
CHAPTER 6. Ginnie Mae Issuers of Mortgage-Backed Securities Audit Guidance

- 6-1 Program Objective.** The Government National Mortgage Association, also known as Ginnie Mae, is a wholly owned government corporation. Created by Congress in 1968, Ginnie Mae's mission is to support expanded affordable housing in America by providing an efficient government-guaranteed secondary market vehicle linking the global capital markets with the federal housing market. It does this by facilitating secondary market activities for packaged residential mortgages. Through its well-known mortgage-backed securities (MBS) and multiclass programs, Ginnie Mae creates a vehicle for channeling funds from the securities markets into the mortgage market and helps to increase the supply of credit available for housing.
- 6-2 Program Procedures.** The parties involved in the MBS program are Ginnie Mae, the securities issuer, the securities dealer, the investor, a custodian of mortgage documents, a mortgage servicer (often the issuer), and a transfer agent. Once approved by Ginnie Mae, the issuer of the mortgage-backed securities is responsible for: acquiring eligible mortgages; creating a pool of mortgages to be held by a custodian; issuing the securities backed by a pool of mortgages; arranging for the marketing of the securities; servicing the mortgages in the pool; administering the securities outstanding; and, making the full and timely payment of all amounts due to the investors. The issuer is responsible for using its own resources to cover shortfalls in amounts due to investors that result from mortgage delinquencies or foreclosures.

For each pool or loan package of mortgages and accompanying issue of securities, there can only be one issuer. While the issuer is responsible for servicing the pool or loan package of mortgages, the servicing may be carried out on behalf of the issuer by another servicer (hereafter referred to as a subcontract servicer), which must also be a Ginnie Mae-approved issuer. The issuer is responsible and fully liable for the satisfactory performance of any work performed by a subcontract servicer. All activities of any subcontract servicer must be covered by a contractual agreement between the issuer and the subcontract servicer and approved by Ginnie Mae. *The issuer may not delegate or transfer to others its obligations to (a) withdraw funds from a Principal and Interest (P&I) custodial account for any purpose, (b) sign any accounting reports and certifications to Ginnie Mae, and (c) withdraw mortgage documents from the document custodian. In addition to obligations described above, Ginnie Mae I MBS program issuers may not delegate or transfer the following obligations to others: (a) sign checks to Ginnie Mae, (b) sign remittance advice to security holders, (c) fund guaranty fees due Ginnie Mae, and (d) maintain the register for security holders.*

- 6-3 Reference Material.** *Throughout this chapter, reference is made to handbooks using the base handbook number without the revision number (i.e., REV-1, REV-6, etc.). This will enable periodic updates to paragraph 6-3 rather than revising the references in the entire handbook/chapter. Also, the auditor should ensure that the updated reference is used for performing the audit. If reference to the handbook is needed in the audit report, the auditor should ensure that the entire updated reference, including the revision number, is used.

Ginnie Mae program regulations are contained in 24 CFR [*Code of Federal Regulations*] Parts 300 through 395. The HUD Handbook for Ginnie Mae is 5500.3, REV-1, Government National Mortgage Association Mortgage-Backed Securities Guide (MBS Guide). The issuer should have a copy of or access to the guide. The MBS Guide is available on the Internet at www.ginniemae.gov.*

- 6-4 Reporting Requirements.** Ginnie Mae issuers of MBS, including those Ginnie Mae-approved issuers who are inactive, are required to submit the following financial statements, reports, and supplemental information on an annual basis:

Type of report	Reference in IG 2000.4, REV-1
Financial statements and opinion	Chapter 2, section 2-1
Internal controls	Chapter 2, section 2-1
Compliance with specific requirements	Chapter 2, section 2-1
Supplemental information	
Issuer's adjusted net worth	Chapter 6, attachment B
Parent's adjusted net worth (if appropriate)	Chapter 6, attachment C
Insurance requirement	Chapter 6, attachment D
Corrective action plan (if appropriate)	Chapter 1, section 1-9

Nonprofit organizations that elect to submit audited financial statements in accordance with OMB Circular A-133 must also independently submit evidence of meeting Ginnie Mae's fidelity bond and errors and omissions insurance requirements and adjusted net

*worth requirements. The issuer's chief financial officer or executive officer must certify to the accuracy of the unaudited insurance and net worth schedules.

Issuers that did not have outstanding Ginnie Mae securities or commitment authority to issue new securities at any time during the fiscal year under audit do not have to submit an internal controls report, a report on compliance with specific requirements, and supplemental information. However, they must still submit evidence of meeting Ginnie Mae's fidelity bond and errors and omissions insurance requirements and adjusted net worth requirements. The issuer's chief financial officer, president, or chief executive officer must certify to the accuracy of the unaudited insurance and net worth schedules.*

- A. Audited Financial Statements.** Issuers are required to submit audited annual financial statements, which include a balance sheet, statement of operations, cash flow statements, notes to financial statements, and supplemental schedules as stipulated in chapter 2 of this guide. The financial documents are to be submitted to Ginnie Mae's review agent using the transmittal/checklist presented in attachment F to this chapter.
- B. Other Reports.** In addition to the financial statements, all issuers must submit a report on internal controls and a report on compliance with specific requirements. A sample report on consideration of internal controls and report of compliance with specific requirements are included in chapter 2.

The computation of the issuer's and issuer parent's adjusted net worth and computation of issuer's insurance requirements are to be reported on supplemental schedules to the basic financial statements. The computation of the issuer's and issuer parent's adjusted net worth is designed to eliminate those assets considered unacceptable by Ginnie Mae. **Note that the adjusted net worth computation for the issuer's parent is only required when the issuer's parent presents a consolidated financial statement, along with consolidating schedules that reflect the financial condition of the issuer, and the issuer makes up less than 40 percent of the parent's equity.** Similarly, the required reporting format for presenting this analysis is provided in attachment B for the issuer and attachment C for the issuer's parent. The required reporting format for presenting the analysis of the issuer's insurance is presented in attachment D.

Ginnie Mae requires submission of audited financial statements exclusively of the issuer. However, Ginnie Mae will accept alternative financial statements (i.e., not exclusively of the issuer) if certain conditions are met as stated below:

1. For issuers that make up 40 percent or more of the equity of their parent (the 40 percent threshold may be collectively met by related party issuers that have entered into a cross-default agreement with Ginnie Mae), Ginnie Mae will accept consolidated financial statements of the issuer's parent provided that the consolidating schedules, which distinguish the balance sheet and operating

statement of the Ginnie Mae issuer, are included with the parent's audit. The consolidating schedules must be subjected to the auditing procedures applied to the consolidated statement of the parent.

2. For an issuer whose equity is less than 40 percent of the equity of its parent, Ginnie Mae will accept consolidated financial statements of the issuer's parent provided the conditions in item (1) above are met and the issuer's parent enters into a corporate guarantee agreement (agreement) with Ginnie Mae to guarantee the performance of the issuer. The parent must meet the terms and conditions of the agreement for the issuer to remain in good standing with Ginnie Mae.

Further, the issuer is required to submit with its parent's consolidated audited financial statements an adjusted net worth calculation on the parent. The parent's net worth, after adjustments for unacceptable assets, is required to be at least 110 percent (120 percent for issuers approved to issue manufactured housing or multifamily pools) of the required net worth of the issuer. That organization's auditor, in accordance with this audit guide, must audit the parent's audited financial statement and adjusted net worth calculations. The parent must also demonstrate in its adjusted net worth calculation that it meets the 110 percent (120 percent for issuers approved to issue manufactured housing or multifamily pools) requirement noted above.

