

REDACTED AUDIT REPORT



Issue Date December 3, 2008

Audit Report Number 2009-DP-0002

TO: Joseph Murin, President, Government National Mortgage Association

[Handwritten signature]

FROM: Hanh Do, Director, Information Systems Audits Division, GAA

SUBJECT: Review of Controls over Securitized Single Family Loans

HIGHLIGHTS

What We Audited and Why

We audited the Government National Mortgage Association (Ginnie Mae) Mortgage-Backed Securities Information System (MBSIS) related to the “match to terminated” process. We conducted the audit because of concerns about potential exposure of the Ginnie Mae Mortgage-Backed Securities programs to fraud and the lack of mortgage insurance on several mortgages that were issued into the Ginnie Mae mortgage-backed securities pools. Our objective was to perform a limited scope review to assess the [REDACTED] and the inadequacies of the documentation [REDACTED]

What We Found

Ginnie Mae developed and implemented a robust [REDACTED] matching process in 2003 that compares issuer-submitted data to the Federal Housing Administration’s (FHA) Single Family Insurance System (SFIS - A43) data. The “match to terminated” process was developed along with the [REDACTED] matching processes and was first run on an [REDACTED] basis in May 2005 to determine whether the Ginnie Mae pools of FHA single-family loans contained any loans with

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terminated mortgage insurance as reported by FHA's SFIS database. [REDACTED]

[REDACTED]. While Ginnie Mae maintains a high [REDACTED] match rate and we acknowledge its continuing efforts to enhance the matching processes, there are some control aspects of the "match to terminated" process that could be improved. [REDACTED]

[REDACTED]

The conditions we identified leave HUD and Ginnie Mae at risk to issuer misrepresentations and uninsured/uninsurable or fraudulently obtained loans.

What We Recommend

We recommend that Ginnie Mae: (1) Ensure that the Ginnie Mae Office of Information Management Division continues to be involved in the management of information system projects for the agency; (2) [REDACTED] and prepare detailed system documentation for the process; (3) Implement specific policies and procedures that define the actions [REDACTED] data errors and when issuers fail to make data corrections in a timely manner; (4) Implement controls that prevent issuer errors/misrepresentations and improve the [REDACTED] process; and (5) Assess the implementation of controls that identify loan characteristics that are indicators of loans obtained/insured using fraudulent methods and that test for [REDACTED]

For each recommendation without a management decision, please respond and provide status reports in accordance with HUD Handbook 2000.06, REV-3. Please furnish us copies of any correspondence or directives issued because of the audit.

Auditee's Response

The complete text of the auditee's response, along with our evaluation of that response, can be found in appendix A of this report.

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BACKGROUND AND OBJECTIVES

Ginnie Mae is a wholly owned corporate entity of the United States within the U.S. Department of Housing and Urban Development (HUD). Ginnie Mae is authorized under Title III of the National Housing Act, as amended (12 U.S.C. (*United States Code*) 1716 et seq.). It guarantees privately issued securities backed by pools of mortgages that are insured or guaranteed by the Federal Housing Administration (FHA), the U.S. Department of Veterans Affairs, the Rural Housing Service of the U.S. Department of Agriculture, or HUD's Native American Program (Office of Public and Indian Housing) through its Mortgage-Backed Securities programs. Ginnie Mae guarantees the registered holder (i.e. investor) the timely payment of scheduled monthly principal and interest payments, loan prepayments, and early recoveries of principal on the underlying mortgages. It uses its Mortgage-Backed Securities programs to provide a structure for channeling funds from the nation's capital markets into the housing market. Each mortgage-backed security enjoys the U.S. government's full faith and credit guaranty backing.

Ginnie Mae established matching criteria to be used to provide an electronic agreement between Ginnie Mae and FHA that the loan is insured and that a claim will be honored on the strength of the electronic match. FHA single family loans represent the largest percentage of loans (approximately 72 percent, 2.7 million) in Ginnie Mae pools. [REDACTED]

Ginnie Mae established an additional match process that matches the active Mortgage-Backed Securities Information System (MBSIS) loan records to the FHA Single Family Insurance System (SFIS) active data file, which contains more than 26 million loan records, with the unpaid balances totaling more than \$335 billion. [REDACTED] to determine whether the Ginnie Mae pools of FHA single-family loans contain any loans with terminated mortgage insurance as reported by FHA's SFIS database. The match is referred to as the [REDACTED]

We initiated this audit based on concerns about the potential exposure of the Ginnie Mae Mortgage-Backed Securities programs to fraud and the lack of mortgage insurance on several mortgages that were issued into the Ginnie Mae mortgage-backed securities pools.

