AUDITORS' REPORT

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

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

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

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

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

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

Deloitte & Touche LLP

December 1, 2011

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

1. FINANCIAL HIGHLIGHTS

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

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

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

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

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

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

2. OVERVIEW OF THE FINANCIAL STATEMENTS

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

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

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

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

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

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

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

3. GOVERNMENT-WIDE FINANCIAL ANALYSIS

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

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

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

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

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

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

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

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

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

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

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

4. GOVERNMENTAL FUND RESULTS

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

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

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

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

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

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

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

5. BUSINESS-TYPE ACTIVITIES

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

(b) *Provision for Losses on Loans*

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

(c) Noninterest Income

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

(d) Noninterest Expenses

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

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

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

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

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

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

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

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

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

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

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

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

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

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

6. CONTACTING THE BANK'S FINANCIAL MANAGEMENT

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

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

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

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

See notes to basic financial statements.

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

STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2011

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

See notes to basic financial statements.

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

BALANCE SHEET — GOVERNMENTAL FUNDS
AS OF JUNE 30, 2011

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

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

See notes to basic financial statements.

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

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

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

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

See notes to basic financial statements.

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

BALANCE SHEET — ENTERPRISE FUNDS
AS OF JUNE 30, 2011

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

See notes to basic financial statements.

(Continued)

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

BALANCE SHEET — ENTERPRISE FUNDS
AS OF JUNE 30, 2011

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

See notes to basic financial statements.

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

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

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

See notes to basic financial statements.

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

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

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

See notes to basic financial statements.

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

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

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

See notes to basic financial statements.

(Continued)

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

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

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

See notes to basic financial statements.

(Continued)

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

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

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

(Concluded)

See notes to basic financial statements.

1. REPORTING ENTITY

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

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

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

The Housing Finance Authority (formerly known as the Puerto Rico Housing Finance Corporation) was created in 1977 to provide public and private housing developers with interim and permanent financing through mortgage loans for the construction, improvement, operation, and maintenance of rental housing for low and moderate-income families. The Housing Finance Authority also issues bonds and notes, the proceeds of which are deposited in separate trusts and generally invested in mortgaged-backed securities collateralized by mortgage loans on properties located in Puerto Rico purchased by low and moderate-income families. The Housing Finance Authority is authorized by the U.S. Department of Housing and Urban Development (HUD) to administer the U.S. Housing Act Section 8 program in Puerto Rico and to act as an approved mortgagor, both for multifamily rental units and for single-family homes. In addition, it is an authorized issuer of Government National Mortgage Association (GNMA) mortgage-backed securities, and is Puerto Rico's State Credit Agency for the Low-Income Housing Tax Credit Program under Section 42 of the U.S. Internal Revenue Code. Effective July 1, 2010, the Housing Finance Authority was also authorized by HUD to administer the HOME Investment Partnerships Program.

The Housing Finance Authority, in conjunction with the Puerto Rico Department of Housing, is the entity responsible for certifying projects under the New Secure Housing Program (known in Spanish as "Nuevo Hogar Seguro"), with the approval of the Federal Emergency Management Agency (FEMA). This program is directed to plan, coordinate, and develop the construction of new housing as a replacement to those destroyed by Hurricane Georges in 1998, and to attend the housing needs of families living in flood zone areas.

The Tourism Development Fund was created in 1993 to promote the hotel and tourism industry of the Commonwealth, primarily through the issuance of letters of credit and guarantees. The Tourism Development Fund is also authorized to make capital investments and provide direct financing to tourism-related projects.

The Development Fund was created in 1977 to expand the sources of financing available for the development of the private sector of the economy of Puerto Rico and to complement the Bank's lending program. The Development Fund may also guarantee obligations of private sector enterprises and invest in their equity securities.

The Public Finance Corporation was created in 1984 to provide the agencies and instrumentalities of the Commonwealth with alternate means of satisfying financial needs. The resolution creating the Public Finance Corporation states that if it were to be dissolved or cease to exist without a successor public entity being appointed, any funds or assets not required for the payment of its bonds or any other obligation, will be transferred to the Secretary of the Department of the Treasury of the Commonwealth (the "Department of the Treasury") for deposit in the Commonwealth's general fund.

The Capital Fund was created in 1992 to expand the investment options available to the Bank and to administer, separately from the Bank's general investment operations, an equity investments process through professional equity investment managers. On May 31, 2010, the board of directors of the Capital Fund authorized the transfer of its investments portfolio of approximately $72 million to the Tourism Development Fund. The transfer was completed on June 30, 2010. The Capital Fund's activities have been reduced significantly after June 30, 2010.

Other nonmajor funds include the JMB Institute and the Education Assistance Corporation. The JMB Institute was created in 2002 to complement the Bank's mission of promoting economic development by providing specialized training on the theory and practice of public finances and economics to talented young professionals in order to attract them to join the public service. The Education Assistance Corporation was created in 1981 to administer the Stafford Loan Program in Puerto Rico and guarantee the payment of student loans granted by financial institutions in Puerto Rico under certain terms and restrictions. The operations of this fund were transferred to a guarantee agency designated by the U.S. Department of Education. The Education Assistance Corporation is currently inactive.

To minimize its risk of loss, the Bank purchases insurance coverage for public liability, hazard, automobile, crime, and bonding as well as workmen's insurance for employees. The selection of the insurer has to be approved by the Public Insurance Office of the Department of the Treasury. Insurance coverage is updated annually to account for changes in operating risk. For the last three years, insurance settlements have not exceeded the amount of coverage.

2. BASIS OF PRESENTATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of the Bank conform to accounting principles generally accepted in the United States of America (U.S. GAAP), as applicable to governmental entities. The Bank follows

Governmental Accounting Standards Board (GASB) statements under the hierarchy established by Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*, in the preparation of its financial statements. The Bank has elected to apply all Financial Accounting Standards Board's pronouncements issued after November 30, 1989, in accounting and reporting for its enterprise funds and business type activities to the extent they do not conflict with GASB pronouncements.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reported period. Actual results could differ from those estimates.

Government-Wide and Fund Financial Statements:

Government-Wide Financial Statements — The statement of net assets (deficiency) and the statement of activities report information on all activities of the Bank. The effect of interfund balances has been removed from the government-wide statement of net assets, except for the residual amounts due between governmental and business-type activities. Interfund charges for services among functions of the government-wide statement of activities have not been eliminated. The Bank's activities are distinguished between governmental and business-type activities. Governmental activities generally are financed through intergovernmental revenues and other nonexchange revenues. Business-type activities are financed in whole or in part by fees charged to external parties for goods or services and interest earned on investment securities and loans. Following is a description of the Bank's government-wide financial statements.

The statement of net assets (deficiency) presents the Bank's assets and liabilities, with the difference reported as net assets (deficiency). Net assets are reported in three categories:

- Invested in capital assets, net of any related debt, consists of capital assets, net of accumulated depreciation and amortization and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets.
- Restricted net assets result when constraints placed on net assets use are either externally imposed by creditors, grantors, contributors, and the like, or imposed by law through constitutional provisions or enabling legislation.
- Unrestricted net assets (deficiency) consist of net assets (deficiency) that do not meet the definition of the two preceding categories. Unrestricted net assets often are designated, in order to indicate that management does not consider them to be available for general operations. Unrestricted net assets often have constraints on use that are imposed by management, but such constraints may be removed or modified.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable within a specific function. Program revenues include: (1) interest income on loans and investments, changes in the fair value of investments, and fees and charges to customers for services rendered or for privileges provided, and (2) grants and contributions that are restricted to meet the operational or capital requirements of a particular function. Other items not meeting the definition of program revenues are reported as general revenues.

Fund Financial Statements — Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts. The financial activities of the Bank that are reported in the accompanying basic financial statements have been classified into governmental and enterprise funds.

Separate financial statements are provided for governmental funds and enterprise funds. Major individual governmental and enterprise funds are reported as separate columns in the fund financial statements, with nonmajor funds being combined into a single column. Fund balances at the beginning of the year are restated to reflect changes in major fund definition. In the case of enterprise funds, each individual blended component unit of the Bank with the exception of JMB Institute and Education Assistance Corporation, which have been grouped as other nonmajor funds, has been reported as a separate major fund in the fund financial statements. In the case of the Housing Finance Authority, all of its activities not classified and reported as governmental funds have been reported as an enterprise fund.

Fund balances for each governmental fund are displayed in the following classifications depicting the relative strength of the spending constraints placed on the purposes for which resources can be used:

- Nonspendable — amounts that cannot be spent because they are either not in a spendable form (such as inventories and prepaid amounts) or are legally or contractually required to be maintained intact.
- Restricted — amounts that can be spent only for specific purposes because of constraints imposed by external providers (such as grantors, bondholders, and higher levels of government), or imposed by constitutional provisions or enabling legislation.
- Committed — amounts that can be spent only for specific purposes determined by a formal action of the government's highest level of decision-making authority.
- Assigned — amounts the government intends to use for specific purposes that do not meet the criteria to be classified as restricted or committed.
- Unassigned — amounts that are available for any purpose.

Measurement Focus, Basis of Accounting, and Financial Statements Presentation:

Government-Wide Financial Statements — The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Grants and similar items are recognized as revenues as soon as all eligibility requirements imposed by the provider have been met.

Governmental Funds' Financial Statements — The governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the Bank considers revenues to be available if they are collected within 120 days after the end of the fiscal year. Principal revenue sources considered susceptible to accrual include federal and Commonwealth funds to be received by the HUD Programs, ARRA Funds and Closing Costs Assistance Program. Other revenues are considered to be measurable and available only when cash is received. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. Modifications to the accrual basis of accounting include:

- Employees' vested annual leave is recorded as expenditure when utilized. The amount of accumulated annual leave unpaid at June 30, 2011 is reported only in the government-wide financial statements.

- Interest on general long-term obligations is generally recognized when paid.

- Debt service principal expenditures and claims and judgments are recorded only when payment is due.

Governmental Funds — The following governmental activities of the Bank are classified as major governmental funds:

- HUD Programs — This special revenue fund accounts for the subsidy to low and moderate-income families for the rental of decent and safe dwellings under the U.S. Housing Act Section 8 programs.

- ARRA Funds — This special revenue fund accounts for funds received under Title XII and Section 1602 of the American Recovery and Reinvestment Act of 2009. Title XII is a grant program that provides funds for capital investments in low-income housing tax credit projects. Section 1602 grants funds to states to finance construction or acquisition and rehabilitation of qualified low-income buildings for low-income housing in lieu of low-income housing tax credits.

- Closing Costs Assistance Program — This special revenue fund accounts for revenues received mainly from appropriations from the Commonwealth to provide subsidies to eligible individuals or families for the purchase of an eligible principal residence.

- My New Home Program — This special revenue fund accounts for revenues provided by Act 122 of August 6, 2010, which assigned to the Housing Finance Authority, for a period of seven years, a portion of no less than 80% of the unreserved monies and other liquid funds abandoned or unclaimed in the financial institutions that will be transferred to the general funds of the Commonwealth.

  The following governmental activities of the Bank are accounted for in other nonmajor governmental funds:

- Affordable Housing Mortgage Subsidy Program (Stages 2, 3, 6, 7, 8, 9, 10 and 11) — These special revenue funds are used to account for the proceeds of specific revenue sources under Stages 2, 3, 6, 7, 8, 9, 10 and 11 of the Affordable Housing Mortgage Subsidy Program (AHMSP) that are legally restricted for expenditures to promote the origination of mortgage loans by financial institutions in the private sector to low and moderate-income families. Under these stages, the Housing Finance Authority provides subsidy for the down payment and/or the principal and interest payments on mortgage loans originated under a predetermined schedule of originations and, in the case of Stages 9, 10, and 11, to acquire such mortgages in the form of mortgage-backed securities issued by the financial institutions. Loans originated, as well as servicing, are kept by the originating financial institution. There was no open schedule of originations under these stages as of June 30, 2011.

- AHMSP Act No. 124 — This special revenue fund accounts for excess subsidy funds as well as accumulated net assets, released periodically from arbitrage structures used to provide housing assistance.

- Affordable Housing Mortgage Subsidy Mortgage-Backed Certificates — This special revenue fund is used to account for specific revenue sources used to provide subsidy for the mortgages underlying the mortgage-backed securities held as collateral for the mortgage-backed certificates issued in fiscal year 2007.

- New Secure Housing Program — This special revenue fund is used to account for federal and local resources directed to plan, coordinate, and develop the construction of new housing units as a replacement for those destroyed by Hurricane Georges in 1998 and to assist with the housing needs of those families living in hazard prone areas.

- HOME Program — Effective July 1, 2010, the Housing Finance Authority was certified by the HUD to administer the HOME Investment Partnerships ("HOME") Program. The objectives of the HOME Program include: (1) expanding the supply of decent and affordable housing, particularly housing for low- and very low-income families; (2) strengthening the abilities of state and local governments to design and implement strategies for achieving adequate supplies of decent, affordable housing; (3) providing financial and technical assistance to participating jurisdictions, including the development of model programs for affordable low-income housing; and (4) extending and strengthening partnerships among all levels of government and the private sector, including for-profit and nonprofit organizations, in the production and operation of affordable housing.

- Protecting Your Home Program — This special revenue fund accounts for mortgage payment subsidy for up to 18 months or $20,000, whichever is lower, and is intended to reduce the amount of home foreclosures among low- and moderate-income families with recent financial difficulties. This loss mitigation program was financed with $20 million of excess funds from previous bond issuances under the AHMSP.

Enterprise Funds' Financial Statements — The financial statements of the enterprise funds are reported using the economic resources measurement focus and the accrual basis of accounting, similar to the government-wide statements described above.

Enterprise funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses are those that result from the Bank and its components units providing the services that correspond to their principal ongoing operations. Operating revenues are generated from lending, investing, banking and fiscal agency services, and other related activities. Operating expenses include interest expense, any provision for losses on loans, advances, letters of credit, or guarantees and all general and administrative expenses, among others. Revenues and expenses not meeting these definitions are reported as nonoperating revenues and expenses.

Securities Purchased Under Agreements to Resell — The Bank enters into purchases of securities under agreements to resell. The amounts advanced under these agreements generally represent short-term loans and are reflected as an asset. The securities underlying these agreements are usually held by the broker or his/her agent with whom the agreement is transacted. There were no securities purchased under agreements to resell outstanding at June 30, 2011.

Investments and Investment Contracts — Investments and investment contracts are carried at fair value, except for money market instruments and participating investment contracts with a remaining maturity at the time of purchase of one year or less, and nonparticipating investment contracts (guaranteed investment contracts), which are carried at cost; and investment positions in 2a-7 like external investment pools, which are carried at the pools' share price. Fair value is determined based on quoted market prices and quotations received from independent broker/dealers or pricing service organizations. Realized gains and losses from the sale of investments and unrealized changes in the fair value of outstanding investments are included in net increase (decrease) in fair value of investments.