The required format for presenting the "presentation of adjusted net worth calculation for issuer's parent" is provided in attachment C of this chapter.

3. For issuers that are federal- or state-regulated institutions, such as those under the supervision of the Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, and Office of Thrift Supervision, Ginnie Mae will accept audited financial statements of the issuer's parent, so long as the issuer makes up *40* percent or more of the parent's equity and there is no more than one bank holding company covered in the audit. *In such instances and in addition to the audited financial statement of the issuer's parent, the issuer must submit its unaudited regulatory report (Call report, OTS report, or 10K).*

Although Ginnie Mae may accept alternative audited financial statements, all other required reports (internal controls, compliance with specific requirements, adjusted net worth calculation, insurance requirement) must be prepared by *a certified public accounting firm that is an independent auditor (auditor) exclusively for the issuer.*

A sample auditor's report on the consolidating balance sheet and operating statement is included as attachment E to this chapter.

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- C. **Submission of Reports.** The issuer must submit two copies of the audited financial statements and auditor's reports, independent of whether the issuer had securities or commitment authority outstanding. Reports must be submitted within 90 days of the end of the issuer's fiscal year to Ginnie Mae's review agent. The review agent's address may be obtained from the address list found in the *MBS Guide.*
- D. **Single Auditor Approach.** In many instances, it may be to the advantage of the custodian, the issuer, or both to hire a *certified public accounting firm (auditor)* to conduct a review of the mortgage documents that are held by a particular custodian who has responsibility for several issuers' documents, rather than having each issuer require that a different auditor review that part of the custodial documents pertaining to each issuer's pools. The single auditor approach may also resolve practical problems associated with travel when the issuer, custodian, and auditor are not located near each other, thus reducing the cost of compliance while assuring necessary audit coverage.

To determine whether the single auditor approach is practical in a given situation, the auditor and the issuer should contact the custodian(s) holding the issuer's pool and loan documents to determine the extent of the custodian's activities with other issuers. Arrangements may then be reached as to the most effective approach to conducting the review of custodial documents. Under the single auditor approach, the custodian will arrange with an auditor to review documents relating to each of the respective issuer's pools. The auditor for each issuer's pools will then prepare separate reports.

The single auditor approach and the reviews of custodial documents by the issuer's auditor are both acceptable methods under the Custodial Review section of the audit guide.

6-5 **Compliance Requirements and Suggested Audit Procedures.**

A. **Federal Financial Reports.**

1. **Compliance Requirement.** Issuers participating in HUD-assisted activities are required to ensure that financial status reports contain reliable financial data and are presented in accordance with the terms of applicable agreements between the entity and HUD. The individual agreements contain the specific reporting requirements that the entity is to follow.
2. **Suggested Audit Procedures.**
 - a. Identify all required financial reports by inquiry of the issuer.

- b. Obtain an understanding of the auditee's procedures for preparing and reviewing the financial reports.
- c. Select a sample of financial reports, other than those which are included in the audited financial statements, and determine that the reports selected are prepared in accordance with HUD instructions.
- d. For the sample, trace significant data to supporting documentation; i.e., worksheets, ledgers, etc. Report all material differences between financial reports and issuer records.
- e. Review significant adjustments made to the general ledger accounts affecting HUD-assisted activity and evaluate for propriety.

B. Eligibility to Issue Mortgage-Backed Securities.

- 1. **Compliance Requirement.** To be approved and maintain eligibility to issue Ginnie Mae-guaranteed mortgage-backed securities and act as administrator of such securities, an applicant must meet and maintain the following requirements:
 - a. Be a Federal Housing Administration (FHA)-approved mortgagee in good standing. A state or local government instrumentality that is an FHA-approved mortgagee is eligible. Mortgagees approved by FHA solely as loan correspondents are not eligible to be Ginnie Mae issuers.
 - b. *Maintain its Fannie Mae and/or Freddie Mac approval, which ever they have or both if they have both.* Loss of either approval may cause the issuer to become ineligible to issue and service Ginnie Mae mortgage-backed securities.
 - c. Conduct, as a principal element of its business operation, the origination or servicing of mortgage loans.
 - d. Conduct its business operations in accordance with accepted sound mortgage lending and servicing practices, ethics, and standards and have the experience, management capability, and access to adequate facilities necessary to assure Ginnie Mae of its ability to issue and service mortgage-backed securities. Except in instances in which the issuer can demonstrate that an alternative arrangement constitutes a sound business practice, the issuer must have at least three full-time officers and one additional employee, each with sufficient experience in the origination and/or servicing of mortgages of the type to be pooled to ensure effective pool management on a long-term basis. The officer in charge of day-to-

day operations must be a full-time employee solely of the issuer firm, and the issuer's offices must be self-contained and separate from those of any other entity.

- e. Maintain policies that prohibit any discrimination of a borrower based on race, religion, color, sex, national origin, age, familial status, or disability. The issuer shall comply with any applicable rules, regulations, and orders of general applicability issued under Title VI of the Civil Rights Act of 1964; Executive Order 11063, Equal Opportunity in Housing, issued November 20, 1962; Title VII of the Civil Rights Act of 1968, as amended; and with applicable rules and regulations of the Federal Housing Administration. Moreover, this section incorporates by reference section 202 of Executive Order 11246, Equal Employment Opportunity, issued on September 24, 1965, as amended. The issuer is required to comply with the implementing rules and regulations of the U.S. Department of Labor (41 CFR Part 60-1) and the U.S. Department of Housing and Urban Development (24 CFR Part 130).
- f. Have and maintain fidelity bond coverage and a mortgage servicing errors and omissions policy based on the issuer's total servicing portfolio in accordance with *the MBS Guide, chapters 2 and 3, both of which* name Ginnie Mae as loss payee.
- g. Maintain a net worth based on an audited financial statement prepared in accordance with generally accepted accounting principles in assets acceptable to Ginnie Mae, as outlined in paragraph 6-5, section G.2 of this chapter.

2. Suggested Audit Procedures.

- a. Determine that the issuer meets stated requirements covered in section 6-5, paragraph B above.
- b. Test whether the issuer has in place and follows an established policy that prohibits discrimination in housing and lending as communicated in chapters 2 and 3 of the MBS Guide, as well as section 1-10 of this guide.
- c. Recompute the issuer's required fidelity bond and mortgage servicing errors and omissions coverage policy at the end of the fiscal year in accordance with *chapters 2 and 6 of the MBS Guide.* Verify that: (1) Ginnie Mae is named as the loss payee, (2) the required levels of insurance were maintained throughout the year, with testing of the adequacy of insurance at least *once per quarter* and, (3) verify that the fidelity bond and errors and omissions policies are written by an

insurance carrier *who maintains an A.M. Best rating of B+ or better in the Best Insurance Reports and* is specifically licensed or authorized by law to transact business within the state or territory where the named insured has its corporate headquarters. Lloyd's of London, although not rated, is an accepted insurer.

An issuer's minimum insurance coverage must comply with the following, based on the issuer's total servicing portfolio irrespective of ownership:

- (1) For issuers with a total mortgage-servicing portfolio of \$100 million or less: \$300,000.
- (2) For issuers with a total mortgage-servicing portfolio of more than \$100 million and up to \$500 million: \$300,000, plus 0.15 percent of the amount of total servicing in excess of \$100 million.
- (3) For issuers with a total mortgage-servicing portfolio of more than \$500 million and up to \$1 billion: \$900,000, plus 0.125 percent of the amount of total servicing in excess of \$500 million.
- (4) For issuers with a total mortgage-servicing portfolio of more than \$1 billion: \$1,525,000, plus 0.1 percent of total servicing in excess of \$1 billion.