Our objective was to perform a limited scope review to assess the [REDACTED] and the inadequacies of the documentation [REDACTED]

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RESULTS OF AUDIT

Finding 1: Ginnie Mae Did Not Take Sufficient Action to Ensure Data Reliability and Did Not Manage Its “Match to Terminated” Process Effectively

Ginnie Mae did not take sufficient action to ensure data reliability and did not manage its “match to terminated” process effectively. Ginnie Mae relies upon the results of the [REDACTED] match process to identify issuers that [REDACTED] regarding terminated FHA loans. The conditions occurred because Ginnie Mae did not establish specific policies and procedures [REDACTED]

[REDACTED] Therefore, HUD and Ginnie Mae are at risk to issuer misrepresentations and uninsured/uninsurable or fraudulently obtained loans.

Ginnie Mae Did Not Take Sufficient Action to Ensure Data Reliability

Ginnie Mae did not make data integrity a program priority and, therefore, accepted potentially inaccurate data from its issuers. [REDACTED]

Office of Management and Budget (OMB) Circular A-127, part 7, section j, “Internal Controls,” requires that financial management systems include a system of internal controls to ensure that resource use is consistent with laws, regulations, and policies; resources are safeguarded against waste, loss, and misuse; and reliable data are obtained, maintained, and disclosed in reports.

OMB Circular A-127 also requires that appropriate internal controls be applied to all system inputs, processing, and outputs. It requires agencies to analyze how system improvements, new technology supporting financial management systems, and modifications to work processes can together enhance agency operations and improve program and financial management. It further requires that (1) the reassessment of information and processing be an integral part of the determination of system requirements and (2) agencies consider program

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operations, roles and responsibilities, and policies/practices to identify related changes necessary to facilitate financial management systems' operational efficiency and effectiveness.

Ginnie Mae Did Not Take Sufficient Action to Ensure That Data Errors Were Corrected in a Timely Manner

Ginnie Mae did not take sufficient action to ensure that issuers corrected data errors. [REDACTED]

[REDACTED] Ginnie Mae tracked the data reporting errors using reports and through follow-up by both contractor and Ginnie Mae personnel. However, Ginnie Mae did not issue specific policies and procedures defining what actions should be taken or how the errors should be ranked or rated. In addition, Ginnie Mae's policies did not identify specific actions to be taken [REDACTED] exposes HUD and Ginnie Mae to the risk of issuer misrepresentations and uninsured/uninsurable or fraudulently obtained loans.

Ginnie Mae Did Not Perform a Match of the Data [REDACTED]

Ginnie Mae did not perform a match of the data [REDACTED] used in the insurance match. Although not specifically required by the memorandum of understanding between Ginnie Mae and FHA, the inclusion of [REDACTED] should decrease the occurrence of false positives and potential fraud.

[REDACTED] We conducted a match using 2007 MBSIS loan level data provided by Ginnie Mae and the 2007 FHA SFIS data provided by FHA. Our match produced an additional [REDACTED] matches over the terminated match performed by Ginnie Mae [REDACTED]

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[REDACTED]

[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]

[REDACTED]

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Ginnie Mae Did Not Implement Controls to Prevent the Acceptance of [REDACTED]

Ginnie Mae did not implement controls to prevent the acceptance of [REDACTED]

[REDACTED]

Issuers were also advised of other data quality issues. By not implementing controls to prevent inaccurate data submissions, HUD and Ginnie Mae are at risk of issuer misrepresentations and uninsured/uninsurable or fraudulently obtained loans.

[REDACTED]

Ginnie Mae did not implement [REDACTED] Title 24 of the Code of Federal Regulations Subpart A Subsection 320.3 “Eligibility of Issuers” parts d and e require issuers of Ginnie Mae securities to be in compliance with FHA requirements and to conduct business operations in compliance with mortgage banking practices, ethics and standards. In order to ensure issuer compliance with these requirements and eligibility to continue to participate in Ginnie Mae programs, Ginnie Mae needs to implement controls that verify and validate the loans issued into Ginnie Mae securities. Using a data verification and analytical tool, we noted several conditions indicative [REDACTED]

[REDACTED]

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[REDACTED]

[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

[REDACTED]

Ginnie Mae Did Not Manage Its “Match to Terminated” Process Effectively

Ginnie Mae did not effectively manage its “match to terminated” process. It did not adequately document the process, did not ensure that [REDACTED]