Loans Receivable and Allowance for Loan Losses — Loans in the enterprise funds are presented at the outstanding unpaid principal balance reduced by an allowance for loan losses. The accrual of interest on loans to the private sector ceases when loans become past due over six months. For loans to public sector entities, the accrual of interest ceases when management determines that all of the following characteristics are present: (a) a loan is six months past due; (b) it has no current source of repayment; (c) it is not covered by a formal commitment from the Commonwealth; and (d) it has no designated collateral or such collateral is insufficient. Once a loan is placed in nonaccrual status, all accrued interest receivable is reversed from interest income. Interest income on nonaccrual loans is thereafter recognized as income only to the extent actually collected. Nonaccrual loans are returned to an accrual status when management has adequate evidence to believe that the loans will be performing as contracted.

The allowance for loan losses is established through provisions recorded in the fund financial statements. This allowance is based on management's evaluation of the risk characteristics of the loan including such factors as the nature of individual credits outstanding, past loss experience, known and inherent risks in the portfolios, adverse situations that may affect the borrower's ability to repay, the estimated value of any underlying collateral, and general economic conditions. Loan charge-offs are recorded against the allowance when management believes that the collection of the principal is unlikely. Recoveries of amounts previously charged off are credited to the respective allowance. Because of uncertainties inherent in the estimation process, management estimate of credit losses in the outstanding loans receivable portfolios and the related allowance may change in the near future.

Management, considering current information and events regarding the borrowers' ability to repay their obligations, considers a loan to be impaired when it is probable that the Bank will be unable to collect all amounts due according to the contractual terms of the loan agreement. Interest income and cash receipts on impaired loans are accounted for predominantly in the same manner as nonaccrual loans.

Loans considered to be impaired are generally reduced to the present value of expected future cash flows, discounted at the loan's effective interest rate or, as a practical expedient, at the loan's observable market price or the fair value of the collateral if the loan is collateral dependent, by establishing a valuation allowance.

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

Management believes that no losses will be incurred by the Bank with respect to principal and interest on most of its loans to the public sector (including municipalities) and, as a result, no allowance for loan losses is generally established for them. For public sector loans, excluding municipalities, management bases its position in that in the past, the Director of the OMB has included in the budget of the Commonwealth appropriations to assist the Commonwealth and certain public sector corporations, agencies, and instrumentalities in repaying their loans with the Bank. The Legislature of the Commonwealth (the "Legislature") has generally approved these appropriations, and such practice is anticipated to continue in the future. Further, in accordance with Act No. 164 of December 17, 2001, the Bank is no longer allowed to originate loans to any governmental entity for which the source of repayment consists of appropriations from the Commonwealth's general fund without first obtaining the approval of the Legislature, except for (i) loans up to an aggregate amount of $100,000,000 as long as, among other things, the Bank obtains the written approval of the Governor and the Director of OMB, (ii) loans to any financially troubled governmental entity to enable it to honor its debt obligations, and (iii) loans to the Secretary of the Treasury under legislation authorizing the Secretary to borrow funds in anticipation of tax revenues.

In addition, on May 13, 2006, the Legislature enacted Act No. 91 that established the *Dedicated Sales Tax Fund*, known as FIA by the acronym of its Spanish name (the "FIA Fund"). Act No. 91 originally provided that the first one percent of the Commonwealth's share of the sales and consumption tax ("Pledged Sales Tax") will be used to repay certain obligations of the Commonwealth that were outstanding at June 30, 2006, payable to the Bank and the Public Finance Corporation, generally referred to as extra-constitutional debt, including approximately $2.8 billion of loans due by the Commonwealth and certain of its instrumentalities to the Bank at such date. The outstanding balance of such loans amounted to approximately $770.8 million at June 30, 2011.

Act No. 91 was amended by Act No. 291, enacted on December 26, 2006, and by Act No. 56, enacted on July 5, 2007, to create the Puerto Rico Sales Tax Financing Corporation (the "Sales Tax Corporation") as an independent governmental instrumentality that will own and hold the FIA Fund for the purpose of financing the payment, retirement or defeasance of the extra-constitutional debt.

On January 14, 2009, Act No. 91 was amended by Act No. 1 ("Act No. 1") to increase the Pledged Sales Tax to 2% of the Commonwealth's share of the sales and consumption tax. Furthermore, Act No. 1 amended Act No. 91 to allow the use of the proceeds of future bond issuances by the Sales Tax Corporation to, among other, pay principal and/or interest of loans granted by the Bank to the Commonwealth payable from future Commonwealth general obligation bonds and any debt of the Commonwealth outstanding as of December 31, 2008 that did not have a source of repayment or was payable from budgetary appropriations.

Finally, Act No. 7 of March 9, 2009 amended Act No. 91 to increase the Pledged Sales Tax by an additional 0.75% or to 2.75% effective July 1, 2009 which represents 50% of the Commonwealth's share of the sales and consumption tax.

During the fiscal year ended June 30, 2011, the Bank collected interest amounting to approximately $6.6 million on outstanding public sector loans from funds held by the Sales Tax Financing Corporation.

Also, loans granted to finance capital improvement programs of certain public entities are generally repaid from the proceeds of future bond issuances of these public entities or the Commonwealth. The public corporations and the Commonwealth have never defaulted on their respective bonds.

Although management of the Bank believes that no additional losses of principal and interest will be incurred by the Bank with respect to loans outstanding to the public sector at June 30, 2011, there can be no assurance that the director of the OMB will include amounts for loan repayments in the Commonwealth's budget, and that the Legislature will appropriate sufficient funds in the future to cover all amounts due to the Bank by the Commonwealth or public sector entities requiring the Commonwealth's support, or that the proceeds from any future bond issuances by the Sales Tax Corporation or certain public entities which have financed their capital improvement programs with the Bank, will be sufficient to cover the outstanding amount of extra-constitutional or capital improvement program debt at June 30, 2011. The participation of certain public entities in the bond market has been delayed waiting for the credit rating of such entities to improve or for more favorable market conditions. Because of the relationship among the Bank, the public sector entities, the director of the OMB, and the Legislature, the timing and amount of any financial assistance and bond proceeds to be used to repay certain public sector loans cannot be reasonably estimated by the Bank. The Bank, however, has in the past collected the outstanding principal and interest at the contractual rate on loans repaid from Commonwealth's appropriations or bond proceeds. Accordingly, no allowance has been established in the case of public sector loans for any shortfall between the present value of the expected future cash flows and the recorded investment in the loans.

Loans to municipalities amounting to approximately $956 million at June 30, 2011 are collateralized by a pledge of a portion of property tax assessments of each municipality. These loans include bonds and notes issued by Puerto Rico municipalities which are acquired by the Bank as bridge financing until such financings can be packaged and securitized. Subsequently, from time to time, the Bank sells, at par, a selection of these bonds and notes to the Puerto Rico Municipal Finance Agency (MFA), a component unit of the Commonwealth organized to create a capital market to assist municipalities in financing their public improvements programs. These loans, when sold, are pledged to secure the debt service payments for the bonds issued by MFA. In addition, Act. No. 80, enacted on July 29, 2007, provides that a portion of the municipal sales tax will be deposited in special accounts with the Bank for the purpose of granting loans to municipalities. The funds available in such accounts increase the borrowing capacity of the corresponding municipality. As of June 30, 2011, loans to municipalities repayable from these accounts amounted to approximately $559 million.

Allowance for Losses on Guarantees and Letters of Credit — Management of the Bank periodically evaluates the credit risk inherent in the guarantees and letters of credit on the same basis as loans are evaluated. The Bank charges as expense the amount required to cover estimated losses by establishing a specific allowance component for guarantees and letters of credit relating to loans in default, determined on the basis of the estimated future net cash outlays in connection with the related guarantees and letters of credit, and a general component for the risk inherent in the other guarantees and letters of credit outstanding, established as a percentage of the principal amount of the underlying loans, based on the Bank's loss experience on financial guarantees and letters of credit, and management's best judgment.

When a guarantee or letter of credit is honored, the Bank recognizes any disbursement as a nonperforming loan; therefore, no interest is accrued on the principal. After a specific analysis of the provision requirements, the related allowance included in the allowance for guarantees and letters of credit is reclassified to the allowance for loan losses. Any deficiency in the estimated allowance requirement is recorded as an additional provision to the allowance for loan losses.

The concentration of risk in the guarantees and letters of credit issued, predominantly those issued by the Tourism Development Fund (small number of large guarantees, geographical concentration in Puerto Rico, industry concentration in hotel and tourism), as well as other economic factors, compounds the uncertainty in management's estimate of the allowance for losses on guarantees and letters of credit. As a result, the aggregate losses on guarantees and letters of credit ultimately incurred by the Bank may differ from the allowance for losses as reflected in the accompanying basic financial statements, and such differences may be material.

Pursuant to the legislation under which the Tourism Development Fund was created, the executive director of the Tourism Development Fund is required to certify each year to the director of the OMB the amount, if any, that is necessary to reimburse the Tourism Development Fund for disbursements made in the previous year in connection with obligations guaranteed in excess of fees and charges collected on such guarantees ("net disbursements"). On December 16, 2009, Act No. 173 was enacted, which amended the legislation that created the Tourism Development Fund, to modify the definition of net disbursements to include disbursements made by the Tourism Development Fund for (i) loans to third parties, (ii) the acquisition of loan participations, and (iii) the acceleration of maturities of loans, notes, bonds or other type of debt guaranteed by the Tourism Development Fund. In addition, Act No. 173 provides that disbursements shall not be deemed made in the year in which the disbursement occurs but shall be deemed made in the year in which the executive director of the Tourism Development Fund determines that a loss was incurred with respect to a loan, note, bond or debt (such determination being referred to as a "realized loss"). The director of the OMB has to include the amount subject to reimbursement in the general fund budget of the Commonwealth for the following fiscal year for the Legislature's consideration and approval. The Legislature is not obligated to authorize such appropriations. As of June 30, 2011, there were no outstanding claims for reimbursements.

Debt Issue Costs — Debt issue costs are deferred and amortized, as a component of interest expense, over the term of the related debt using the effective interest method, or a systematic and rational method that approximates the interest method. Issuance costs of bonds accounted for in the governmental funds are recorded as expenditures when paid.

Real Estate Available for Sale — Real estate available for sale comprises properties acquired in lieu of payment and through foreclosure proceedings. It also includes loans that are treated as if the underlying collateral had been foreclosed because the Bank has taken possession of the collateral, even though legal foreclosure or repossession proceedings have not taken place. Those properties are carried at the lower of cost or fair value, which is established by a third party professional assessment or based upon an appraisal, minus estimated costs to sell. At the time of acquisition of properties in full or in partial satisfaction of loans, any excess of the loan balance over the fair value of the properties minus estimated costs to sell is charged against the allowance for loan losses. Subsequent declines in the value of real estate available for sale are charged to expenditure/expense. Gain or loss on sale related to real estate available for sale is included within revenues in the accompanying statement of revenues, expenditures and changes in fund balances and within noninterest income in the accompanying statement of revenues, expenses, and changes in net assets.

Allowance for Losses on Mortgage Loan Insurance — The allowance for losses on mortgage loan insurance is based on management's evaluation of potential losses on insurance claims after considering economic conditions, fair value of related property and other pertinent factors. Such amount is, in the opinion of management, adequate to cover estimated future normal mortgage loan insurance losses. Actual losses for mortgage loan insurance are charged and recoveries, if any, are credited to the allowance for losses on mortgage loan insurance. Because of uncertainties inherent in the estimation process, management's estimate of losses in the outstanding mortgage loans insurance portfolio and the related allowance may change in the near future.

Capital Assets — Capital assets, which include premises and equipment, are stated at cost less accumulated depreciation and amortization, and are reported in the business-type activities column in the government-wide financial statements. Capital assets are defined by the Bank as assets that have a cost of $500 or more at the date of acquisition and have an expected useful life of three or more years. Depreciation is charged to operations and included within other noninterest expense, and is computed on the straight-line basis over the estimated useful lives of the depreciable assets. Leasehold improvements are amortized over the terms of the respective leases or the estimated useful lives of the improvements, whichever is shorter. Costs of maintenance and repairs which do not improve or extend the lives of the respective assets are charged to expense as incurred.

Estimated useful lives are as follows:

Building	40 years
Leasehold improvements	Lesser of 10 years or lease term
Information systems	3–5 years
Office furniture and equipment	5 years
Vehicles	5 years

Securities Sold Under Agreements to Repurchase — The Bank enters into sales of securities under agreements to repurchase. These agreements generally represent short-term financings and are reflected as a liability. The securities underlying these agreements are usually held by the broker or his/her agent with whom the agreement is transacted.

Compensated Absences — The employees of the Bank are granted 30 days of vacation and 18 days of sick leave annually. Vacation and sick leave may be accumulated up to a maximum of 72 and 90 days, respectively. In the event of employee resignation, an employee is reimbursed for accumulated vacation and sick leave days up to the maximum allowed. The enterprise fund financial statements and the government-wide financial statements present the cost of accumulated vacation and sick leave as a liability. There are no employees paid by governmental funds.

Deferred Revenues — Deferred revenues at the governmental fund level arise when potential revenues do not meet the available criterion for recognition in the current period. Available is defined as due at June 30 and expected to be collected within 120 days thereafter to pay obligations due at June 30. Deferred revenues at the government-wide level arise only when the Bank receives resources before it has a legal claim to them.

Refundings — Refundings involve the issuance of new debt whose proceeds are used to repay immediately (current refunding) or at a future time (advance refunding) previously issued debt. The difference between the reacquisition price and the net carrying amount of the old debt is deferred and amortized as a component of interest expense over the remaining life of the old debt or the life of the new debt, whichever is shorter. The deferred amount is recorded as an addition to or deduction from the new debt.

No-Commitment Debt — The Housing Finance Authority has issued notes and bonds in connection with the financing of low and moderate-income housing projects. Certain of the obligations issued by the Housing Finance Authority are considered no-commitment debt and are excluded, along with the related assets held in trust, from the accompanying basic financial statements. The Bank, the Housing Finance Authority and the Commonwealth, except for the assets held in trust and earnings thereon, are not liable directly or indirectly for the payment of such obligations.

Certain other collateralized obligations of the Housing Finance Authority are included in the accompanying basic financial statements either because they represent general obligations of the Housing Finance Authority or it maintains effective control over the assets transferred as collateral.

From time to time, the Public Finance Corporation issues bonds, the proceeds of which are used to purchase from the GDB Operating Fund promissory notes of the Commonwealth, and of certain of its instrumentalities and public corporations. The bonds are limited obligations of the Public Finance Corporation and, except to the extent payable from bond proceeds and investments thereon, are payable solely from the pledge and assignment of amounts due on the notes. Principal and interest on the notes are payable solely from legislative appropriations to be made pursuant to acts approved by the Legislature. The underlying notes represent debt of the issuing instrumentalities. The bonds are considered no-commitment debt, and therefore neither the bonds nor the notes purchased with the proceeds therefrom are presented in the accompanying basic financial statements.