The maximum mortgage servicing errors and omission insurance coverage requirement is \$20 million. The maximum fidelity bond coverage is not limited.

The required reporting format for the "Presentation of Insurance Requirement" is provided in attachment D of this chapter.

- d. Determine whether the issuer is an affiliate (parent, subsidiary, or related party) of any other Ginnie Mae issuer(s). All affiliated Ginnie Mae issuers should be identified in the auditor's verification of insurance. If an affiliate(s) is covered by the same insurance policy, then the servicing of each issuer must be added together to calculate the combined total servicing portfolio. The amount of this combined servicing portfolio should be used to determine the minimum required insurance coverage.
- e. Compare the issuer's adjusted net worth (net worth reported in the audited financial statements as adjusted for any unacceptable Ginnie Mae assets) to the minimum required net worth as discussed in section 6-5, paragraph G.2, of this chapter.

C. Review of Custodial Documents.

1. **Compliance Requirements.** Documents relating to the pooled mortgages are required to be held on Ginnie Mae's behalf for the life of the pool by a custodial institution. It is the issuer's responsibility to arrange for such an institution to hold the documents. The custodial relationship must be evidenced by the execution of a "Master Custodial Agreement" with the custodian certifying on the reverse side of the Schedule of Pooled Mortgages that it has examined and has in its possession all required documents.

A custodial institution is permitted to function as a custodian to more than one issuer. An issuer may use more than one custodian. Pools issued on or after February 1, 1979, must have a single custodian, unless Ginnie Mae has given written permission for more than one custodian.

A custodial institution must meet the eligibility requirements as specified in *chapter 13 of the Ginnie Mae MBS Guide. The eligibility requirements for custodians are also depicted in chapter 2 of the Document Custody Manual, hereinafter referred to as Document Custody Manual MBS Guide, appendix V-1.*

If an (i) onsite review of the document custodian was performed within one of the previous two fiscal years, (ii) the issuer's securities balance outstanding amounts to less than \$50 million, and (iii) the document custodian has not received any pools within the past fiscal year, Ginnie Mae will permit an off-site review of the document custodian. The auditor must follow the procedures in section 6-5, paragraph C.2, below. All document custodians with Ginnie Mae portfolios must have an on-site review at least once every three years.

2. **Suggested Audit Procedures.**

- a. Determine whether an issuer uses more than one custodial institution. If more than one custodian is used, at least one custodial institution must be reviewed each year, and all custodial institutions must be reviewed within a three-year cycle. Determine that the custodial institution meets the following eligibility requirements:

- (1) Is a federally regulated financial institution in good standing with its primary regulator and not in receivership, conservatorship, liquidation, or any other management oversight by its primary regulator, unless operating under an approved management plan. If *the document custodian is a Government Sponsored Enterprise (GSE)-approved document custodian, it must be in good standing*

with the GSE(s). The auditor shall determine whether the issuer has ever been the subject of any adverse action by a GSE.

- (2) If recognized by Ginnie Mae before September 1, 2004, maintains a secure, one and one-half hour fire-resistant storage facility standard with adequate access controls *Document custodians recognized by Ginnie Mae after August 31, 2004, are required to maintain a secure, two hour fire resistant storage facility standard with adequate access controls.*
- (3) Uses knowledgeable employees in its custodial function to handle mortgage documents and perform custodial functions.
- (4) Maintains for review annual financial statements audited by an auditor for itself or its parent.
- (5) Maintains the minimum insurance requirements of its primary regulator and maintains coverage to indemnify against losses involving Ginnie Mae pools and loan documents custody.
- (6) Maintains updated written procedures within its operation, in addition to the Document Custodian Manual.
- (7) Satisfies eligibility requirements and other requirements as directed by Ginnie Mae.
- (8) *A custodian that maintains issuer records on its own behalf, its parent or affiliated entity (self-custodian) must be part of a trust department that is physically separate from the service area and operations of the issuer.* The self-custodian must also have obtained prior approval to exercise fiduciary powers from its primary regulator. Such fiduciary powers must include ordinary trust services such as personal trust services, personal representative services (executor), guardianship, custodian services, and/or investment advisory services offered to the public and not be limited to maintaining custody of valuable documents for Ginnie Mae issuers. The trust service function must be subject to periodic review or inspection by its primary regulator.
- (9) *If a non self-custodian does not* meet all of the requirements in paragraph C.2.a.(8) above, or if the custodial documents are not held in the trust department, the custodian must provide evidence that there is a vertical independence between the issuer and the custodial/warehouse institution.

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- (10) *Maintains a written disaster recovery plan that covers restoration of the facilities, physical recovery of the files, and backup and recovery of information from electronic tracking systems.
 - (11) Tests whether the document custodian has in place a quality control plan for document review standards.*
- b. Verify that the custodial institution maintains or performs the following inventory accounting requirements:
- (1) Maintains an issuer master file, which contains the issuer custodial register, any blanket legal opinions, a copy of the issuer's corporate resolution for a name change, and any other applicable issuer-level documents.
 - (2) Maintains an issuer custodial register, which includes a list of pools currently in custody (must provide pool identification numbers), the actual and/or due dates for final certification and recertification, and a count of the total number of pools in custody.
 - (3) Maintains a pool master file for each pool in custody, which contains a copy of the master custodial agreement, schedule of pooled mortgages, form HUD 11711B (Certification and Agreement), form HUD 11711A (Release of Security Interest) if applicable, original blanket interim assignment(s) (a copy of which is included in each individual loan file to which the blanket interim assignment applies), copies of opinion(s) from qualified outside legal counsel (originals maintained in the issuer master file), original pool-level waiver letters from Ginnie Mae, and all forms HUD 11708 (Request for Release of Documents) for liquidated release codes.
 - (4) Has performed an annual physical inventory of all pools held for the issuer, which will include, at a minimum, a reconciliation of the pool numbers on the issuer custodial register to a current issuer-provided pool listing and verification that the pool numbers on the issuer custodial register agree with the pool master files in custody.
 - (5) Maintains a nonliquidation release inventory/file of all forms HUD 11708 submitted on or after July 1, 1992, on the basis of the nonliquidation release code 6. If a file is maintained, copies of the forms HUD 11708 must be kept in chronological order by
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document release date. If an inventory is maintained, it must contain the pool number, FHA/U.S. Department of Veterans Affairs (VA)/U.S. Department of Agriculture *Rural Development (RD)*/Office of Public and Indian Housing (PIH) case number or loan number, and the document release date.

If any documents have been released for more than* 90 days (non-liquidation reason code 6)*, the custodian is required to notify the issuer of the overdue documents every 90 days. *If the document is outstanding after 180 days, Ginnie Mae must be notified*. The notification must be in writing and documented in the inventory or file.

- c. If more than one custodial institution is used, identify which pools are at which custodial institution to select a sample of pooled mortgages for that institution. If the issuer uses only one custodial institution, obtain a list of the pools. Select a representative sample of Ginnie Mae pools for review. For pools selected, determine whether the pools include

(1) An executed original form HUD 11711B (Certification) signed by an officer of the issuer covering the mortgages that are being reviewed and that were closed after March 31, 1979, stating that

(a) *Release(s) of security interest (form HUD 11711A) delivered by the issuer to the custodian comprise(s) all evidence of any security agreements affecting any and all mortgages in this pool. Upon the delivery of securities, only Ginnie Mae will have any ownership interest in and to the pooled mortgages, or

(b) Other than the unrecorded assignment to Ginnie Mae, there are and will be no security agreements affecting any mortgages in this pool.