Loan Origination Costs and Commitment Fees — GASB No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues*, requires that loan origination and commitment fees and direct origination costs be amortized over the contractual life of the related loan. The Bank generally recognizes commitment fees as income when collected and the related loan origination costs as expense when incurred. In the opinion of management, the difference between the two methods does not have a significant effect on the Bank's financial position and changes in financial position.

Transfers of Receivables — Transfers of receivables are accounted and reported as a sale if the Bank's continuing involvement with those receivable is effectively terminated. This approach distinguishes transfers of receivables that are sales from transfers that are collateralized borrowings.

The Bank's continuing involvement is considered to be effectively terminated if all of the following criteria are met: (i) the transferee's ability to subsequently sell or pledge the receivables is not significantly limited by constraints imposed by the Bank, either in the transfer agreement or through other means, (ii) the Bank does not have the option or ability to unilaterally substitute for or reacquire specific accounts from among the receivables transferred, except in certain limited circumstances, (iii) the sale agreement is not cancelable by either party, including cancellation through payment of a lump sum or transfer of other assets or rights, and (iv) the receivables and the cash resulting from their collection have been isolated from the Bank.

The Bank services loans for investors and receives servicing fees generally based on stipulated percentages of the outstanding principal balance of such loans. Loan servicing fees, late charges, and other miscellaneous fees are recognized as revenues as the related mortgage payments are collected, net of fees due to any third-party servicers. No servicing asset is recognized since fees are considered adequate compensation.

Future Adoption of Accounting Pronouncements — The GASB has issued the following Statements:

- GASB Statement No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employers Plans*, which if effective for periods beginning after June 15, 2011.

- GASB Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, which is effective for periods beginning after December 15, 2011.

- GASB Statements No. 61, *The Financial Reporting Entity: Omnibus – an amendment of GASB Statements No. 14 and No. 34*, which is effective for periods beginning after June 15, 2012.

- GASB Statements No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements,* which is effective for periods beginning after December 15, 2011.

- GASB Statements No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position,* which is effective for periods beginning after December 15, 2011.

- GASB Statements No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions — An Amendment of GASB Statement No. 53,* which is effective for periods beginning after June 15, 2011.

Management is evaluating the impact that these statements will have on the Bank's basic financial statements.

3. CASH AND DUE FROM BANKS, FEDERAL FUNDS SOLD, AND DEPOSITS PLACED WITH BANKS

The table presented below discloses the level of custodial credit risk assumed by the Bank at June 30, 2011. Custodial credit risk is the risk that, in the event of a financial institution failure, the Bank's deposits may not be returned to it. The Commonwealth requires that public funds deposited in commercial banks in Puerto Rico must be fully collateralized for the amount deposited in excess of federal depository insurance. All securities pledged as collateral are held by the Secretary of the Treasury of the Commonwealth. The Bank does not have a formal policy for custodial credit risk for cash accounts opened with commercial banks outside Puerto Rico. These accounts are opened only with well-capitalized financial institutions.

The Bank' policies for deposits placed with banks and federal funds sold establish maximum exposure limits for each institution based on the institution's capital, financial condition and credit rating assigned by nationally recognized rating agencies. Deposits placed with banks of approximately $740.5 million mature within one year. Federal funds sold mature overnight and no collateral is required. As of June 30, 2011, $1,171,971,387 of the depository bank balance of $1,177,222,759 was uninsured and uncollateralized as follows:

	Carrying Amount	Depository Bank Balance	Amount Uninsured and Uncollateralized
Cash and due from banks	$ 347,407,500	$ 347,909,368	$ 342,657,996
Deposits placed with banks	740,463,391	740,463,391	740,463,391
Federal funds sold	88,850,000	88,850,000	88,850,000
Total	$ 1,176,720,891	$ 1,177,222,759	$ 1,171,971,387

Reconciliation to the government-wide statement of net assets (deficiency):

Unrestricted:	
Cash and due from banks	$ 341,790,505
Federal funds sold	88,850,000
Deposits placed with banks	219,315,862
Total unrestricted	649,956,367
Restricted:	
Cash and due from banks	5,616,995
Deposits placed with banks	521,147,529
Total restricted	526,764,524
Total	$ 1,176,720,891

4. INVESTMENTS

The Bank's investment policies allow management to purchase or enter into the following investment instruments:

- U.S. government and agencies obligations
- Certificates of deposit and time deposits
- Bankers' acceptances
- Obligations of the Commonwealth of Puerto Rico, its agencies, municipalities, public corporations, and instrumentalities
- Federal funds sold
- Securities purchased under agreements to resell
- World Bank securities
- Mortgage-backed and asset-backed securities
- Corporate debt, including investment contracts
- External investment pools
- Stock of corporations created under the laws of the United States of America or the Commonwealth of Puerto Rico
- Options, futures, and interest-rate swap agreements for hedging and risk control purposes, as well as for the creation of synthetic products which qualify under any of the foregoing investment categories

- Open-end mutual funds with acceptable underlying assets and rated AAA by Standard & Poor's or its equivalent by Moody's

The Bank's investment policies establish limitations and other guidelines on maturities and amounts to be invested in the aforementioned investment categories and by issuer/counterparty and on exposure by country. In addition, such policies provide guidelines on the institutions with which investment transactions can be entered into. In addition, the investment committee and the board of directors of the Bank will determine, from time to time, other transactions that the Bank may enter into.

The Bank's investment policies provide that investment transactions shall be entered into only with counterparties that are rated BBB+/A-1 or better by Standard & Poor's or equivalent rating by Moody's Investors Service or Fitch Ratings, depending on the type and maturity of the investment and the counterparty to the transaction. Any exceptions must be approved by the Bank's board of directors. The investment policies also provide that purchases and sales of investment securities shall be made using the delivery vs. payment procedures.

The Bank's investment policies also provide that the Asset Liability Management Committee (ALCO) is responsible for implementing and monitoring the Bank's interest rate risk policies and strategies. The ALCO meets on a monthly basis to coordinate and monitor the interest rate risk management of interest sensitive assets and interest sensitive liabilities, including matching of their anticipated level and maturities, consistent with the Bank's liquidity, capital adequacy, risk and profitability goals set by the Bank's board of directors.

The following table summarizes the type and maturities of investments held by the Bank at June 30, 2011. Investments by type in any one issuer representing 5% or more of total investments of either the Bank or its blended component units have been separately disclosed. Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Investment Type	Within One Year	After One to Five Years	After Five to Ten Years	After Ten Years	Total
U.S. Treasury bills	$ 843,858,209	$ -	$ -	$ -	$ 843,858,209
U.S. Treasury notes	200,749,558	553,547,664	438,162,500	50,023,438	1,242,483,160
U.S. sponsored agencies notes:					
Federal National Mortgage Association ("FNMA")		25,051,650		1,550,783	26,602,433
Federal Home Loan Bank ("FHLB")	150,005,500	572,646,875			722,652,375
Federal Home Loan Mortgage Corporation ("FHLMC")		76,585,920			76,585,920
Federal Farm Credit Bank ("FFCB")		79,507,335			79,507,335
Mortgage and asset-backed securities:					
Government National Mortgage Association ("GNMA")	79,387	2,797,706	3,258,505	467,070,128	473,205,726
Federal National Mortgage Association ("FNMA")			110,318,422	467,882,745	578,201,167
FHLMC			88,497,892	356,687,331	445,185,223
Other			287,059		287,059
Corporate debt:					
Goldman Sachs	4,000,160				4,000,160
General Electric	708,680	4,110,146			4,818,826
Andrew Mellow Foundation		3,159,600			3,159,600
Walmart Stores		2,116,340			2,116,340
First Puerto Rico Family of Funds	50,000,000				50,000,000
External investment pools—					
Fixed-income securities	123,186,460				123,186,460
PR Housing Bank Portfolio II bonds				4,744,394	4,744,394
Nonparticipating investment contracts:					
American International Group				198,151,692	198,151,692
Other				98,484,022	98,484,022
U.S. Municipal notes	1,418,382	74,073,529	58,599,962	71,186,679	205,278,552
Commonwealth agency bonds	-	3,530,000	-	46,326,069	49,856,069
Total investments	$ 1,374,006,336	$ 1,397,126,765	$ 699,124,340	$ 1,762,107,281	5,232,364,722
External investment pools:					
Equity securities:					
Russell 1000 Growth Common Trust Fund					47,581,657
Global Opportunities Capital Appreciation Fund					14,757,197
Preferred securities / interests:					
Grupo Hima San Pablo					3,642,563
Desarrolladora del Norte					50,000,000
Other					247,436
Total					$ 5,348,593,575
Reconciliation to the government-wide statement of net assets					$ 3,775,241,121
Unrestricted investments and investment contracts					1,573,352,454
Restricted investments and investment contracts					$ 5,348,593,575

Investments in fixed-income external investment pools had an average maturity of less than 60 days; accordingly, they were presented as investments with maturity of less than one year. These investments include $117,362,255 invested in the Puerto Rico Government Investment Trust Fund, a government-sponsored pool, which is administered by the Bank. This pool is subject to regulatory oversight by the Commissioner of Financial Institutions of Puerto Rico. The fair value of the pool is the same as the value of the pool shares.

At June 30, 2011, the total amount of $9,386,086 of the Bank's investment in corporate debt maturing over one year, bear a fixed interest rate. Also, at June 30, 2011, approximately 32% of the Bank's investments in mortgage and asset-backed securities were held by trustees in connection with bonds issued by the Housing Finance Authority, the terms of which generally provide for early redemption of the bonds if the securities are early repaid.

All of the Bank's investments in U.S. Treasury securities and mortgage-backed securities guaranteed by GNMA carry the explicit guarantee of the U.S. government. The credit quality ratings for investments in debt securities, excluding U.S. Treasury securities and mortgage-backed securities guaranteed by GNMA, at June 30, 2011 are as follows:

	Credit Risk				
	Rating				
Securities Type	**AAA to A-**	**BBB**	**B**	**Not Rated**	**Total**
U.S. sponsored agencies notes:					
FNMA	$ 26,602,433	$ -	$ -	$ -	$ 26,602,433
FHLB	722,652,375				722,652,375
FHLMC	76,585,920				76,585,920
FFCB	79,507,335				79,507,335
Mortgage-backed and asset-backed securities:					
FNMA	578,201,167				578,201,167
FHLMC	445,185,223				445,185,223
Other	16,861			270,198	287,059
Corporate debt	64,094,926				64,094,926
External investment pools —					
Fixed-income securities	123,186,460				123,186,460
PR Housing Bank Portfolio II bonds	4,744,394				4,744,394
Nonparticipating investment contracts	254,832,428	41,803,286			296,635,714
U.S. municipal notes	205,278,552				205,278,552
Commonwealth agency bonds				49,856,069	49,856,069
Total	$2,580,888,074	$41,803,286	$ -	$50,126,267	$2,672,817,627

The credit quality ratings of nonparticipating investment contracts are based on the credit quality ratings at June 30, 2011 of the counterparties with whom these contracts are entered into. The credit quality ratings of the counterparties should follow the ratings required by the investment policies of the Bank.

As of June 30, 2011, the Bank had pledged investments and investment contracts to secure the following:

Payment of principal and interest on obligations issued by a blended component unit	$ 675,952,789
Securities sold under agreements to repurchase	970,818,550
Certificates of indebtedness	4,300,000

5. LOANS RECEIVABLE AND ALLOWANCE FOR LOAN LOSSES

Loans at June 30, 2011 consist of the outstanding balance of credit facilities granted to the following (in thousands):

	GDB Operating Fund (1)	Tourism Development Fund	Housing Finance Authority	Development Fund	Total
Public corporations and agencies	$6,002,823	$ -	$ -	$ -	$6,002,823
Municipalities	1,792,058				1,792,058
Allowance for loan losses	(4,000)				(4,000)
Total loans to public sector	7,790,881	-	-	-	7,790,881
Private sector	5,000	432,298	302,371	17,375	757,044
Allowance for loan losses	(264)	(86,815)	(35,655)	(9,320)	(132,054)
Deferred origination fees			(19,912)		(19,912)
Total loans to private sector	4,736	345,483	246,804	8,055	605,078
Balance — end of year	$7,795,617	$345,483	$246,804	$8,055	$8,395,959

(1) Excluding loans to component units.

Reconciliation to the government-wide statement of net assets:	
Unrestricted loans receivable — net	$8,360,977
Restricted loans receivable — net	34,982
Total	$8,395,959

For the year ended June 30, 2011, public sector loan originations and collections amounted to $4.6 billion and $3.2 billion, respectively.

Public sector loans amounting to approximately $2.3 billion as of June 30, 2011 were delinquent by 90 days or more or had matured. Public sector loans classified as nonaccrual amounted to approximately $57 million at June 30, 2011. Interest income that would have been recorded if such nonaccrual loans had been accruing in accordance with their original terms was approximately $1.9 million in 2011. Interest collected on these loans during the year ended June 30, 2011 was not material.

At June 30, 2011, loans to public corporations and agencies of the Commonwealth amounting to $6,002,823 were repayable from the following sources (in thousands):

Repayment Source	**Amount**
Proceeds from future bond issuances of public corporations	$ 1,646,025
Operating revenues of public entities other than the Commonwealth	1,554,059
Legislative appropriations — previously from issuance of Commonwealth's general obligation bonds	1,116,859
Legislative appropriations — previously from FIA Fund	770,799
Legislative appropriations — other	848,239
Other — including funds from federal grants	66,842
Total	$ 6,002,823

During fiscal year 2011, the Bank received $63.1 million and $101.4 million of appropriations to repay principal of and interest on public sector loans whose repayment source was originally from the FIA Fund and from future issuances of Commonwealth's general obligations bonds, respectively. The Commonwealth's general fund budget for fiscal year 2012 includes $65.1 million and $91.5 million of appropriations to repay principal of and interest on public sector loans whose repayment source was originally from the FIA Fund and from future issuances of Commonwealth's general obligations bonds, respectively. These appropriations are based on payment schedules proposed by the Bank, which are based on a period of amortization of 30 years each, at contractual interest rates. The Bank will annually submit to the OMB, to be included in the Commonwealth's budget for legislative approval in each subsequent fiscal year, an amount established in the payment schedules with the terms stated above. The Bank expects that future appropriations will be approved by the Legislature of the Commonwealth to comply with such schedules. However, there can be no assurance that the director of OMB will include an amount for loan repayments in the Commonwealth's budget, and that the Legislature will appropriate sufficient funds in the future to cover all amounts due to the Bank on these loans.

Since one of the Bank's principal functions is to provide financing to the Commonwealth and its instrumentalities, the Bank's loan portfolio includes loans to various departments and agencies of the Commonwealth, to various public corporations, and to municipalities, which represent a significant portion of the Bank's assets. Loans to the Commonwealth and its departments and agencies typically include working capital lines of credit payable from short-term tax and revenue anticipation notes issued by the Commonwealth, interim financing of capital improvements payable from Commonwealth general obligation bonds or revenue bonds issued by the corresponding agency and, in recent years, loans to finance the Commonwealth's budget deficit payable from the FIA Fund, uncollected taxes and annual appropriations made by the Legislature of Puerto Rico. Loans to the public sector, excluding municipalities, amounted to approximately $6.0 billion or 38.7% of the Bank's government-wide total assets at June 30, 2011.

At June 30, 2011, approximately $2.7 billion of the public sector loans are payable from legislative appropriations from, or future tax revenues of, the Commonwealth. Accordingly, the payment of these loans may be affected by budgetary constraints, the fiscal situation and the credit rating of the Commonwealth. Significant negative changes in these factors may have an adverse impact on the Bank's financial condition. From fiscal years 2003 to fiscal year 2010, the Commonwealth's recurring expenditures have exceeded its recurring revenues. These shortfalls were partially covered with loans from the Bank and other nonrecurring revenues. In addition, the Commonwealth has preliminary estimated that its expenditures will exceed its revenues for fiscal year 2011. From fiscal year 2003 to 2008, the Bank granted loans to the Commonwealth aggregating to $1,964 million to cover part of the

Commonwealth's deficit. As of June 30, 2011, the outstanding principal amount of these loans was $227 million.

In addition, at June 30, 2011, approximately $3.3 billion of public sector loans are payable from proceeds from future bond issuances and operating income of public corporations of the Commonwealth. The Bank lends funds to such public corporations for capital improvements and operating needs. The loans for capital improvements generally are construction loans and are repaid from the proceeds of future bond issuances of the respective public corporations. Such loans may, however, also be repaid from the revenues of such public corporations, from loans provided by sources other than the Bank, from federal grants, and from the sale of assets of such public corporations. The amount of outstanding loans from the Bank to the public corporations fluctuates annually, depending upon the capital program needs of the public corporations, the timing and level of their capital expenditures, and their ability to gain access to the long-term capital markets. The participation of certain of these public entities in the bond market has been delayed waiting for the credit rating of such entities to improve or for more favorable market conditions. At June 30, 2011, the Bank has approximately $1.3 billion and $1 billion of loans outstanding due from the Puerto Rico Highways and Transportation Authority and the Puerto Rico Aqueduct and Sewer Authority, representing approximately 71% of the $3.3 billion mentioned above. As explained below, to manage the credit risk of these and other debtors, the Bank has entered into fiscal oversight agreements, whereby the Bank, among other things, imposes conditions on the extensions of credit to these entities and continually monitors their finances. The default by any such and other public sector borrowers on the Bank's loans may have a material adverse effect on the financial condition and operating results of the Bank.

Starting in fiscal year 2010, as part of its risk management activities and as a condition to provide financing support to certain public corporations, GDB has entered into fiscal oversight agreements with such public corporations. The agreements require the public corporations, among other, to implement a comprehensive expense reduction program, including certain fiscal oversight controls, subject to laws and existing agreements of the public corporations, designed to minimize future tariff increases to households and the private sector, and to protect and improve the credit rating of the public corporations, so that the public corporations may obtain adequate financing to fund its capital expenditure requirements and to operate its infrastructure in an efficient and reliable manner and in compliance with applicable laws and regulations. GDB's agreement to provide current financing and any future financing is expressly conditioned upon the public corporations' compliance with the covenants established in the fiscal oversight agreement and GDB's right to monitor and enforce such compliance. These agreements will be in effect until the public corporations have regained a level of financial stability and are able to secure long-term financing that will result in the continued stability of the public corporations' operations and financial condition. As of June 30, 2011, management of the Bank determined that all public corporations and agencies have complied with the material terms and conditions of their respective agreements.

Also, as part of its role of providing financing to the Commonwealth and its instrumentalities to further the economic development of Puerto Rico, and as part of its risk management activities, the Bank is renegotiating and/or restructuring payment terms of the loans to certain governmental entities. Some of the renegotiations/restructurings extend the period for principal repayment but provide for repayment of the contractual interest in accordance with the original terms.

In addition, due mainly to the Commonwealth's financial situation and the unfunded status of the Puerto Rico Government Employee Retirement System, which represents a challenge that could affect Puerto Rico's credit rating, major credit rating agencies, such as Moody's Investors Service ("Moody's") Standards & Poor's Rating Services (S&P), and Fitch, Inc. ("Fitch") have downgraded the Commonwealth's credit ratings during the past years.

However, on March 7, 2011, S&P raised its rating on the Commonwealth unenhanced general obligation bonds to BBB with a stable outlook from BBB- with a positive outlook and assigned such rating to the bonds issued by the Commonwealth. In taking this rating action, S&P stated that the upgrade reflects the Commonwealth's recent revenue performance and continued efforts to achieve fiscal and budgetary balance. S&P noted, however, that other medium-term budget pressures, such as the Commonwealth's retirement benefit obligations, remain a limiting credit factor. S&P's stable outlook is based on the Commonwealth's recent implementation of significant expenditure controls and revenue enhancement measures that could help restore balance within the next two years. S&P also stated that it would raise the rating if, over the upcoming two years, in conjunction with an improvement in the Commonwealth's economic performance, budget controls remain in place and there is continued progress toward achieving balance between ongoing revenues and expenditures as well as in addressing the Commonwealth's unfunded retirement benefit obligations. At June 30, 2011, the credit rating assigned by Moody's, S&P, and Fitch to the general obligation bonds of the Commonwealth was A3 with a negative outlook and on watchlist, BBB with a stable outlook, and BBB+ with a stable outlook, respectively.

Subsequent to year end, on August 8, 2011, Moody's lowered its rating on the Commonwealth's unenhanced general obligation bonds to Baa1 with a negative outlook from A3. This rating action was a result of Moody's review of the Commonwealth's rating, which had been placed on watchlist on May 3, 2011. In taking this rating action, Moody's stated the downgrade reflects the continued financial deterioration of the severely underfunded retirement systems, continued weak economic trend, and weak finances, with a historical trend of funding budget gaps with borrowings. Moody's negative outlook reflects the stress the Commonwealth will face in the next few years as it continues to address the underfunding of the retirement systems from an already weak financial and economic position. The downgrade and negative outlook also affects bonds whose ratings are determined by or linked to that of the Commonwealth, including the Bank's outstanding notes previously issued under an indenture, which were downgraded to Baa1.

Also, on August 8, 2011, S&P reaffirmed its BBB rating of the Commonwealth's unenhanced general obligation bonds.

In an effort to address the Commonwealth's structural budget imbalance, the Legislature enacted Act No. 117 of July 4, 2006 ("Act No. 117"), which amended the Puerto Rico Internal Revenue Code of 1994 to provide, among other things, for a general sales and consumption tax of 5.5% (the "Sales Tax") to be imposed by the Commonwealth. Act No. 117 also eliminated the 5% general excise tax imposed on imported goods and the 3.6% general excise tax on goods manufactured in Puerto Rico, and provided certain income tax reductions to taxpayers. The Sales Tax was effective on November 15, 2006.

Act No. 91 was amended by Act No. 291, enacted on December 26, 2006, and by Act No. 56, enacted on July 6, 2007, to create the Puerto Rico Sales Tax Financing Corporation (the "Sales Tax Corporation") as an independent governmental instrumentality that will own and hold the FIA Fund for the purpose of financing the payment, retirement or defeasance of the extra-constitutional debt. Pursuant to Act No. 91, ownership of the FIA Fund, was transferred to the Sales Tax Corporation.

On January 14, 2009, Act No. 91 was amended by Act No. 1 ("Act No. 1") to increase the Pledged Sales Tax to 2% of the Commonwealth's share of the sales and consumption tax. Furthermore, Act No. 1 amended Act No. 91 to allow the use of the proceeds of future bond issuances by the Sales Tax Corporation to, among other, pay principal and/or interest of loans granted by the Bank to the Commonwealth payable from future Commonwealth general obligation bonds and any debt of the Commonwealth outstanding as of December 31, 2008 that did not have source of repayment or was payable from budgetary appropriations.

Finally, Act No. 7 of March 9, 2009 amended Act No. 91 to increase the Pledged Sales Tax, effective July 1, 2009, by an additional 0.75% or to 2.75%, which represents 50% of the Commonwealth's share of the sales and consumption tax. In addition, Act. No. 7 created an integrated plan for the Commonwealth's fiscal stabilization that includes: (i) operating expense-reduction measures, including various workforce reduction initiatives and a temporary halt of salary increases and other economic benefits included in certain laws and collective bargaining agreements; (ii) tax revenue enforcement measures; (iii) a combination of permanent and temporary tax increases, and (iv) other financial measures, including the increase of the Pledged Sales Tax. During the fiscal year ended June 30, 2011, the Bank collected interest amounting to approximately $6.6 million on outstanding public sector loans from funds held by the Sales Tax Financing Corporation.

Although the Commonwealth is using its best efforts to maximize revenues and reduce expenditures, there can be no assurance that its future revenues will be greater than its expenditures.

Based on previous experience and recent developments, management of the Bank believes that the carrying amount of the loans to the public sector will be collected (including interest at the contractual interest rate), and, accordingly, no additional allowance for loan losses to the public sector is needed at June 30, 2011.

Loans to the private sector include the outstanding principal balance of credit facilities granted by the Bank and the Development Fund to private enterprises in Puerto Rico, the activities of which are deemed to further the economic development of Puerto Rico. They also include the outstanding principal balance of mortgage loans granted to low and moderate-income families for the acquisition of single-family housing units and to developers of low and moderate-income multifamily housing units in Puerto Rico, and direct loans to tourism projects. These credit facilities, net of allowance for loan losses, amounted to approximately $600.3 million at June 30, 2011 of which approximately $246.8 million are mortgage loans for low and moderate-income housing units and approximately $345.5 million are for tourism projects.

Private sector loans classified as nonaccrual amounted to approximately $211 million at June 30, 2011. Interest income that would have been recorded if these loans had been performing in accordance with their original terms was approximately $11 million in 2011. No interest was collected on these loans for the year ended June 30, 2011.

The following is a summary of private sector loans of the enterprise funds considered to be impaired as of June 30, 2011, and the related interest income for the year then ended (in thousands):

	Enterprise Funds				
	GDB Operating Fund	Housing Finance Authority	Tourism Development Fund	Development Fund	Total
Recorded investment in impaired loans:					
Not requiring an allowance for loan losses	$ 129	$ 3,334	$ -	$ -	$ 3,463
Requiring an allowance for loan losses	264	48,253	141,062	16,930	206,509
Total recorded investment in impaired loans	$ 393	$ 51,587	$ 141,062	$ 16,930	$ 209,972
Related allowance for loan losses	$ 264	$ 33,643	$ 76,502	$ 9,387	$ 119,796
Average recorded investment in impaired loans	-	58,781	134,331	8,465	201,577
Interest income recognized on impaired loans	-	562	-	-	562

The following is a summary of the activity in the allowance for loan losses for the year ended June 30, 2011 (in thousands):

	Enterprise Funds				
	GDB Operating Fund	Housing Finance Authority	Tourism Development Fund	Development Fund	Total
Balance — beginning of year	$ 9,814	$ 28,970	$ 55,763	$ -	$ 94,547
Provision (credit) for loan losses	(5,550)	7,547	31,052	9,320	42,369
Transfer to enterprise funds					-
Net charge-offs		(862)			(862)
Balance — end of year	$ 4,264	$ 35,655	$ 86,815	$ 9,320	$ 136,054

6. DUE FROM FEDERAL GOVERNMENT

Under the New Secure Housing Program (the "Program"), the Housing Finance Authority is responsible for administering the Program, including contracting, supervising and paying the designers, inspectors, and legal services needed for the Program. The Housing Finance Authority also provides all the funding for the Program through a $67 million nonrevolving line of credit with the Bank. The Department of Housing is responsible for land acquisitions, auctioning projects, awarding construction contracts, qualifying participants, and selling housing units to eligible participants.

Under the terms of the grant, the construction of, and relocation of participants into new secure housing facilities was to be completed by December 31, 2007. In addition, FEMA would reimburse 75% of the allowable costs of the Program. Funds collected under the Program since its inception amounted to approximately $113 million and are subject to compliance audits under OMB Circular A-133 and federal granting agencies audits.

In April 2007, FEMA discontinued reimbursing the Housing Finance Authority's allowable costs based on the Program's noncompliance with the scheduled dates for construction activities and case management. The Department of Housing requested a one-year extension, up to December 31, 2008, and although original request was denied, FEMA granted such request in 2007.

On June 6, 2008, the Department of Housing requested an additional one-year extension, up to December 31, 2009, for the completion of the construction and relocation of participants into new secure housing facilities. On July 1, 2008, FEMA denied the additional one-year extension. The Department of Housing requested through the Governor's Authorized Representative (GAR) on September 19, 2008, a reconsideration of FEMA's decision not to grant the extension. On December 23, 2008 FEMA granted an extension up to June 30, 2010.

Although significant progress was made through June 30, 2010 in the construction activities and in the case management of the Program, the Housing Finance Authority was not able to fully comply with the terms of the extension granted by FEMA. On September 30, 2011, the Housing Finance Authority provided FEMA and the GAR the program closeout documentation, which is under FEMA's review. Based on this and the fact that no reimbursements have been received from FEMA since April 2007, management has decided to establish an allowance for the $26 million due from the FEMA at June 30, 2011.

The Housing Finance Authority, as a public housing agency, is authorized to administer the U.S. Housing Act Section 8 Programs in Puerto Rico. The revenues and expenses of such federal financial assistance are accounted for as a major governmental fund under the HUD Programs fund. Revenues and expenditures related to the administration of the U.S. Housing Act Section 8 Programs amounted to approximately $127.1 million during the year ended June 30, 2011. This amount includes approximately $4,980,000 of administrative fees for services performed as contract administrator, which are reimbursed by HUD. As of June 30, 2011, the amounts due from federal government under the HUD Programs fund amounted to approximately $1.3 million.

In addition, on February 17, 2009, the American Recovery and Reinvestment Act of 2009 (ARRA) was signed into law in the United States of America. The purpose of ARRA is to jumpstart the nation's ailing economy with the primary focus on creating and saving jobs in the near term and investing in infrastructure that will provide long-term economic benefits. The Housing Finance Authority expended $95.7 million of ARRA program funds during the year ended June 30, 2011, of which $11.2 million are due from the federal government at June 30, 2011.

During 2010, the Housing Finance Authority received from the Department of Housing approximately $1.6 million of cash and approximately $17 thousand in capital assets, as well as liabilities amounting to approximately $1.6 million, that were held by the Department of Housing as the previous administrator of the HOME Program. This transaction did not have an effect on the Housing Finance Authority's 2011 statement of activities and statement of revenues, expenditures, and changes in fund balances – governmental funds.

During the year ended June 30, 2011, the Housing Finance Authority expended $16.6 million of HOME Program funds, of which $8.7 million are due from the federal government as of June 30, 2011. In accordance with the Housing Finance Authority's accounting policies, the Housing Finance Authority has deferred the recognition of revenue of approximately $4.6 million due from the federal government as such amounts are not considered to be available. This amount has been recorded as a deferred revenue in the accompanying balance sheet – governmental funds.