(2) If noted on the form HUD 11711B that a form HUD 11711A is required, an original form HUD 11711A (Release of Security Interest) executed by any and all secured institution(s), relating to any or all mortgages included in the mortgage pool that are being reviewed and that were closed after March 31, 1979. The form should state:

“The lending (or other financing) institution named below agrees to relinquish any and all right, title, or interest it may have in mortgages to be placed in this Ginnie Mae mortgage-backed*”

securities pool or loan package no later than the date and time of delivery of the securities by Ginnie Mae or its agent.”

- d. Obtain a copy of the original schedule of pooled mortgages (form HUD 11706)¹ from the document custodian for each of the pools selected. The purpose of the schedule of pooled mortgages is to provide a means to identify and control mortgages placed in the pool, which secures the obligations issued. Accordingly, select a sample of pooled mortgages from the schedule of pooled mortgages.
- e. *Procedures for the custodian document review are contained in paragraph 13-4 and appendix V1 of Ginnie Mae’s MBS Guide. For sampled mortgages, review the custodial files for the following documents and compare the information shown on these documents to the information on the schedule of pooled mortgages. Reconcile and report on any differences.*
- (1) The original note or other evidence of indebtedness endorsed in blank and without recourse.
 - (2) For multifamily and manufactured housing pools only, an assignment to Ginnie Mae of the mortgage or other security instrument in recordable form but not recorded.* The assignments to Ginnie Mae can be in blanket form. The blanket assignments must apply to mortgages in the same pool and same recording jurisdiction. If the pool was issued after March 31, 1979, and if the mortgage was originated by a mortgagee other than the issuer, there also must be a recorded assignment, if state law requires recordation to make the assignment valid against all lien holders from the originating mortgagee to any intervening interest holder and from such holder to any further holders of mortgage ownership. An assignment to the issuer must immediately precede the unrecorded assignment to Ginnie Mae. These interim assignments must be either originals or certified copies of the originals and, if required by state law to assure validity, be either recorded or certified by the issuer to have been transmitted for recordation.
- f. Within 12 months of the issuance of the securities,* transfer of issuer, and/or change of custodial responsibility, the files at the custodian must

¹ For programs other than the Single Family Mortgage-Backed Securities Program, the form number, before January 1, 1996, was

- Project loans: form HUD 11721.
- Manufactured home loans: form HUD 11725.

contain the following documents. *Report any missing documentation as a finding.*

- (1) Original evidence of guaranty for PIH loans or evidence of the custodian's verification of insurance or guaranty for the FHA, VA, and RD loans if the loans were originated before January 1, 2003, or

If the loan is a VA vendee loan or contract, there will be a portfolio loan statement of settlement form from VA, rather than a loan guarantee certificate (LGC).

- (2) Original recorded mortgages (or other security instruments) signed by the mortgagor securing repayment of the indebtedness. (Note: Compare the mortgagor's name as it appears on the schedule of pooled mortgages with that which appears on the recorded mortgage to assure identity). Copies of the recorded mortgage are acceptable if the copies clearly show the document recording information.
- (3) Evidence that a mortgage title insurance policy has been obtained or other evidence of title acceptability to FHA, VA, RD, or PIH (not required in cases involving the conveyance of HUD secretary-owned property, if an exception has been authorized by Ginnie Mae, or on VA vendee loans or contracts). Copies of mortgagee title insurance policies are acceptable.
- (4) A complete chain of original recorded interim assignments. These are not required if the mortgage is retained by the original lender. Copies of the recorded interim assignments are acceptable if the copies clearly show the document recording information.
- (5) Verification that the custodian has completed the final certification on the back of the schedule of pooled mortgages.

Within 12 months of a transfer of issuer responsibility the following documents must be in the custodial file and the custodian is required to have completed recertification of the appropriate pools:

- (6) An updated endorsement on the promissory notes.
- (7) A recorded assignment of the mortgage to the issuer.
- (8) All documents required in paragraphs C.2.d and C.2.e above.

Within 12 months of a transfer of custodial responsibility, all documents required in C.2.d and C.2.e above must be in the custodial file. The custodian is required to have a completed recertification of the appropriate pools within 12 months. Report any pool(s) for which the final certification or recertification is past due and has not been completed.

If an issuer has entered into a representations and warranties (R&W) agreement with Ginnie Mae, the documents referenced above that must be in the custodian file are subject to chapter 13 and appendix V-1 of the Ginnie Mae MBS Guide 5500.3, REV-1.

- g. Determine that documents and/or loan files released from custodial files are evidenced by a request for release of documents (form HUD 11708). For the sampled mortgages,
- (1) Determine whether the custodian is in possession of a form HUD 11708 for documents and/or files removed from the custodian's care.
 - (2) Prepare a list of missing documents and/or loan files not supported by a form HUD 11708. This listing should be reviewed with the custodian and also with the issuer. Any items not reconciled should be reported as a finding.
- h. Select paid-in-full and/or foreclosed mortgages listed on form HUD 11708 on a test basis. Verify that these mortgage documents are no longer with the custodian. The custodian should note this removal on its inventory control record (the schedule of pooled mortgages).

Any discrepancies should be noted on an exceptions listing, noting the pool number, the mortgagor, and the defect, and reported as a finding. This listing should be reviewed with the custodian, and errors should be corrected by the custodian. The custodian should furnish this listing to the appropriate issuers, and the auditor should then review with the issuer the reasons for any missing or deficient documents.

Missing documents for mortgages that are still current by the issuer's records could be an indication that the issuer has received mortgage payoffs and not passed through payments to securities holders.

- i. In lieu of an on-site audit of the document custodian, follow the following procedures, provided the conditions set forth in section C.1 above have been met.
 - (1) Confirm that the document custodian meets all eligibility requirements as stated in section 6-5, paragraph C.2.a., above. A written certification from the document custodian that it meets all eligibility requirements is acceptable.
 - (2) Confirm that the document custodian maintains or performs the required inventory accounting required in section 6-5, paragraph C.2.b., above. A certification from the document custodian that it (i) maintains the issuer master file for the issuer, (ii) maintains a pool master file for each pool in custody for the issuer, (iii) has performed and provided the date of the annual physical inventory for all pools held for the issuer, (iv) maintains a nonliquidation release inventory/file for all forms HUD 11708 submitted on or after July 1, 1992, on the basis of the nonliquidation reason code, and (v) obtains from the document custodian a copy or list of any documents that have been released for more than 180 days and have not been returned to the document custodian. Item (v) above should be reviewed with the issuer, and any items not reconciled should be reported as a finding.
 - (3) Select a representative sample of Ginnie Mae pools for review and request verification from the document custodian of the following;
 - (a) Using the issuer's trial balance, certify that the loans on the trial balance agree with the loans in custody.
 - (b) Verify that all pools are properly certified and report any pool past due for certification in accordance with section 6-5, paragraph C.2.f., above.

D. Issuer's Administration of Pooled Mortgage.

1. **Compliance Requirement.** Administration of the pool of mortgages and of payments to securities holders is the responsibility of the issuer. Servicing of pooled mortgages must be carried out in accordance with generally accepted practices in the mortgage lending industry. Contractual requirements with respect to pool administration are contained in the guaranty agreement executed by the issuer and Ginnie Mae for each pool. The servicing system must be capable of producing, at any time for any mortgage, an accounting which identifies the Ginnie Mae pool number for each listed mortgage and for each

monthly due date, the amount of each collection, disbursement, advance, or adjustment. It should also indicate the latest outstanding balances of principal, deposits, advances, and unapplied payments. In no instance may the issuer or subservicer remove a loan from a pool, reduce a loan balance, or remove funds from any pool custodial account without prior written approval by Ginnie Mae.