7. REAL ESTATE AVAILABLE FOR SALE

Real estate available for sale at June 30, 2011 consisted of the following:

	GDB Operating Fund	Housing Finance Authority	Total
Residential (1–4 units)	$ -	$ 13,653,479	$ 13,653,479
Commercial	138,800,232		138,800,232
Valuation allowance	(13,121,013)	(10,764,378)	(23,885,391)
Total real estate available for sale	$125,679,219	$ 2,889,101	$128,568,320

Reconciliation to the government-wide statement of net assets (deficiency):

Unrestricted real estate available for sale	$126,641,380
Restricted real estate available for sale	1,926,940
Total	$128,568,320

The following is a summary of the activity in the valuation allowance for the year ended June 30, 2011:

	GDB Operating Fund	Housing Finance Authority	Total
Balance — beginning of year	$ 13,121,013	$ 7,443,470	$ 20,564,483
Provision for possible losses	-	4,089,470	4,089,470
Write-offs	-	(768,562)	(768,562)
Balance — end of year	$ 13,121,013	$ 10,764,378	$ 23,885,391

During fiscal year 2009, the Bank entered into an agreement with an agency of the Commonwealth whereby the Bank received several properties with appraised values (based on appraisals made near the transaction date) of $155.9 million in lieu of payment of a loan whose principal balance and accrued interest receivable amounted to $144.2 million at December 30, 2008. Management of the Bank has subsequently obtained appraisals of the properties, which have resulted in a decrease in the appraised values of certain of such properties, net of estimated selling costs, of approximately $62 million, which have been recorded as a reduction of the carrying value of the properties (included within real estate available for sale in the accompanying statement of net assets) and a receivable from the Commonwealth's agency [included within other receivables in the accompanying statement of net assets (deficiency)]. The interagency agreement provides that the agency of the Commonwealth shall transfer to the Bank additional properties to cover any deficiency in the properties values during a period of five years. In addition, on October 16, 2011, the Bank obtained a commitment from the director of the OMB, whereby OMB commits to pay $7.5 million to the Bank before December 31, 2011 to cover a portion of the outstanding balance at June 30, 2011. In addition, the director of the OMB has committed to include in the Commonwealth's general fund budget, for legislative approval, appropriations of approximately $3.8 million, plus interest at 7%, for the next 15 years to cover the remaining balance. The Legislature is not obligated to authorize such appropriations. Management of the Bank is of the opinion that it will receive properties or cash to cover such deficiency and, accordingly, believes that no valuation allowance on the receivable from the Commonwealth's agency is needed at June 30, 2011.

8. CAPITAL ASSETS

Capital assets activity for the year ended June 30, 2011, was as follows:

Governmental Activities:

	Beginning Balance	Additions	Reductions/ Reclassifications	Ending Balance
Capital assets:				
Information systems	$ -	$ 66,329	$ -	$ 66,329
Office furniture and equipment	-	33,967	-	33,967
Vehicles	-	66,135	-	66,135
Total capital assets	-	166,431	-	166,431
Less accumulated depreciation and amortization for:				
Information systems	-	(35,494)	-	(35,494)
Office furniture and equipment	-	(23,094)	-	(23,094)
Vehicles	-	(66,132)	-	(66,132)
Total accumulated depreciation and amortization	-	(124,720)	-	(124,720)
Capital assets governmental activities — net	$ -	$ 41,711	$ -	41,711

Business Type - Activities

Capital assets not being depreciated — land	Beginning Balance	Additions	Reductions/ Reclassifications	Ending Balance
Land	$ 2,845,000	$ -	$ -	$ 2,845,000
Land under development	-	-	56,454,861	56,454,861
	2,845,000	-	56,454,861	59,299,861
Total capital assets not being depreciated				
Capital assets being depreciated:				
Building	8,988,048	-	-	8,988,048
Leasehold improvements	4,429,170	53,599	(21,058)	4,461,711
Information systems	3,707,774	86,193	(1,762,379)	2,031,588
Office furniture and equipment	2,687,793	49,584	(24,686)	2,712,691
Software	3,522,685	1,147,199	(244,712)	4,425,172
Vehicles	217,119	-	(4)	217,115
Total capital assets being depreciated	23,552,589	1,336,575	(2,052,839)	22,836,325
Less accumulated depreciation and amortization for:				
Building	(2,134,660)	(224,701)	2	(2,359,363)
Leasehold improvements	(1,746,839)	(450,359)	21,058	(2,176,140)
Information systems	(2,468,416)	(513,508)	1,372,096	(1,609,828)
Office furniture and equipment	(1,949,436)	(299,324)	407,975	(1,840,785)
Software	(2,163,973)	(1,034,043)	251,443	(2,946,573)
Vehicles	(184,528)	(11,223)	264	(195,487)
Total accumulated depreciation and amortization	(10,647,852)	(2,533,158)	2,052,838	(11,128,176)
Total capital assets being depreciated — net	12,904,737	(1,196,583)	(1)	11,708,153
Capital assets business type activities — net	$15,749,737	$ (1,196,583)	$ 56,454,860	71,008,014
Total capital assets — net				$ 71,049,725

Land under development represents property owned by the Bank that is being developed for future government benefit. It was transferred from real estate available for sale to capital assets as of June 30, 2011, at cost. Specifically, as part of its functions of furthering the economic development of Puerto Rico, the Bank is developing the infrastructure and public spaces of the "Comunidad Río Bayamón Norte" as per the Master Plan approved by the Puerto Rico Planning Board. The infrastructure development includes the construction of the roads, sidewalks, electric, sanitary and sewer systems and an urban park with recreational area, clubhouse and tennis courts. As part of the development, the Bank is contributing to certain offsite improvements with the Puerto Rico Electric and Power Authority, the Puerto Rico Aqueduct and Sewer Authority and the Puerto Rico Highways and Transportation Authority. The development will have access to Tren Urbano's Jardines Station. Management is evaluating the transfer of these improvements and structures to the corresponding governmental agency for the proper maintenance upon completion of the development.

9. DEPOSITS

Deposits consist predominantly of interest-bearing demand accounts, special government deposit accounts, and time deposits from the Commonwealth, its agencies, instrumentalities, and municipalities. Interest expense on these deposits amounted to approximately $94 million in 2011.

10. SECURITIES SOLD UNDER AGREEMENTS TO REPURCHASE

The following is selected information concerning securities sold under agreements to repurchase:

Carrying amount at June 30, 2011	$ 970,818,550
Maximum amount outstanding at any month-end	970,818,550
Average amount outstanding during the year	650,175,776
Weighted average interest rate for the year	2.43%
Weighted average interest rate at year-end	0.13%

The following summarizes the activity of securities sold under agreements to repurchase for the year ended June 30, 2011:

	Beginning Balance	Issuances	Maturities	Ending Balance
GDB Operating Fund	$ 1,058,834,752	$4,477,337,335	$4,565,353,537	$ 970,818,550

All sales of investments under agreements to repurchase are for fixed terms. In investing the proceeds of securities sold under agreements to repurchase, the Bank's policy is for the term to maturity of investments to be on or before the maturity of the related repurchase agreements. At June 30, 2011, the total amount of securities sold under agreements to repurchase mature within one year.

11. CERTIFICATES OF INDEBTEDNESS

Certificates of indebtedness consist of time deposits from corporations that have grants of tax exemptions under the Commonwealth's industrial incentives laws. The following summarizes the certificates of indebtedness activity for the year ended June 30, 2011:

	Beginning Balance	Issuances	Maturities	Ending Balance	Due Within One Year
GDB Operating Fund	$11,800,000	$ -	$ 7,500,000	$ 4,300,000	$4,300,000

At June 30, 2011, certificates of indebtedness amounting to approximately $4.3 million contractually mature during the fiscal year ending June 30, 2012.

12. BONDS, NOTES, AND MORTGAGE-BACKED CERTIFICATES PAYABLE, AND OTHER LIABILITIES

The activity of bonds payable and other borrowed funds for the year ended June 30, 2011 is as follows:

	Beginning Balance	Debt Issued	Debt Paid	Reductions	Ending Balance	Due Within One Year
Governmental activities — Commonwealth appropriation bonds and notes — note payable — AHMSP Stage 7	$4,811,237	$ -	$ -	$ -	$4,811,237	$ -

	Beginning Balance	Additions	Reductions	Ending Balance	Due Within One Year
Business-type activities:					
GDB Operating Fund:					
Adjustable Refunding Bonds	$ 267,000,000	$ -	$ -	$ 267,000,000	$ -
Senior Notes 2006 Series B	428,655,000		(63,295,000)	365,360,000	62,665,000
Senior Notes 2006 Series C	81,960,000			81,960,000	
Senior Notes 2008 Series A	571,533,000		(571,533,000)		
Senior Notes 2008 Series B	195,467,000		(195,467,000)		
Senior Notes 2009 Series A	250,000,000		(250,000,000)		
Senior Notes 2009 Series B	200,000,000		(200,000,000)		
Senior Notes 2009 Series C	1,013,200,000		(53,427,000)	959,773,000	
Senior Notes 2009 Series D	342,876,000		(41,718,000)	301,158,000	
Senior Notes 2010 Series A		1,448,741,000		1,448,741,000	28,316,000
Senior Notes 2010 Series B		151,259,000		151,259,000	
Senior Notes 2010 Series C		1,086,478,000		1,086,478,000	
Senior Notes 2010 Series D		96,411,000		96,411,000	
Senior Notes 2011 Series A		70,000,000		70,000,000	
Senior Notes 2011 Series B		650,000,000		650,000,000	
Add (deduct) unamortized premium (discount)	7,065,393		(2,132,927)	4,932,466	157,136
Total GDB Operating Fund	3,357,756,393	3,502,889,000	(1,377,572,927)	5,483,072,466	91,138,136
Housing Finance Authority					
Mortgage Trust III	904,333,874		(42,530,000)	861,803,874	42,030,000
Revenue bonds:					
Single Family Mortgage Revenue Bonds — Portfolio IX	107,295,000		(9,145,000)	98,150,000	2,210,000
Single Family Mortgage Revenue Bonds — Portfolio X	73,625,000		(3,350,000)	70,275,000	1,275,000
Single Family Mortgage Revenue Bonds — Portfolio XI	18,910,000		(630,000)	18,280,000	310,000
Homeownership Mortgage Revenue Bonds 2000	47,905,000		(3,700,000)	44,205,000	1,065,000
Homeownership Mortgage Revenue Bonds 2001	50,220,000		(4,720,000)	45,500,000	1,210,000
Homeownership Mortgage Revenue Bonds 2003	23,315,000		(1,460,000)	21,855,000	580,000
Mortgage-Backed Certificates — 2006 Series A	120,259,292		(9,070,382)	111,188,910	19,879,063
Total revenue bonds	441,529,292		(32,075,382)	409,453,910	26,529,063
Subtotal	1,345,863,166		(74,605,382)	1,271,257,784	68,559,063
Notes payable:					
GDB	3,495,586	431,395	(1,219,926)	2,707,055	
Special obligation notes	15,000,000	14,000,000		29,000,000	
Citibank notes		80,000,000	(80,000,000)		
Plus unamortized premium	498,253		(36,004)	462,249	
Less unaccreted discount and deferred amount on refunds	(488,082,569)	(6,860,000)	33,302,423	(461,640,146)	
Total Housing Finance Authority	876,774,436	87,571,395	(122,558,889)	841,786,942	68,559,063
Tourism Development Fund:					
Participation agreement payable	26,000,000			26,000,000	
Notes payable to GDB	362,780,208	44,436,268	(7,700,000)	399,516,476	8,400,000
Total Tourism Development Fund	388,780,208	44,436,268	(7,700,000)	425,516,476	8,400,000
Total	4,623,311,037	3,634,896,663	(1,507,831,816)	6,750,375,884	168,097,199
Less intrafund eliminations	(517,105,240)	(44,867,663)	(3,377,726)	(565,350,629)	(8,400,000)
Total business-type activities	$ 4,106,205,797	$ 3,590,029,000	$ (1,511,209,542)	$ 6,185,025,255	$ 159,697,199

The annual debt service requirements to maturity, including principal and interest, for long-term debt, (excluding notes payable by component units to the Bank) as of June 30, 2011 are as follows:

Years Ending June 30,	GDB Operating Fund Business-Type Activities			
	Principal	Interest	Interest Subsidy (1)	Total
2012	$ 90,981,000	$ 261,859,100	$ (4,984,359)	$ 256,874,741
2013	538,934,000	250,917,106	(4,984,359)	245,932,747
2014	601,727,000	229,344,105	(4,984,359)	224,359,746
2015	1,071,850,000	185,696,752	(4,984,359)	180,712,393
2016	469,065,000	154,119,264	(4,984,359)	149,134,905
2017-2021	2,185,103,000	344,613,780	(24,921,801)	319,691,979
2022-2026	520,480,000	67,699,702	(24,803,957)	42,895,745
Total	$ 5,478,140,000	$ 1,494,249,809	$ (74,647,553)	$ 1,419,602,256

(1) The GDB Senior Notes Series 2010 B and 2010 D were issued as Build America Bonds. The Bank will receive a subsidy payment from the federal government equal to 35% of the amount of each interest payment.

Years Ending June 30,	Housing Finance Authority			
	Governmental Activities		Business-Type Activities	
	Principal	Interest	Principal	Interest
2012	$ -	$ 261,554	$ 68,559,063	$ 4,846,999
2013		201,452	57,267,066	4,151,196
2014	95,757	217,922	54,392,294	3,717,371
2015	89,306	215,785	50,536,769	3,306,565
2016	107,858	208,628	49,693,737	2,926,059
2017-2021	554,872	913,724	244,359,480	13,532,646
2022-2026	851,237	731,534	594,191,519	12,289,458
2027-2031	3,112,207	422,339	89,758,935	7,512,229
2032-2036			70,950,433	4,866,472
2037-2040			20,548,488	1,440,264
Total	$4,811,237	$3,172,938	$1,300,257,784	$ 58,589,259

Years Ending June 30,	Tourism Development Fund (1) Business-Type Activities Principal	Interest
2012	$ -	$ 730,600
2013		730,600
2014		730,600
2015		730,600
2016		730,600
2017-2019	26,000,000	1,461,200
Total	$26,000,000	$5,114,200

(1) Debt service requirements of this variable-rate debt assume that the interest rate effective at June 30, 2011 remains the same throughout the term of the debt.

Governmental Activities — Bonds and notes payable by governmental activities as of June 30, 2011 consist of the following:

Description and Maturity Date	Interest Rate	Amount Outstanding
Note payable Affordable Housing Mortgage Subsidy Program Stage 7 — due on July 1, 2014 and each July 1, thereafter to July 1, 2031	4.10%–5.25%	$4,811,237

Note Payable to Puerto Rico Public Finance Corporation — On December 27, 2001, the Housing Finance Authority entered into a loan agreement (the "Note") with the GDB Operating Fund to refinance the Affordable Housing Mortgage Subsidy Program Stage 7 note payable (the "Old Note") of the Housing Bank, as authorized by Act No. 164 of December 17, 2001. The Public Finance Corporation acquired and restructured the Note through the issuance of its Commonwealth appropriations bonds ("PFC Bonds"). The PFC Bonds were issued under a trust indenture whereby the Public Finance Corporation pledged and sold the Note, along with other notes under Act No. 164, to certain trustees and created a first lien on the revenues of the notes sold. The notes payable to the Public Finance Corporation were originally composed of a loan granted by the Bank, which, pursuant to Act No. 164 of December 17, 2001, the Public Finance Corporation acquired and restructured through the issuance of Commonwealth appropriation bonds. These bonds were issued under trust indenture agreements whereby the Public Finance Corporation pledged the notes to certain trustees and created a first lien on the pledged revenue (consisting of annual Commonwealth appropriations earmarked to repay these notes) for the benefit of the bondholders.

During June 2004, the Public Finance Corporation advance refunded a portion of certain of its outstanding Commonwealth appropriation bonds issued in 2001 under Act No. 164 of December 17, 2001. The Housing Finance Authority recognizes a mirror effect of this advance refunding by the Public Finance Corporation in its own notes payable in proportion to the portion of the Housing Finance Authority's notes payable included in the Public Finance Corporation refunding. The aggregate debt service requirements of the refunding and unrefunded notes will be funded with annual appropriations from the Commonwealth.

The outstanding balance of this Note at June 30, 2011 was $4,811,237 and matures on July 1, 2031. Interest on the unpaid principal amount of the Note is equal to the applicable percentage of the aggregate interest payable on the Public Finance Corporation Bonds. Applicable percentage is the percentage representing the proportion of the amount paid by Public Finance Corporation on the PFC Bonds serviced by the Note to the aggregate amount paid by Public Finance Corporation on all the PFC Bonds issued by Public Finance Corporation under Act No. 164.

Business-Type Activities — Bonds, notes and mortgage-backed certificates payable of business-type activities consist of the following:

Description and Maturity Date	Interest Rate		Carrying Amount
Remarketed Refunding Bonds —December 1, 2015	4.75%	$	267,000,000
GDB Senior Notes :			
Series 2006 B — Each December 1 until December 1, 2017	5.00		368,832,386
Series 2006 C — January 1, 2015	5.25		83,420,080
Series 2009 C — Each February 1 from 2011 to 2022	2.50–6.00		959,773,000
Series 2009 D — Each February 1 from 2011 to 2022	2.50–6.00		301,158,000
Series 2010 A — Each August 1 from 2011 to 2020	2.00–5.50		1,448,741,000
Series 2010 B — August 1, 2025	5.75		151,259,000
Series 2010 C — Each August 1 from 2012 to 2019	3.00–5.40		1,086,478,000
Series 2010 D — August 1, 2025	5.75		96,411,000
Series 2011 A — April 1, 2014	3.9		70,000,000
Series 2011 B — May 1, 2014 and May 1, 2016	3.67–4.704		650,000,000
Mortgage Trust III:			
Each July 1 and January 1 until July 1, 2011	Zero Coupon		21,250,000
Each July 1 and January 1 until January 1, 2021	Zero Coupon		241,014,876
Single Family Mortgage Revenue Bonds — Portfolio IX — Each December 1 and June 1 until December 1, 2012	4.85%–5.60%		98,150,000
Single Family Mortgage Revenue Bonds – Portfolio X — Each December and June 1 until December 1, 2037	4.60%–5.65%		70,275,000
Single Family Mortgage Revenue Bonds — Portfolio XI — Each December 1 and June 1 until December 1, 2039	3.460%–5.45%		18,280,000
Homeownership Mortgage Revenue Bonds 2000 Series — Each June 1 and December 1 until December 1, 2032	4.65%–5.20%		44,205,000
Homeownership Mortgage Revenue Bonds 2001 Series:			
Each December 1 until December 1, 2012	4.60%-4.70%		2,495,000
June 1, 2013, and each December 1 and June 1 thereafter until December 1, 2033	5.30%–5.50%		43,005,000
Homeownership Mortgage Revenue Bonds 2003 Series:			
Each December 1 until December 1, 2013	3.80%–4.00%		1,805,000
June 1, 2013, and each December 1 and June 1 thereafter to December 1, 2033	4.375%–4.875%		20,050,000
Mortgage-Backed Certificates, 2006 Series A — Principal and interest payable monthly from September 29, 2006 to August 29, 2030	2.955%–6.560%		99,641,122
Special Obligation Notes, 2010 Series A and B — November 1, 2040	6.96%-6.974%		15,781,791
Total		$	6,159,025,255

GDB Senior Notes, 2010 Series A — On July 29, 2010, the Bank issued $1,448,741,000 of Senior Notes, 2010 Series A (the "2010 Series A Notes"). The 2010 Series A Notes consist of term notes maturing on various dates from August 1, 2011 to August 1, 2020, and carrying fixed interest rates ranging from 2.00% to 5.50%, payable monthly on the first day of each month. The 2010 Series A Notes are subject to redemption prior to maturity at the option of the Bank, either in whole or in part (and if in part, in such order of maturity as directed by the Bank), at a price equal to the principal amount to be redeemed plus accrued interest to the date of redemption, without premium, on August 1, 2011 and on any date thereafter, subject to at least 20 days prior notice.

GDB Senior Notes, 2010 Series B — On July 29, 2010, the Bank issued $151,259,000 of Senior Notes, 2010 Series B (the "2010 Series B Notes"). The 2010 Series B Notes consist of term notes maturing on August 1, 2025, and carrying a fixed interest rate of 5.75 %, payable quarterly on each February 1, May 1, August 1 and November 1. Upon compliance with certain requirements of the U.S. Internal Revenue Code, the Bank will receive a subsidy payment from the federal government equal to 35% of the amount of each interest payment of the Notes. The 2010 Series B Notes are subject to redemption prior to maturity at the option of the Bank, either in whole or in part, at a price equal to the principal amount to be redeemed plus accrued interest to the date of redemption, without premium, on August 1, 2011 and on any date thereafter, subject to at least 20 days prior notice.

GDB Senior Notes, 2010 Series C — On August 24, 2010, the Bank issued $1,086,478,000 of Senior Notes, 2010 Series C (the "2010 Series C Notes"). The 2010 Series C Notes consist of term notes maturing on various dates from August 1, 2012 to August 1, 2019, and carrying fixed interest rates ranging from 3.00% to 5.40%, payable monthly on the first day of each month. The 2010 Series C Notes are subject to redemption prior to maturity at the option of the Bank, either in whole or in part (and if in part, in such order of maturity as directed by the Bank), at a price equal to the principal amount to be redeemed plus accrued interest to the date of redemption, without premium, on September 1, 2011 and on any date thereafter, subject to at least 20 days prior notice.

GDB Senior Notes, 2010 Series D — On August 24, 2010, the Bank issued $96,411,000 of Senior Notes, 2010 Series D (the "2010 Series D Notes"). The 2010 Series D Notes consist of term notes maturing on August 1, 2025, and carrying a fixed interest rate of 5.75 %, payable quarterly on each February 1, May 1, August 1 and November 1. Upon compliance with certain requirements of the U.S. Internal Revenue Code, the Bank will receive a subsidy payment from the federal government equal to 35% of the amount of each interest payment of the Notes. The 2010 Series D Notes are subject to redemption prior to maturity at the option of the Bank, either in whole or in part, at a price equal to the principal amount to be redeemed plus accrued interest to the date of redemption, without premium, on September 1, 2011 and on any date thereafter, subject to at least 20 days prior notice.

GDB Senior Notes, 2011 Series A — On March 2, 2011, the Bank issued $70,000,000 of Senior Notes, 2011 Series A (the "2011 Series A Notes"). The 2011 Series A Notes consist of term notes maturing on April 1, 2014, and carrying a fixed interest rate of 3.90%, payable monthly on the first day of each month.

GDB Senior Notes, 2011 Series B — On May 26, 2011, the Bank issued $650,000,000 of Senior Notes, 2011 Series B (the "2011 Series B Notes"). The 2011 Series B Notes consist of term notes maturing on May 1, 2014 and May 1, 2016, and carrying fixed interest rates ranging from 3.670% to 4.704%, payable semi-annually arrears on the first day of May and November. The 2011 Series B Notes are subject to redemption prior to maturity at the option of the Bank, either in whole or in part (and if in part, in such order of maturity as directed by the Bank), at a price equal to the greater of the principal amount to be redeemed or the sum of the present value of the remaining schedule payments of principal and interest to the maturity date of the 2011 Series B Notes to be redeemed, subject to at least 30 days prior notice.

Special Obligation Notes, 2010 Series A and B — On October 22, 2009 and November 10, 2010, the Housing Finance Authority issued $15,000,000 and $14,000,000 respectively, of Special Obligation Notes, 2010 Series A and 2010 Series B, respectively. These notes are collateralized by certain second mortgage loans originated under the Home Purchase Stimulus Program. The notes will be repaid from collections of principal and interest of the underlying collateral, net of servicing and guarantee fees. The second mortgage loans are guaranteed by the Housing Finance Authority's Act No. 87 insurance fund.

Participation Agreement Payable — On April 10, 2006, the Tourism Development Fund entered into a debt restructuring agreement with Hotel Dorado, S.E. (the "Hotel") whereby the Tourism Development Fund, as guarantor of the Hotel's outstanding bonds, accelerated the payment of the bonds in exchange for a note receivable of $26 million (the "Note") from the Hotel. In addition, on April 10, 2006, the Tourism Development Fund entered into a participation agreement with a financial institution whereby the Tourism Development Fund transferred a 100% participation (the "Participation") in the Note.

The Participation is subject to recourse and the Tourism Development Fund is obligated to purchase the loan from the financial institution upon the occurrence and during the continuance of an event of default under the participation agreement. The participation agreement also stipulates that the financial institution cannot sell, pledge, transfer, assign or dispose of the Participation without the Tourism Development Fund's consent. Accordingly, the Tourism Development Fund has recorded the Note as part of loans receivable and has recorded a participation agreement payable (i.e. a collateralized borrowing) in the accompanying statement of net assets (deficiency) and balance sheet — enterprise funds.

The Participation bears a variable interest rate based on the three-month LIBOR plus 2.50%, until maturity. Interest is payable on a quarterly basis. In August 2008, The Tourism Development Fund agreed to extend the maturity to July 1, 2018 and approved a conditional-commitment to provide a guarantee for a permanent loan to be provided by the financial institution upon completion of the construction of some amenities and subject to compliance with certain conditions. The outstanding principal balance of the Note and the corresponding participation agreement payable amounted to $26 million as of June 30, 2011.

The activity for noncurrent accounts payable and accrued liabilities during the year ended June 30, 2011 follows:

Balance — beginning of period	$ 7,283,627
Additions	766,699
Reductions	(2,877,034)
Balance — end of period	$ 5,173,292

The activity for compensated absences included within accounts payable and accrued liabilities during the year ended June 30, 2011 follows:

	Beginning Balance	Provision	Reductions	Ending Balance	Due Within One Year
Vacation	$2,725,603	$2,339,445	$2,684,075	$2,380,973	$ 2,344,696
Sickness	2,677,182	1,419,170	1,818,652	2,277,700	1,547,278
Total	$5,402,785	$3,758,615	$4,502,727	$4,658,673	$ 3,891,974

Compensated absences are available to be liquidated by the employees during the year.

13. RESTRICTED NET ASSETS — MORTGAGE LOAN INSURANCE FUND

The Mortgage Loan Insurance fund was created by Act No. 87 of June 25, 1965, as amended, known as the *Mortgage Loan Insurance*. This act provides mortgage credit insurance to low- and moderate-income families on loans originated by the Housing Finance Authority and other financial institutions. This activity can be increased through legislative appropriations, if and when needed, and derives its revenue from premiums charged to the borrowers, interest on investments, and sales of properties acquired through foreclosure. The Housing Finance Authority manages the risk of loss of its mortgage loan insurance activities by providing its insurance program only to financial institutions that (1) maintain certain defined minimum capital, (2) are qualified based on experience and resources, (3) perform certain collection efforts, and (4) comply with established procedures and requirements. In addition, the Housing Finance Authority requires certain loan-to-value ratios on loans insured and recording of the collateral in the property registry of the Commonwealth.

During the year ended June 30, 2008, the Housing Finance Authority created the Puerto Rico Housing Administration program, known in Spanish as "FHA Boricua," expanding requirements and parameters under the existing act. The program allows citizens, paying an annual insurance premium, to originate mortgage loans with up to a 98% loan-to-value ratio. The program insures participating lending institutions in events of foreclosure. The program is financed through annual insurance premiums, commitment and transaction fees, and proceeds from any sale of foreclosed real estate. The program also requires participants to comply with various eligibility requirements.

The Commonwealth guarantees up to $75 million of the principal insured by the mortgage loan insurance program. As of June 30, 2011, the mortgage loan insurance program covered loans aggregating to approximately $566 million.

The regulations adopted by the Housing Finance Authority require the establishment of adequate reserves to guarantee the solvency of the Mortgage Loan Insurance Fund. At June 30, 2011, the Housing Finance Authority had restricted net assets for such purposes of approximately $61.1 million and an estimated liability for losses on mortgage loan insurance of approximately $3.7 million.

The summary of the activity in the allowance for losses on mortgage loan insurance for the year ended June 30, 2011, is as follows:

Balance — beginning of year	$ 346,330
Provision for losses on mortgage loan insurance	3,325,677
Claims paid	(3,064,766)
Foreclosed real estate acquired from insured financial institutions	3,064,766
Balance — end of year	$ 3,672,007

14. TERMINATION BENEFITS

On October 13, 2010, the Bank announced to its employees a voluntary termination plan (the "Plan") based on Act No. 70 enacted on July 2, 2010. The Plan was approved by the Bank's board of directors on October 6, 2010. Act No. 70 provides that eligible employees may retire from employment with the Commonwealth in exchange for an early pension, an economic incentive and other benefits. The Plan only applied to employees who were ten years or less from retirement in accordance with their applicable retirement plans as of December 31, 2010. The Plan approved by the Bank's board of directors provides the following:

- The employee will receive an annuity of fifty percent of salary in effect at September 30, 2010. The Bank is responsible for the payment of the annuity in addition to the related employee and employer contributions to the Retirement System for a maximum period of ten years.

- The employee will receive an economic incentive of six month's salary. This incentive is exempt from income taxes as established by Act No. 70.

- The employee will receive the benefits of health and dental insurance for a period of one year.

The total amount of employees that were voluntarily separated from employment was five. Total cost related to these termination benefits was $2.6 million. Employee and employer contributions to the Retirement System and the employee annuity for the applicable period were discounted based on the average interest rate of unpledged investments. As of June 30, 2011, the total liability related to this plan was approximately $2.2 million.

15. FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK

In the normal course of business, the Bank is party to transactions involving financial instruments with off-balance-sheet risk to meet the financing needs of its customers. These financial instruments include commitments to extend credit, standby letters of credit, and financial guarantees. These instruments involve, to varying degrees, elements of credit risk in excess of amounts recognized in the accompanying statement of net assets and fund balance sheets. These off-balance-sheet risks are managed and monitored in manners similar to those used for on-balance-sheet risks. The Bank's exposures to credit loss for lending commitments, financial guarantees, and letters of credit are represented by the contractual amount of those transactions.

Commitments to extend credit are agreements to lend to a customer as long as there is no violation of any condition established in the contract. Commitments generally have fixed expiration dates or other termination clauses and may require payment of a fee. Since many of the commitments are expected to expire without being drawn upon, the total commitment amounts do not necessarily represent future cash requirements. The Bank, as applicable, evaluates each customer's creditworthiness on a case-by-case basis. The amount of collateral obtained upon extension of credit is based on management's credit evaluation of the counterparty. Collateral held varies but may include property, plant, and equipment, and income-producing commercial properties. Standby letters of credit and financial guarantees are written conditional commitments issued by the Bank to guarantee the performance of a customer to a third party. Those guarantees are primarily issued to support public and private borrowing arrangements. The credit risk involved in issuing letters of credit is essentially the same as that involved in extending loan facilities to customers.

At June 30, 2011, the off-balance-sheet risks consisted of the following (in thousands):

Financial instruments whose credit risk is represented by contractual amounts:

Financial guarantees:	
Public sector	$ 52,000
Private sector	357,864
Total	$ 409,864
Standby letters of credit — Public sector	$ 674,429
Commitments to extend credit:	
Public sector	$ 2,418,998
Private sector	51,000
Total	$ 2,469,998

Following is the activity of the allowance for losses on guarantees and letters of credit for the year ended June 30, 2011:

	Beginning Balance	Provision (Credit)	Payments / Reductions	Ending Balance	Due Within One Year
GDB Operating Fund	$ 1,000,000	$ (1,000,000)	$ -	$ -	$ -
Tourism Development Fund	21,284,600	2,370,598	-	23,655,198	-
Development Fund	2,490,804	1,496,066	2,486,870	1,500,000	1,500,000
Total	$ 24,775,404	$ 2,866,664	$ 2,486,870	$ 25,155,198	$ 1,500,000

16. RETIREMENT SYSTEM

Defined Benefit Pension Plan — The Employees' Retirement System of the Government of the Commonwealth of Puerto Rico (the "Retirement System"), created pursuant to Act No. 447 of May 15, 1951, as amended, is a cost-sharing, multiple-employer, defined benefit pension plan sponsored by and reported as a component unit of the Commonwealth. All regular employees of the Bank hired before January 1, 2000 and less than 55 years of age at the date of employment became members of the Retirement System as a condition of their employment. No benefits are payable if the participant receives a refund of their accumulated contributions.

The Retirement System provides retirement, death, and disability benefits pursuant to legislation enacted by the Legislature. Retirement benefits depend upon age at retirement and the number of years of creditable service. Benefits vest after 10 years of plan participation. Disability benefits are available to members for occupational and nonoccupational disabilities. However, a member must have at least 10 years of service to receive nonoccupational disability benefits.

Members who have attained 55 years of age and have completed at least 25 years of creditable service, or members who have attained 58 years of age and have completed 10 years of creditable service, are entitled to an annual benefit payable monthly for life. The amount of the annuity shall be 1.5% of the average compensation, as defined, multiplied by the number of years of creditable service up to 20 years, plus 2% of the average compensation, as defined, multiplied by the number of years of creditable service in excess of 20 years. In no case will the annuity be less than $200 per month.

Participants who have completed 30 years of creditable service are entitled to receive the Merit Annuity. Participants who have not attained 55 years of age will receive 65% of the average compensation, as defined; otherwise, they will receive 75% of the average compensation, as defined.

Commonwealth's legislation requires employees to contribute 5.775% of the first $550 of their monthly gross salary and 8.275% for the excess over $550 of monthly gross salary. The Bank is required by the same statute to contribute 9.275% of each participant's gross salary. On July 6, 2011, Act No. 116 was approved to increase the employer's contribution for each participant. Starting on July 1, 2011, the employer's contribution will be 10.275% and will increase annually by 1.00% until June 30, 2016. Effective July 1, 2016, the employer's contribution will increase by 1.25% annually, until reaching 20.525%.

Defined Contribution Plan — The Legislature enacted Act No. 305 on September 24, 1999, which amended Act No. 447 to establish, among other things, a defined contribution savings plan program (the "Program") to be administered by the Retirement System. All regular employees hired for the first time on or after January 1, 2000, and former employees who participated in the defined benefit pension plan, received a refund of their contributions, and were rehired on or after January 1, 2000, become members of the Program as a condition to their employment. In addition, employees who at December 31, 1999 were participants of the defined benefit pension plan had the option, up to March 31, 2000, to irrevocably transfer their prior contributions to the defined benefit pension plan plus interest thereon to the Program.

Act No. 305 requires employees to contribute 8.275% of their monthly gross salary to the Program. Employees may elect to increase their contribution up to 10% of their monthly gross salary. Employee contributions are credited to individual accounts established under the Program. Participants have three options to invest their contributions to the Program. Investment income is credited to the participant's account semiannually.

The Bank is required by Act No. 305 to contribute 9.275% of each participant's gross salary. The Retirement System will use these contributions to increase its asset level and reduce the unfunded status of the defined benefit pension plan. On July 6, 2011, Act. No. 116 was approved to increase the employer's contribution for each participant. Starting on July 1, 2011, the employer's contribution will be 10.275% and will increase annually by 1.00% until June 30, 2016. Effective July 1, 2016, the employer's contribution will increase by 1.25% annually, until reaching 20.525%.

Upon retirement, the balance in each participant's account will be used to purchase an annuity contract, which will provide for a monthly benefit during the participant's life and 50% of such benefit to the participant's spouse in case of the participant's death. Participants with a balance of $10,000 or less at retirement will receive a lump-sum payment. In case of death, the balance in each participant's account will be paid in a lump sum to the participant's beneficiaries. Participants have the option of receiving a lump sum or purchasing an annuity contract in case of permanent disability.

Total employee contributions for the defined benefit pension plan and the defined contribution plan during the year ended June 30, 2011 amounted to approximately $719,000 and $827,000 respectively. The Bank's contributions during the years ended June 30, 2011, 2010, and 2009 amounted to approximately $1,731,000, $1,910,000, and $1,946,000, respectively. These amounts represented 100% of the required contribution for the corresponding year. Individual information for each option is not available since the allocation is performed by the Retirement System itself.

Additional information on the Retirement System is provided in its stand alone financial statements for the year ended June 30, 2011, a copy of which can be obtained from the Employees' Retirement System of the Commonwealth of Puerto Rico, P.O. Box 42004, San Juan PR 00940-2004.

17. COMMITMENTS AND CONTINGENCIES

Lease Commitments — The Bank leases office and storage space from the governmental and private sectors. Principally, office space is leased under a short-term operating lease agreement that renews automatically every year, if it is not canceled by any of the parties before the beginning of each year. The storage space agreement expires in July 2016. In addition, during fiscal year 2010, the Bank entered into a lease agreement with the Puerto Rico Industrial Development Company (PRIDCO) for office space in PRIDCO's New York Office. This agreement expires in 2022.

The Housing Finance Authority entered into a 30 year lease agreement with the Puerto Rico Department of Housing (PRDH) to rent office space expiring in 2037. During the term of the lease, the Housing Finance Authority will pay an annual rent of $1.5 million. The agreed upon rent includes parking spaces, maintenance and security services in common areas. PRDH will be responsible for the payment of utilities in exchange for an additional payment of $350,000 payable in a lump sum on or before August 31st of each year.

Rent charged to operations in fiscal year 2011 amounted to approximately $2.7 million. At June 30, 2011, the minimum annual future rentals under noncancelable leases are approximately as follows:

Year Ending June 30,	Amount
2012	$ 2,932,000
2013	2,943,000
2014	2,949,000
2015	2,957,000
2016	2,964,000
Thereafter	54,812,000
Total	$69,557,000

Cooperative Development Investment Fund — On August 18, 2002, the Legislature approved Law No. 198, which creates the Cooperative Development Investment Fund. The purpose of this fund is to promote the development of cooperative entities. This fund will be capitalized through contributions to be provided by the Bank up to $25 million to be matched by cooperative entities. As of June 30, 2011, the Bank has contributed $16.9 million to the Cooperative Development Investment Fund, $673,000 of which were contributed during the year ended June 30, 2011.

Other Risks Related to Mortgage Loans Servicing and Insurance Activities — Certain loan portfolios of the Housing Finance Authority are administered by private servicers who are required to maintain an error and omissions insurance policy. The Housing Finance Authority has a program to manage the risk of loss on its mortgage loan lending and insurance activities.

Loan Guarantees — The Development Fund has entered into an agreement (the "Agreement") with Economic Development Bank for Puerto Rico (EDB) whereby the Development Fund would guarantee a portion of loans granted by EDB under a government program named The Key for Your Business (the "Program"). Under the Agreement, the Development Fund would assign $15 million of its capital for the program. The Development Fund guarantees one-third of the outstanding principal balance of each loan plus accrued interest and certain other charges. The Development Fund charges one percent of the loan amount as guarantee fee and no loan can exceed $50,000. At June 30, 2011, the outstanding balance of loans guaranteed amounted to approximately $14.2 million and the allowance for losses on guarantees amounted to by the Development Fund approximately $1.5 million.

Custodial Activities of Enterprise Funds — At June 30, 2011, the Housing Finance Authority was custodian of approximately $212,000 in restricted funds of the former "*Corporación de Renovación Urbana y Vivienda*" (CRUV). As of June 30, 2011, such funds are deposited with the Bank. These funds are not owned by the Housing Finance Authority's enterprise funds and thus are not reflected in the accompanying basic financial statements.

Loan Sales and Securitization Activities — On July 13, 1992, the Housing Finance Authority entered into an agreement to securitize approximately $20.7 million of mortgage loans into a FNMA certificate. The Housing Finance Authority agreed to repurchase, at a price of par plus accrued interest, each and every mortgage loan backing up such security certificate that become delinquent for 120 days or more. As of June 30, 2011, the aggregate outstanding principal balance of the loans pooled into the FNMA certificate amounted to approximately $545,295.

Mortgage Loan Servicing Activities — The Housing Finance Authority acts as servicer for a number of mortgage loans owned by other investors. The servicing is generally subcontracted to a third party. As of June 30, 2011, the principal balance of the mortgage loans serviced for others is approximately as follows:

Popular Mortgage, Inc.	$ 37,609
R-G Mortgage, Inc.	1,439,434
CRUV or its successor without guaranteed mortgage loan payments	42,929
Total	$1,519,972

HOME Program — The U.S. Office of Inspector General (OIG) has performed various examinations of the HOME Program covering fiscal years ended prior to July 1, 2010. These examinations covered the periods in which the HOME Program was under the administration of the Department of Housing. These examinations identified instances of noncompliance with terms and conditions of the grant agreements, applicable federal law, and the HOME Program's regulations, including but not limited to the expenditure of resources for eligible purposes. OIG identified in its examinations disallowed costs amounting to approximately of $18.3 million. The Housing Finance Authority's management is of the opinion that these disallowed costs are a liability of the Department of Housing and, therefore, the Housing Finance Authority has not recorded a contingency in its basic financial statements.

Litigation — The Bank and certain if its component units are defendants in several lawsuits arising out of the normal course of business. Management, based on advice of legal counsel, is of the opinion that the ultimate liability, if any, resulting from these pending proceedings will not have a material adverse effect on the financial position and results of operations of the Bank or its component units.

18. NO-COMMITMENT DEBT AND PROGRAMS SPONSORED BY THE HOUSING FINANCE AUTHORITY

The Public Finance Corporation has issued approximately $5.9 billion of Commonwealth appropriation bonds (the "Bonds") maturing at various dates through 2032. The proceeds of the Bonds, except for approximately $1.7 billion, were used to provide the necessary funds to purchase from the Bank separate promissory notes of the Department of the Treasury of the Commonwealth and certain of its instrumentalities and public corporations (the "Promissory Notes"). The $1.7 billion referred to above were used to refund a portion of certain bonds issued by the Public Finance Corporation (also no-commitment debt) between fiscal years 1995 and 2005. The outstanding balance of the Bonds at June 30, 2011 amounted to approximately $1.6 billion.

The Bonds are limited obligations of the Public Finance Corporation and, except to the extent payable from bond proceeds and investment earnings thereon, will be payable solely from a pledge and assignment of amounts due under the Promissory Notes. Principal and interest on the Promissory Notes are payable solely from legislative appropriations to be made pursuant to acts approved by the Legislature of the Commonwealth. These acts provide that the Commonwealth shall honor the payment of principal and interest on the Promissory Notes, and that the Director of the OMB shall include in the budget of the Commonwealth submitted to the Legislature the amounts necessary to pay the principal and interest on the Notes. The underlying Promissory Notes represent debt of the issuing instrumentalities (all part of the Commonwealth or its component units), and, for purposes of the Public Finance Corporation, the Bonds are considered no-commitment debt. Neither the Bonds nor the Notes purchased with the proceeds therefrom are presented in the accompanying basic financial statements.

Certain bonds of the Housing Finance Authority are considered no-commitment debt as more fully described in Note 2. At June 30, 2011, there were restricted assets held in trust by others, outstanding obligations, fund balances, and excess of fund expenses over revenues, net of transfers (all of which are excluded from the accompanying basic financial statements), as indicated below (unaudited):

Restricted assets	$	1,804,410
Restricted liabilities (no-commitment debt)		1,804,410
Restricted fund balance	$	-
Excess of fund expenses over revenues	$	1,033,159

In December 2003, the Housing Finance Authority issued $663 million in Capital Fund Program Bonds Series 2003 to lend the proceeds thereof to the Public Housing Administration (PHA), a governmental instrumentality of the Commonwealth. PHA utilized such funds for improvements to various public housing projects in the Commonwealth. The Capital Fund Program Bonds Series 2003 are limited obligations of the Housing Finance Authority, which will be paid solely from an annual allocation of public housing capital funds when received from the U.S. Department of Housing and Urban Development and other funds available under the bonds indenture. Accordingly, these bonds are considered no-commitment debt and are not presented in the accompanying basic financial statements. The outstanding balance of these bonds amounted to $179,945,000 million at June 30, 2011.

On August 1, 2008, the Housing Finance Authority issued the Capital Fund Modernization Program Subordinate Bonds amounting to $384,475,000 and the Housing Revenue Bonds amounting to $100,000,000. The proceeds from the issuance were mainly used to finance a loan to a limited liability company (the "LLC") and pay the costs of issuance. The $384,475,000 bonds are limited obligations of the Housing Finance Authority, payable primarily by a pledge and assignment of federal housing assistance payments made available by the U.S. Department of Housing and Urban Development, with an outstanding balance of $343,840,000 at June 30, 2011. The $100,000,000 bonds are also limited obligations of the Housing Finance Authority, payable from amounts deposited in escrow accounts with a trustee and the proceeds of a loan to be made by the Housing Finance Authority to the LLC using moneys received as a grant from the Department of Housing of Puerto Rico. Payment of principal of the Housing Revenue Bonds is also secured by an irrevocable standby letter of credit issued by the Bank. These bonds are considered no-commitment debt and, accordingly, are excluded, along with the related assets held in trust, from the Housing Finance Authority's financial statements.