The issuer may incur losses for pooled loans that are not fully insured, such as coinsured multifamily loans, manufactured housing loans, and VA guaranteed loans. For each of these loan types, should a foreclosure take place, the issuer may not be fully reimbursed through the claims process. Any shortfall in collections must be paid to the securities holder out of the issuer's own funds. These shortfalls have been particularly large in the VA program. Special attention should be given to issuers with a concentration of VA loans in declining market areas.

In the VA program, should a default occur, VA will determine the cost effectiveness of bidding at the foreclosure sale. VA will not bid if it believes its losses will exceed the guarantee amount. Consequently, this "no bid" scenario may be costly to the issuer, as it must pay off the security holder for the outstanding mortgage balance.

2. Suggested Audit Procedures.

- a. Test whether the issuer meets Ginnie Mae's requirement for separate custodial bank accounts for principal and interest collections (non-interest-bearing) and tax and insurance escrow funds (option of interest bearing) applicable to pooled mortgages with the principal and interest accounts held in institutions meeting Ginnie Mae's rating requirements (All Participants Memorandum, dated July 10, 1990). Test the custodial account titles for compliance with requirements established by Ginnie Mae letter agreements, forms HUD-11709 and 11720. If a principal and interest disbursement clearing account is used, verify that it is only used for payments to Ginnie Mae securities holders. (Note: These accounts may contain funds for more than one pool, provided that the issuer maintains separate accounting records for each pool).
- b. Review monthly collections of mortgage principal and interest, as well as collections of claims on defaulted and liquidated mortgages, to determine that funds have been deposited into the appropriate custodial account(s) on a daily basis.
- c. Test whether the issuer is making proper payments of interest, principal, and unscheduled principal to certificated securities holders so that those payments are received no later than the 15th of the month. Test whether

partial prepayments, prepayments in full, assignments, and foreclosures are passed through to the securities holders in the regular monthly payment following the month of receipt. Test that all such recoveries are recorded on mortgage-backed securities report controls, the pool collateral is removed from the custodian's possession, and the transaction is supported by documentation.

- d. Test whether disbursements from principal and interest custodial bank accounts are authorized pursuant to the guaranty agreement.
- e. Review a representative sample of payments to securities holders to determine that such payments were made to those shown in the securities holders register for the pools being tested.
- f. Compare mortgages listed in the issuer's liquidation schedule (form HUD-11710E) to those identified on form HUD-11708 held by the custodian as having been withdrawn from the pool to ensure proper pass-through of proceeds to securities holders.
- g. Test whether the issuer is using its own resources to
 - (1) Make advances to the pool accounts to cover shortfalls in collections from mortgagors. (Note: Limited exceptions to this requirement are included in the Ginnie Mae handbooks.) Special attention should be given to the issuer's calculation and use of excess funds, particularly for internal reserve pools.
 - (2) Cover principal amounts not recovered in claim settlements or which are due in connection with defective loans. (Issuers are required to "buy out" uninsured or otherwise defective loans from the pools in accordance with instruction communicated in the *MBS Guide*, using the issuer's own funds. *Such buyouts may only occur once the issuer has received prior approval by Ginnie Mae).*
- h. Obtain an understanding of the issuer's controls to project the need for and availability of funds. These controls should allow the issuer to make required advances to securities holders, as required under section 4.02 of the guaranty agreement.
- i. Test whether the issuer incurred losses for pooled loans not fully insured, such as coinsured multifamily loans, manufactured housing loans, and VA guaranteed loans. Determine that the issuer has disclosed a contingent liability in its financial statements.

-
- j. Test that the issuer has a system to follow up on and obtain the required documents to enable the custodian to make its final certification in a timely manner. Ginnie Mae must receive the final certification, covering documents listed on the reverse side of the schedule of pooled mortgages, within the timeframes identified in the *MBS Guide.*
 - k. If the issuer has acquired pools from another issuer or if the issuer has transferred pools from one document custodian to another, test whether these pools have received new final certifications (recertification) within the timeframes outlined in the Ginnie Mae handbooks.
 - l. Test whether the issuer has established a complete securities holders' register in accordance with Ginnie Mae instructions and has updated the register before paying holders each month. The register should include a record of all certificate transfers for the life of the pool.
 - m. Test whether the issuer is servicing delinquent mortgages and managing foreclosures and assignments in accordance with the applicable requirements of VA, FHA, RD, PIH, and the Ginnie Mae Guide.
 - n. Test whether undelivered payments are deposited into the principal and interest custodial account and that checks which remain outstanding in excess of six months of the payment date are made payable to Ginnie Mae and sent to the pool processing agent pending a claim from the security owner. Undelivered payments should not be used as excess funds or used by the issuer to fund pool shortfalls.
 - o. Test whether any transfer of the P&I or T&I custodial accounts, change of document custodian, change of mortgage servicer, or transfer of issuer responsibility were accomplished after written approval from Ginnie Mae was obtained

E. Review of Monthly Accounting Reports and Quarterly Submissions.

- 1. **Compliance Requirement.** Ginnie Mae issuers of mortgage-backed securities are required to submit the following reports periodically throughout the year:
 - a. Forms: HUD-11710A, HUD-11710D, and HUD 11710E.
Issuers reporting: all Ginnie Mae issuers of record.
Frequency of reporting: monthly.
Deadline for submission: *on or before the 10th calendar day of the month following the month covered in the report.*

- b.** Trial balance *(loan level)* information.
Issuers reporting: all Ginnie Mae issuers of record.
Frequency of reporting: *monthly.*
Deadline for submission: *on or before the 15th calendar day of month.*
- c.** Mortgage Bankers Quarterly Financial Reporting, Form HUD-11750.
Issuers reporting: mortgage bankers not federally regulated.
Frequency of reporting: quarterly.
Deadline for submission: *30 days after end of calendar quarters and 60 days after end of calendar year.*
- d.** *Monthly reports must be submitted to Ginnie Mae on each pool.* Such reports must be provided on form HUD-11710A (Issuer's Monthly Accounting Report), form HUD-11710E (Liquidation Schedule), and form HUD-11710D (Issuer's Monthly Summary Report). Issuers with more than 100 pools (including Ginnie Mae I pools and Ginnie Mae II pools and loan packages) are required to report in electronic form using the procedures and format specified in the *MBS Guide.*

Additional or alternative reports are required in connection with pools other than those for single-family level payment loans, as explained in the chapters and appendixes for the other programs.

The reports, along with supporting documents, must be sent to Ginnie Mae with sufficient lead time and via a method that ensures delivery no later than the 10th calendar day of each month. Instructions for the preparation and submission of the forms or *compact disc* are found in *appendix VI of the MBS Guide*.