On February 23, 2009, the Housing Finance Authority entered into an agreement with the Department of Housing of the Commonwealth whereby a limited liability company was incorporated by the name of Puerto Rico Community Development Fund, LLC (PRCDF). PRCDF is a community development entity (CDE). A CDE is any duly organized entity treated as a domestic corporation or partnership for federal income tax purposes that: (a) has a primary mission of serving or providing investment capital for low-income communities or low-income persons; (b) maintains accountability to residents of low-income communities through their representation on any governing board of the entity or any advisory board to the entity; and (c) has been certified as a CDE by the CDFI Fund of the U.S. Department of Treasury. On March 2, 2009, in order to carry out its mission, PRCDF requested New Markets Tax Credits (NMTC). The NMTC Program permits taxpayers to receive a credit against Federal income taxes for making qualified equity investments in designated Community Development Entities. PRCDF received a $45 million NMTC allocation related to 2009.

19. CONTRIBUTION FROM PUERTO RICO INFRASTRUCTURE FINANCING AUTHORITY

On January 14, 2009, the Legislature enacted Act No. 3 to, among other; authorize the Puerto Rico Infrastructure Financing Authority, an affiliate of the Bank, to sell securities deposited at a corpus account, the proceeds of which would be used, among other, to make a contribution to the Bank. Approximately $555 thousand were contributed by the Puerto Rico Infrastructure Financing Authority to the Bank during fiscal year 2011.

20. ESTIMATED FAIR VALUE OF FINANCIAL INSTRUMENTS

For a significant portion of the Bank's financial instruments (principally loans and deposits) fair values are not readily available since there are no available trading markets. Accordingly, fair values can only be derived or estimated using valuation techniques, such as present-valuing estimated future cash flows using discount rates, which reflect the risk involved, and other related factors. Minor changes in assumptions or estimation methodologies may have a material effect on the results derived therefrom.

The fair values reflected below are indicative of the interest rate environment as of June 30, 2011 and do not take into consideration the effects of interest rate fluctuations. In different interest rate scenarios, fair value results can differ significantly. Furthermore, actual prepayments may vary significantly from those estimated resulting in materially different fair values.

The difference between the carrying value and the estimated fair value may not be realized, since, in many of the cases, the Bank intends to hold the financial instruments until maturity, or because the financial instruments are restricted. Comparability of fair values among financial institutions is not likely, due to the wide range of permitted valuation techniques and numerous estimates that must be made in the absence of secondary market prices.

The following methods and assumptions were used by the Bank in estimating fair values of the financial instruments for which it is practicable to estimate such values:

- Short-term financial instruments, such as cash and due from banks, federal funds sold, deposits placed with banks, certificates of deposit, due from federal government, repurchase agreements, certificates of indebtedness, and accrued interest receivable and payable have been valued at the carrying amounts reflected in the statement of net assets, as these are reasonable estimates of fair value given the relatively short period of time between origination of the instruments and their expected realization.

- Financial instruments that are primarily traded in secondary markets, such as most investments, were valued using either quoted market prices or quotations received from independent brokers/dealers or pricing service organizations.

- Financial instruments that are not generally traded, such as long-term deposits placed with banks, investment contracts, long-term certificates of deposit, and bonds, notes and mortgage-backed certificates issued with fixed interest rates, were fair valued using the present values of estimated future cash flows at the appropriate discount rates. Bonds and other borrowings issued with interest rates floating within certain ranges were fair valued at their outstanding principal balance. The fair value of liabilities with no defined maturities, such as demand deposits, was reported as the amounts payable upon demand.

- Loans, participation agreement payable, commitments to extend credit, financial guarantees and standby letters of credit to the private sector are mostly industrial development, tourism development, and low-cost housing development projects. For these types of loans and commitments, there is no secondary market, and the actual future cash flows may vary significantly as compared to the cash flows projected under the agreements, due to the degree of risk. Accordingly, management has opted not to disclose the fair value of these financial instruments, as such information may not be estimated with reasonable precision.

- Disclosure of the fair value of loans, commitments to extend credit, standby letters of credit, and financial guarantees relating to instrumentalities of the Commonwealth is omitted, as these agreements are with component units of the Commonwealth.

The following table presents the carrying amounts and estimated fair values of the Bank's financial instruments at June 30, 2011 (in millions):

Financial assets:		
Cash and due from banks	$ 347	$ 347
Federal funds sold	89	89
Deposits placed with banks	740	740
Due from federal government	21	21
Investments and investment contracts	5,349	5,483
Accrued interest receivable and other receivables	237	237
Financial liabilities:		
Demand deposits	3,783	3,783
Certificates of deposit	1,771	1,775
Certificates of indebtedness	4	4
Securities sold under agreements to repurchase	971	971
Accounts payable and accrued liabilities	149	149
Accrued interest payable	31	31
Bonds, notes, mortgage-backed vertificates and participation agreement payable	6,190	6,355

21. INTERFUND BALANCES AND TRANSFERS

The following table is a summary of the interfund balances as of June 30, 2011 between governmental funds and enterprise funds:

Receivable by	Payable by	Purpose		Amount
Governmental fund:	Enterprise fund:			
Other nonmajor funds (New Secure Housing Program)	GDB Operating Fund	Demand deposits and accrued interest	$	270,014
HUD Programs	GDB Operating Fund	Demand deposits and accrued interest		241,573
Other nonmajor funds (AHMSP Act No. 124)	GDB Operating Fund	Investment agreements and accrued interest		564,063
Other nonmajor funds (AHMSP Act No. 124)	GDB Operating Fund	Demand deposits and accrued interest		674,611
Other nonmajor funds (AHMSP-Stage 7)	GDB Operating Fund	Demand deposits and and accrued interest		97,565
Other nonmajor funds (AHMSP-Stage 8)	GDB Operating Fund	Investment agreements and accrued interest		15,373,338
ARRA Funds	GDB Operating Fund	Demand deposits		276
Closing Costs Assistance Program	GDB Operating Fund	Demand deposits and accrued interest		827,797
My New Home Program	GDB Operating Fund	Demand deposits and accrued interest		3,084,709
Subtotal and balance carried forward				21,133,946

(Continued)

The summary of the interfund balances as of June 30, 2011 between government funds is as follows:

Receivable by	Payable by	Purpose	Amount
Balance brought forward			$ 21,133,946
Governmental fund:	Enterprise fund:		
Other nonmajor funds (New Secure Housing Program)	Housing Finance Authority	Reimbursement of expenditures	20,179
Other nonmajor funds (AHMSP Act. No. 124)	Housing Finance Authority	Reimbursement of expenditures	2,930
Sub total			23,109
Total			$ 21,157,055
Enterprise fund:	Governmental fund:		
GDB Operating Fund	Other nonmajor funds (New Secure Housing Program)	Loans payable and accrued interest	(52,684,188)
GDB Operating Fund	Other nonmajor funds (AHMSP-Stage 7)	Loans payable and accrued interest	(39,281,780)
GDB Operating Fund	Other nonmajor funds (AHMSP-Stage 10)	Loans payable and accrued interest	(13,646,644)
Housing Finance Authority	Other nonmajor funds (AHMSP-Stage 7)	Reimbursement of expenditures	(1,217,841)
Housing Finance Authority	Other nonmajor funds (New Secure Housing Program)	Reimbursement of expenditures	(54,117)
Housing Finance Authority	HUD Programs	Reimbursement of expenditures	(1,149,277)
Housing Finance Authority	My New Home Program	Reimbursement of expenditures	(40,119,127)
Housing Finance Authority	HOME Programs	Reimbursement of expenditures	(678,598)
Total			(148,831,572)
Total internal balances — net			$ (127,674,517)

(Continued)

The summary of interfund balances of June 30, 2011, among governmental funds, is as follows:

Receivable by	Payable by	Purpose	Amount
Governmental fund: Other nonmajor funds (Home Secured Program)	Governmental fund: Other nonmajor funds (AHMSP Act No. 124)	Reimbursement of expenditures	$ 303,809

The summary of interfund balances of June 30, 2011, among enterprise funds, is as follows:

Receivable by	Payable by	Purpose	Amount
Enterprise funds: Housing Finance Authority	Enterprise funds: GDB Operating Fund	Demand deposits and accrued interest	$ 8,241,502
Development Fund	GDB Operating Fund	Demand deposits and accrued interest	11,183,720
Tourism Development Fund	GDB Operating Fund	Demand deposits and accrued interest	21,886,826
Public Finance Corporation	GDB Operating Fund	Demand deposits and accrued interest	1,039,206
Other nonmajor (Education Assistance Corporation)	GDB Operating Fund	Demand deposits and accrued interest	2,381,351
Other nonmajor (JMB Institute)	GDB Operating Fund	Demand deposits and accrued interest	94,583
Housing Finance Authority	GDB Operating Fund	Certificates of deposit and accrued interest	396,767,044
Tourism Development Fund	GDB Operating Fund	Certificates of deposit and accrued interest	4,856,417
Housing Finance Authority	GDB Operating Fund	Guaranteed investment contracts and accrued interest	198,151,692
GDB Operating Fund	Housing Finance Authority	Bonds payable	163,127,098
GDB Operating Fund	Tourism Development Fund	Loans receivable and accrued interest	405,178,042
GDB Operating Fund	Housing Finance Authority	Loan receivable and accrued interest	2,733,900
Total balance among enterprise funds eliminated			$ 1,215,641,381

(Concluded)

The following table is a summary of interfund transfers for the year ended June 30, 2011:

Transfer Out	Transfer In	Transfer for	Amount
Governmental funds:	Governmental funds:		
Other nonmajor funds (AHMSP Stage 11)	Other nonmajor funds (AHMSP Act No. 124)	Release of excess funds	$ 19,601,834
Other nonmajor funds (AHMSP Act No. 124)	Other nonmajor funds (Secured Your Home Program)	Contribution	20,000,000
Other nonmajor funds (AHMSP Stage 7)	Other nonmajor funds (AHMSP Act Stage 6)	Contribution	71
Enterprise Funds:	Governmental Funds:		
Housing Finance Authority	Other nonmajor funds (AHMSP Mortgage Backed Certificates)	Subsidy payments	741,042
Governmental funds:	Enterprise funds:		
Other nonmajor funds (AHMSP Mortgage-backed certificates)	Housing Finance Authority	Debt service payments	305,231
Other nonmajor funds (AHSMP Stage 9)	Housing Finance Authority	Contribution	467,146
Other nonmajor funds (AHMSP-Stage 10)	Housing Finance Authority	Debt service payments	187,896
Other nonmajor funds (AHMSP- Stage 11)	Housing Finance Authority	Debt service payments	759
Enterprise funds: GDB Operating Fund	Enterprise funds: Other nonmajor funds (JMB Institute)	Contribution	178,000

22. FUND BALANCE DEFICIT

The following governmental funds reflect a deficit at June 30, 2011: My New Home Program, AHMSP Stage 7, AHMSP Stage 10, HOME Program and New Secure Housing Program for the amount of $30.8 million, $20.3 million, $8.8 million, $4.2 million and $55.8 million, respectively. The deficit of the My New Home Program, AHMSP Stage 7and AHMSP Stage 10 is due to the amounts borrowed by the Housing Finance Authority from the Bank that were used to provide housing subsidies. The deficit of the New Secure Housing Program is due to discontinued reimbursement of the Housing Finance Authority's allowable costs. The Housing Finance Authority expects to cover these deficits through contributions from the Commonwealth.

23. SUBSEQUENT EVENTS

Subsequent events were evaluated through December 1, 2011, the date the financial statements were available to be issued, to determine if any such events should either be recognized or disclosed in the 2011 financial statements.

On July 1, 2011, the Bank refunded $400 million of its then outstanding Senior Notes Series 2009 C and Series 2009 D.

GDB Senior Notes 2011 — On September 13, 2011, the Bank issued $450 million of Senior Notes, 2011 Series C. The Senior Notes, 2011 Series C mature on October 15, 2012 bearing fixed interest rate of 1.00%. Interest on the Senior Notes, 2011 Series C will be payable on maturity. The Bank used the proceeds to provide a loan to the Secretary of the Treasury of Puerto Rico for the purpose of managing intra-year cash flow needs of the Commonwealth during fiscal year 2012.

On October 5, 2011, the Bank issued $295 million of Senior Notes, 2011 Series D. The Senior Notes, 2011 Series D mature on November 8, 2012 bearing fixed interest rate of 1.00%. The Bank used the proceeds to provide a loan to the Secretary of the Treasury of Puerto Rico for the purpose of managing intra-year cash flow needs of the Commonwealth during fiscal year 2012.

On October 11, 2011, the Bank issued $150 million of Senior Notes, 2011 Series E. The Senior Notes, 2011 Series E mature on April 11, 2012 bearing fixed interest rate of 1.85%. Interest on the Senior Notes, 2011 Series E will be payable on a monthly basis. The Bank used the proceeds for general corporate purposes, including, but not limited to, increasing its investment portfolio, making loans and purchasing obligation of the Commonwealth and its public corporations, instrumentalities and municipalities.

On November 7, 2011, the Bank issued $400 million of Senior Notes, 2011 Series F. The Senior Notes, 2011 Series F mature on January 8, 2013 bearing fixed interest rate of 1.750%. Interest on the Senior Notes, 2011 Series F will be payable on maturity. The Bank used the proceeds for general corporate purposes, including, but not limited to, increasing its investment portfolio, making loans and purchasing obligation of the Commonwealth and its public corporations, instrumentalities and municipalities.

Housing Finance Authority

Special Obligation Notes, 2011 Series A — On October 4, 2011, the Housing Finance Authority issued $18 million of its Special Obligation Notes, 2011 Series A (the "2011 Notes") at an aggregate discounted price of $9,180,000. The 2011 Notes will be collateralized by certain second mortgages originated under the Home Purchase Stimulus Program and will be repaid from collections of principal and interest of the underlying collateral. The second mortgage loans will be guaranteed by the Housing Finance Authority's Act No. 87 insurance.

Restructuring of Mortgage Trust III, Collateralized Mortgage Obligations, Series A — In July 2011, the Housing Finance Authority restructured approximately $425 million face amount of Mortgage Trust III bonds and obtained $60 million of cash from the related collateral. The restructuring took place as follows: 1) tender offer amounting to approximately $144 million (including expenses related to the transaction) to acquire and cancel bonds with a carrying amount of approximately $112 million, and 2) purchase AAA securities amounting to approximately $160 million to establish an escrow for the payment through maturity of bonds with a carrying amount of approximately $129 million.

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