- e.** *Monthly reports must be submitted to Ginnie Mae on all of the loans in their portfolio. All issuers must report loan level detail every month. The loan level data should report trial balance information for all nonliquidated loans as part of the cutoff date for the month.
- f.** Quarterly reports on their financial condition must be submitted to Ginnie Mae by issuers that are not federally regulated. Reports must be submitted electronically, using form HUD 11750, Mortgage Bankers' Financial Reporting Form. Issuers may access this shared form at www.mbfrf.org. Federally regulated financial institutions (banks, savings and loans, and credit unions) are not required to submit this report. *

2. Suggested Audit Procedures.

- a. Obtain an understanding of the issuer's procedures for collecting and entering all data relating to mortgage collections and securities payments on form HUD-11710A. Test whether entries are made in accordance with instructions in the Ginnie Mae *MBS Guide*.
- b. Select a sample of form HUD-11710As and trace delinquency information to the issuer's internal mortgage servicing delinquency reports.
- c. Compare the securities balance reported on the form HUD-11710A to the remaining pool balance (RPB) reported to Ginnie Mae or its agent in accordance with Ginnie Mae MBS requirements.
- d. Test whether a liquidation schedule (form HUD-11710E) is submitted to Ginnie Mae for each loan removed from the pool. Also test that the unpaid loan balances passed through to securities holders and reported in the liquidation schedule agree with the issuer's records.
- e. Compare the amount of checks sent to securities holders for the month to the amount reported to Ginnie Mae.
- f. Compare the custodial account balances reported on forms HUD-11710A and 11710D to the actual balances (after reconciliation) of the disbursement clearing and custodial bank accounts as shown by the bank statements.
- g. On pools selected for review, reconcile the total unpaid principal balance of the pooled mortgages to the unpaid principal balance of the securities, as follows:
 - (1) Pool principal balance (section 1, line D, form HUD-11710A).
 - (2) (Plus) prepaid principal (section 1, line F).
 - (3) (Minus) delinquent principal (section 1, line G).
 - (4) (Minus) concurrent date (CD) pools only: scheduled principal (section 1-A, block C).

- (5) (Plus) CD pools only: last liquidation principal installment (principal portion of last installment reported on Liquidation Schedule, form HUD-11710E).
- (6) (Minus) CD pools only: additional principal adjustment or fixed installment control (FIC) change for graduated payment mortgage pools (section 2, block D, other).
- (7) (Equals) security principal balance (section 3, line D).

Differences may arise in the reconciliation between the pooled loan balance and the outstanding securities balance due to additional principal payments or rounding. Such differences should not exceed \$1 for each loan in the pool up to a maximum of \$50 per pool. Any greater difference must be funded to the pool in the current report. At least once a year, adjustments to the securities holder payments must be made in section 2, block D, of form HUD-11710A to fully correct for any difference. Reconcile and report on any difference.

- h.** For pools randomly selected for review, test the expected P&I custodial account balances at cutoff. This test (outlined below) identifies a minimum dollar amount expected in the P&I account for any particular pool as of a given cutoff date. This test verifies the accuracy of the P&I balance reported in section 5, block B2, of the form HUD-11710A report. The test formula will only yield accurate results when the mortgage and securities balances reconcile in step 7 above.

The test assumes that all collections are paid out by the pass-through of funds to securities holders or taken as issuer servicing fees. The test formula is different between internal reserve (IR) and CD pools but in either case indicates the amount of P&I funds which should be held in the account at the cutoff date, which include

- (1) (IR only) plus payment to securities holders, to be distributed on the 15th of the following month (form HUD-11710A, section 2, item G).
- (2) (IR and CD) plus servicing fee, if taken after the cutoff date. If the issuer withdraws its servicing fee before the cutoff, this entry will be zero (section 1, item H).

-
- (3) (IR and CD) plus prepaid P&I, funds which have been collected but are not required to be distributed to holders at the next payment date (section 1, item F, Total).
 - (4) (IR and CD) minus prepaid servicing fee, as calculated based on prepaid interest amounts (section 1, item F, Interest). Servicing fees collected on prepaid interest are already included in item (2) above.
 - (5) (IR and CD) minus delinquent P&I, funds not yet collected but which have already been distributed to holders through calculation of scheduled payment (section 1, item G, Total).
 - (6) (IR and CD) plus delinquent servicing fee as calculated based on total delinquent interest (section 1, item G, Interest). Servicing fees are not distributed to holders, so this amount is not a shortage in the account.
 - (7) (CD only) plus additional principal payments. These are funds collected but not due holders until the 15th of the following month (section 1, line B-2).
 - (8) (CD only) plus additional principal adjustment, the issuer-funded adjustment that has been deposited to the custodial account but is not distributed until the following month (section 1, line C, Pool Interest).
 - (9) (CD only) plus liquidation principal. Similarly, funds collected but not due to be distributed until the following month (section 1, item C).
 - (10) (CD only) plus fixed installment on liquidations because it is necessary to amortize a liquidating loan through one payment beyond the month during which payoff or foreclosure funds are received on CD pools. This “extra” month payment, normally not due until the following month, is included in the scheduled P&I amount.
 - (11) (CD only) minus servicing fee from liquidations, as calculated on the interest portion of the last payment installment (based on last interest installment on the form HUD-11710E).
-

This calculated expected P&I balance should agree with the reported P&I balance (form HUD-11710A, section 5B2). Differences should be reconciled and exceptions reported.

- i. Obtain an understanding of the issuer's procedures and test whether the issuer meets the delivery requirement by the 10th calendar day of each month.
- j. Test that loan level information is being reported monthly to Ginnie Mae.
- k. For all issuers that are not federally regulated financial institutions, test that quarterly financial information (HUD-11750) is being submitted *electronically through the Mortgage Bankers' Financial Reporting Form (MBFRF) Web-based system.*

F. Securities Marketing and Trading Practices.

1. **Compliance Requirement.** Ginnie Mae has established securities marketing and trading requirements, which are intended to ensure that issuers fulfill their securities marketing and trade activities in a manner consistent with prudent business practices and their own and others' financial capacity. There are three components to these requirements: (a) a suitability rule, (b) prudent business practice rules, and (c) minimum forward delivery contract requirements related to so-called mark-to-market deposit requirements. There are also record-keeping and reporting requirements. All approved issuers must implement these procedures, whether or not securities and/or commitments are outstanding. The applicable requirements are found in the *MBS Guide.*

2. **Suggested Audit Procedures.**

- a. Obtain an understanding of the written procedures established by the issuer to determine the financial integrity of dealers, brokers, and investors, including an explanation of standards for and steps taken in determining the financial capacity of dealers, brokers, or investors to complete transactions.
- b. Test whether the issuer is following established procedures to determine the financial capacity of dealers, brokers, and investors to complete a transaction and to determine the business reputation of the dealers, brokers, and investors.

-
- c. Obtain copies of the resolution executed by the issuer's board of directors designating key persons responsible for overall supervision of issuer activities relating to the marketing and trading of securities.
 - d. Obtain an understanding of the procedures established by the issuer to maintain a record of all commitments entered into to deliver or acquire securities.
 - e. Test whether the issuer's records of such commitments include the following:
 - (1) Date of the transaction (trade date).
 - (2) Type of securities.
 - (3) Nature of the transaction: purchase, sale, optional or mandatory delivery, repurchase, or other credit arrangement.
 - (4) Settlement date.
 - (5) Dollar amount of securities.
 - (6) Interest rate on the securities.
 - (7) "Price" of the securities.
 - (8) Name of the firm and individual with whom the transaction was executed.
 - (9) Current market price (value) of the contract.
 - f. For "regulated transactions" (see note 1 at step h), test whether the issuer's records include the following:
 - (1) A copy of the delayed delivery contract required by the Ginnie Mae Handbook.
 - (2) The name of the financial institution with which collateral is, or will be, deposited.
 - (3) Records of mark-to-market computations, including market value, amounts of deposits by issuer and by counterparty, and the type of collateral deposited.
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- (4) If the collateral used is a letter of credit, a copy of the letter of credit.
- g. Review the issuer's statement showing the computation of the issuer's "net position" and compare information to the issuer's accounting records. Prove the mathematical accuracy of the net position. The statement should identify amounts of loans and securities closed and held for sale, plus those expected to be acquired, less commitments the issuer has available for disposing of loans and securities. It also should include any positions involving repurchase, reverse-repurchase, or other credit transactions.
- h. Determine the potential impact on an issuer's net worth of any identified forward or future commitment contract entered into by the issuer to purchase or sell securities. If there are material potential effects on the issuer's net worth, determine whether they are disclosed in the appropriate footnotes to the financial statements.

Note 1: "Regulated transaction" means the purchase or sale of securities by an issuer pursuant to a delayed delivery contract, except that the term does not include

- (1) A sale of securities when (1) the issuer holds a valid, outstanding commitment to guaranty mortgage-backed securities (which is not applied in connection with another transaction) issued by Ginnie Mae in an amount at least equal to the face amount of the securities sold and (2) the settlement date under the contract is no later than the last day of the calendar month in which the 150th day after the contract's trade date falls.
- (2) A sale of securities guaranteed by Ginnie Mae and based on construction loans (construction loan securities) or project loans (project loan securities).
- (3) A sale or purchase of securities pursuant to a contract which does not obligate the issuer to actually sell/purchase securities; that is, a standby commitment on which the issuer has the option to perform.
- (4) A purchase (or sale) of mortgage participation certificates directly from (or to) the Federal Home Loan Mortgage Corporation.

G. Adjusted Net Worth.

1. **Computation.** A “presentation of adjusted net worth calculation” is required for all issuers, even if there were no securities or commitments outstanding at fiscal year end. The required format for the “presentation of adjusted net worth calculation” is provided in attachments B and C of this chapter.

Unacceptable assets are defined in attachment A of this chapter and should be itemized by asset classification. Do not aggregate the unacceptable assets into one line entitled “Unacceptable Assets.” In certain circumstances, and at its sole discretion, Ginnie Mae may accept a corporate guaranty as consideration for reclassifying certain assets that are treated as unacceptable under the HUD Consolidated Audit Guide (e.g., for purposes of computing adjusted net worth, Ginnie may elect to accept a corporate guaranty as consideration for accepting pledged assets).

If evidence exists indicating the existence of related party receivables, which have not been deducted by the auditor, Ginnie Mae will deduct the amount from the issuer’s adjusted net worth.

An issuer’s adjusted net worth will be calculated by subtracting the total amount of unacceptable assets from the net worth as stated on the auditor’s audited balance sheet. Excess (deficit) net worth is computed as the difference between adjusted net worth and required net worth.

Failure of the issuer to respond satisfactorily and in a timely manner to requests made by Ginnie Mae or its agent for additional information could result in disallowance of questionable assets and suspension or termination of issuer status.

When the Ginnie Mae issuer is a subsidiary, the adjusted net worth computation must focus exclusively on the assets and liabilities of the Ginnie Mae issuer.

2. **Required Net Worth.** Required net worth will be calculated as of the end of the issuer’s fiscal year as follows:
 - a. For issuers approved to securitize mortgage-backed securities pools backed by single-family level payment, graduated payment, growing equity, or adjustable rate mortgages, the net worth is *\$1,000,000* base net worth plus 1 percent of the amount of securities outstanding in excess of \$5 million but less than \$20 million plus 0.2 percent of any additional

securities, commitment authority, and total pools funded² in excess of \$20 million.

- b. For issuers approved to securitize mortgage-backed securities pools backed by manufactured home loans, the net worth is *\$1,000,000* base net worth plus 0.2 percent of any additional securities, commitment authority, and total pools funded in excess of \$35 million.
- c. For issuers approved to securitize mortgage-backed securities pools backed by multifamily construction or permanent loans, the net worth is \$500,000 base net worth plus 0.2 percent of any additional securities, commitment authority, total pools funded, and dollar amount of unexpended construction loan draws³ in excess of \$35 million.
- d. *For issuers approved to securitize mortgage-backed securities pools backed by home equity conversion mortgages, the net worth is \$1,000,000 base net worth plus 1 percent of the amount of securities outstanding in excess of \$5 million but less than \$20 million plus 0.2 percent of any additional securities, commitment authority, and total pools funded in excess of \$20 million.
- e. Issuers of Single Family MBS and HMBS approved before October 1, 2008 will have until October 1, 2010 to meet the \$1,000,000 net worth requirement. Issuers approved before October 1, 2008 must maintain a minimum net worth requirement of \$250,000 for single family MBS and a \$500,000 for HMBS until October 1, 2010, when the \$1,000,000 minimum net worth requirement will take effect.*

6-6 **Audit Finding Reporting.** All material instances of noncompliance with any HUD requirement or regulation, deficiencies in internal control, fraud or illegal acts, or contract violations that were disclosed during the audit process must be reported as findings in the audit report. All nonmaterial instances of noncompliance, deficiencies in internal control, fraud or illegal acts, or contract violations disclosed during the audit process may be reported separately to management. Such reporting must be in writing in a management letter or other type of written auditor communication and must be mentioned in the independent auditor's report, including the date of the management letter or other written communication. Noncompliances, deficiencies, or instances of violations that were corrected during the audit process, after the fiscal year under audit, or disclosed as a part of the audit process before the end of the fiscal year under audit and/or before the issuance of

² Pools that have been logged and are in the review process and the commitment line balance has been reduced.

³ The net amount between construction loan commitment authority reserved and total construction loan draws made.

*the audit report must be included in the report as resolved findings or in a management letter, depending on their materiality.

- A. **Content of Finding.** Findings are to be presented in accordance with the standards and requirements of the “Yellow Book.” A finding should be supported by sufficient, competent, and relevant evidence; be presented in a manner to promote adequate understanding of the matters reported; and provide convincing but fair presentations in proper perspective. Please refer to chapter 2 for the information that is to be included in a finding.
- B. **Corrective Action in Process.** Many times when auditees are presented with draft findings, they will start to take action to correct the deficient condition. When this action is underway and the auditor has completed his/her fieldwork, the auditee can include the action completed and the action remaining to be taken in the auditee’s comments and in the corrective action plan. Regardless of whether the auditee is in the process of correcting the finding, the auditor is to include the finding in the report with all required elements.
- C. **Corrective Action Completed.** Many times when auditees are presented with draft findings, they will start to take action and complete that action, correcting the deficient condition before the completion of the fieldwork. When this occurs, the finding is still to be included in the audit report with all required elements. The action taken/completed should be included in the auditee’s comment section and should be validated by the auditor. The recommendation section should follow the auditee’s comment section, and the auditor should state whether he/she validated the action or not. In addition, the auditor could include any additional recommendations he/she believes necessary based on the validation of that action.

- 6-7 **Technical Assistance Needed.** Ginnie Mae contractors will receive, review, and act on audit reports conducted using this chapter. It is important that the report meet Ginnie Mae’s requirements and expectations. For this reason, questions on audits performed using this chapter should be referred to Ginnie Mae’s Office of Mortgage-Backed Securities at (202) 708-1535.*

Unacceptable Assets for Computation of Adjusted Net Worth

1. Any asset or portion thereof pledged to secure obligations of another entity or any person. Supervised institutions that provide financial services to incorporated communities are sometimes required by state law to pledge their assets for the benefit of the community. These pledged assets are acceptable for supervised institutions only.
2. An asset due from an officer or stockholder of the mortgagee or from a related entity, except for
 - a. A construction loan receivable, secured by a first mortgage, from a related entity.
 - b. A mortgage loan receivable established in the normal course of business in an arm's length transaction and secured by a first mortgage on the related property.
 - c. A receivable from a related party when the affected parties have executed a cross-default agreement⁴ or corporate guarantee agreement⁵ with Ginnie Mae.
3. An investment in a related entity in which any officer or stockholder of the mortgagee has a personal interest⁶ unrelated to that person's position as an officer or stockholder of the mortgagee.
4. That portion of an investment in a joint venture, subsidiary, affiliate, and/or other related entity, which is greater than equity, as adjusted. "Equity as adjusted" means the book value on the books of the related entity reduced by the amount of unacceptable assets carried by the related entity.

⁴ A cross-default agreement is an agreement between related affiliated Ginnie Mae issuers, which provides for the default of all affiliated issuers in the event of a default by any one of them.

⁵ A corporate guarantee agreement is an agreement in which the issuer's parent guarantees the performance of the issuer.

⁶ "Personal interest" as used here indicates a relationship between the mortgagee and a person or entity in which that specified person (e.g., spouse, parent, grandparent, child, brother, sister, aunt, uncle, or in-law) has a financial interest in or is employed in a management position by the mortgagee.

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5. Any intangible asset, such as goodwill, covenants not to compete, franchise fees, organization costs, value placed on insurance renewals, and value placed on property management contract renewals.
 6. The value of any servicing contract not determined in accordance with Statement of Financial Accounting Standards (SFAS) No. 65, "Accounting for Certain Mortgage Banking Activities," and SFAS No. 125, "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities," or subsequent revisions thereto.
 7. Any asset not readily marketable and for which appraised values are very subjective. Examples include but are not limited to antiques, artwork, and gemstones.
 8. That portion of any marketable security (listed or unlisted) in excess of the lower of cost or market, except for shares of Fannie Mae stock required to be held under a servicing agreement, which should be carried at cost.
 9. Any amount in excess of the lower cost or market value of mortgages in foreclosure, construction loans, or property acquired through foreclosure.
 10. Any asset that is principally used⁷ for the personal enjoyment or benefit of an officer, director, or stockholder and not for normal business purposes. This includes automobiles and personal residences.
 11. "Other assets" unless the financial statements are accompanied by a schedule prepared by the auditor or a schedule prepared by the issuer/mortgagee and signed by an officer of the issuer/mortgagee.
 12. That portion of contributed property, not otherwise excluded, in excess of the value as of the date of contribution determined by an independent appraisal.

⁷ "Principally used" means that any other use of the property must be solely incidental.

**Required Format for Presentation of
Adjusted Net Worth
Calculation for Issuer**

A. Adjusted net worth calculation:

Stockholder's equity per statement of financial condition at end of reporting period	\$ _____
Less:	
Itemized unacceptable assets ^{1/}	
1.	\$ _____
2.	\$ _____
3.	\$ _____
Total unacceptable assets	\$ _____
Adjusted net worth	\$ _____

B. Required net worth calculation:

Unpaid principal balance of securities outstanding (Note: number of pools = _____)	\$ _____
Plus:	
Outstanding balance of commitment authority issued and requested	\$ _____
Total outstanding portfolio and authority	\$ _____
Required net worth	\$ _____

C. Excess (deficit) net worth

(Adjusted net worth – required net worth)	\$ _____ ^{2/}
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^{1/} Unacceptable assets are defined in attachment A.

^{2/} In the event that adjusted net worth does not meet the Ginnie Mae requirement, the auditor may include any comments from representatives of the issuer of corrective measures contemplated.

ATTACHMENT C

**Required Format for Presentation of
Adjusted Net Worth
Calculation for Issuer's Parent**

A. Adjusted net worth calculation:

Stockholder's equity per statement
of financial condition at end of
reporting period \$ _____

Less:

Itemized unacceptable assets^{1/}

1. \$ _____

2. \$ _____

3. \$ _____

Total unacceptable assets \$ _____

Adjusted net worth \$ _____

B. Comparison of net worth calculation:

Issuer's required net worth
(taken from issuer's adjusted
net worth calculation) \$ _____

(Multiply issuer's required net
worth by 110% for issuers with
single-family status only, otherwise
multiply by 120%) \$ _____

Parent's required net worth \$ _____

C. Excess (deficit): \$ _____

^{1/} Unacceptable assets are defined in attachment A.

**Required Format
For Presentation of
Insurance Requirement**

A. Identification of affiliated^{1/} Ginnie Mae issuers:

Affiliated Ginnie Mae issuers:
(Issuer name and Ginnie Mae issuer identification number)

Affiliated issuers on same insurance policies:
(Issuer name and Ginnie Mae issuer identification number)

B. Required insurance calculation:

Servicing portfolio:	
Ginnie Mae	\$ _____
Fannie Mae	\$ _____
Freddie Mac	\$ _____
Conventional (other)	\$ _____
Total servicing portfolio	\$ _____
Required fidelity bond coverage	\$ _____
Required mortgage servicing errors and omissions coverage	\$ _____

C. Verification of insurance coverage:

Fidelity bond coverage at end of reporting period	\$ _____
Mortgage servicing errors and omissions coverage at end of reporting period	\$ _____

D. Excess (deficit) insurance coverage:

Fidelity bond coverage	\$ _____
Required mortgage servicing errors and omissions coverage	\$ _____

E. Ginnie Mae loss payable endorsement

Fidelity bond coverage	\$ <u>Yes/No</u>
Mortgage servicing errors and omissions coverage	\$ <u>Yes/No</u>

^{1/} **Definition of an affiliate:** An affiliate is a party that, directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with an issuer.

Attachment E

**Report of Independent Auditors on
Consolidating Balance Sheet and
Statement of Income**

Board of Directors
[ABC Financial Corporation]

We have audited, in accordance with generally accepted auditing standards and government auditing standards, the consolidated financial statements of [ABC Financial Corporation and subsidiaries] as of [insert ending date, for example December 31, 1991] and have issued our unqualified opinion thereon, dated [insert date, for example January 24, 1992] included on page [insert page number] of [identify report]. Our audit was conducted for the purpose of forming an opinion on the consolidated financial statements taken as a whole. The following consolidating balance sheet and statement of income on pages [insert page numbers], respectively, are presented for purposes of additional analysis and are not a required part of the consolidated financial statements of [ABC Financial Corporation and subsidiaries]. Such information has been subjected to the auditing procedures applied in our audit of the consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the consolidated financial statements taken as a whole.

This report is intended for the information of the audit committee, management, and the Government National Mortgage Association (Ginnie Mae). However, this report is a matter of public record, and its distribution is not limited.

[Firm signature]

[Date]

**Required Transmittal/Checklist for
Annual Submission of Financial Documents**

Address to: Ginnie Mae's review agent

To whom it may concern:

The following information is being sent to maintain eligibility in the mortgage-backed securities program. If you have any questions regarding the items being sent, you may contact Mr./Mrs. _____ of the organization or me at telephone number _____. Our facsimile number is _____.

Complete items 1 through 7

1. Issuer name: _____
2. Issuer address: _____
3. Issuer's tax identification no.: _____
4. Ginnie Mae I.S. no.: _____
5. FHA mortgagee no.: _____
6. Auditor's tax identification no.: _____
7. Auditor's contact person _____
and telephone number: _____

Place a checkmark by item(s) submitted

1. ___ Annual audited financial statement for period ended ___/___/___
2. ___ Auditor's report on consolidating balance sheet and statement of income (if appropriate)
3. ___ Auditor's report on internal controls
4. ___ Auditor's report on compliance with specific requirements
5. ___ Auditor's presentation of insurance requirement
6. ___ Auditor's presentation of adjusted net worth for issuer
7. ___ Auditor's presentation of adjusted net worth for parent (if appropriate)
8. ___ Corrective action plan (if appropriate)
9. ___ Schedule of "other assets"
10. ___ Name, address, and Ginnie Mae issuer number (if applicable) of all affiliates. An "affiliate" is defined for these purposes as an organization that is related to the issuer through some type of control or ownership as defined by generally accepted accounting principles (GAAP). Use additional page if necessary:

Signature: _____ Date: _____
Type or print signature name: _____
Title: _____