[REDACTED] These practices left Ginnie Mae vulnerable to issuers’ [REDACTED] and diminished Ginnie Mae’s ability to identify this problem [REDACTED]

Ginnie Mae did not adequately document the “match to terminated” process. There was limited external documentation describing [REDACTED] procedure. The only documentation of the process available for review was minimal high-level explanations in draft documents. Additionally, the most detailed documentation we were provided was the [REDACTED] which only noted what files were used in the match and which programs were run to perform the match. Detailed documentation [REDACTED]

[REDACTED] The lack of documentation limited Ginnie Mae’s ability to adequately monitor the “match to terminated” process.

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National Institute of Standards and Technology Special Publication (NIST SP) 800-53,¹ appendix E, “Minimum Assurance Requirements,” for moderate systems requires that “The organization ensures that adequate documentation for the information system and its constituent components is available, protected when required, and distributed to authorized personnel. . . . The organization includes documentation describing the functional properties of the security controls employed within the information system with sufficient detail to permit analysis and testing of the controls.”

HUD Handbook 2400.25, REV-1, Information Technology Security Policy, requires that program offices/system owners ensure that “adequate documentation for the information system and its constituent components is available, current, protected when required, and distributed to authorized personnel.” It identifies the following as included in this requirement: “Certification & Accreditation and System Development Life Cycle documentation; vendor-supplied documentation of purchased software and hardware; network diagrams; application documentation for in-house applications; system build and configuration documentation, which includes optimization of system security settings, when applicable; user manuals; and standard operating procedures.”

Ginnie Mae did not ensure that the “match to terminated” process

[REDACTED]

[REDACTED]

[REDACTED]

We also noted a lack of [REDACTED] results. Using MBSIS data and the match codes provided by Ginnie Mae, a number of loans maintained an [REDACTED] over multiple years. [REDACTED]

¹ NIST SP 800-53, “Recommended Security Controls for Federal Information Systems.”

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[REDACTED]

Year	Total number of loans	[REDACTED]	[REDACTED]	[REDACTED]
2008	2,721,479	48,136	N/A	N/A
2007	2,587,222	26,536	16,871	\$ 1,957,335,239.65
2006	2,656,790	27,515	12,226	\$ 1,336,624,008.86
2005	2,943,486	47,822	8,201	\$ 852,595,916.58

The conditions identified occurred because Ginnie Mae did not establish specific policies and procedures to [REDACTED] on the MBSIS data reliability issues identified by the edit controls in place. There were no specific policies and procedures that dictated how the [REDACTED], and, therefore, the [REDACTED] were not effective in all instances. The policies and procedures in effect relied on the [REDACTED] of the material impact to Ginnie Mae.

Finally, Ginnie Mae inaccurately defined the [REDACTED]. Based on this definition, the Finance Division, who has had project management responsibilities for the matching project since its inception in 2003, determined that system documentation was not required to be developed and did not require the contractor to produce documentation even though the creation of system documentation is a requirement within their contract. Since May of 2005, Ginnie Mae has relied upon the results of this process to identify issuers [REDACTED]. The "match to terminated" process has been run on [REDACTED]. Ginnie Mae's use of this process and its results do not support their definition.

Conclusion

Ginnie Mae relies upon the results of the "match to terminated" process to identify issuers that do not submit correct loan data regarding terminated FHA loans. The conditions we identified leave HUD and Ginnie Mae at risk to issuer misrepresentations and uninsured/uninsurable [REDACTED] loans. During our review, we identified [REDACTED]. The remaining principal balance for the 99 loans identified [REDACTED] in 2007 and [REDACTED] as of February 2008, is \$9.9 million. These funds are at potential risk for FHA. The results also indicate that Ginnie Mae made management

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decisions based on possibly unreliable information and as a result, HUD and Ginnie Mae are vulnerable to issuer misrepresentations and uninsured/uninsurable loans. These problems occurred because Ginnie Mae did not establish specific policies and procedures to [REDACTED] data reliability issues identified by the edit controls in place. There were no specific policies and procedures in place that dictate how the errors [REDACTED] effective in all instances. Ginnie Mae improperly classified the [REDACTED] process, instead of a [REDACTED] process as was implemented by Ginnie Mae. Therefore, system documentation was not developed.

Recommendations

We recommend that Ginnie Mae

- 1A. Implement specific policies and procedures that define the actions to be taken [REDACTED] data errors and when issuers fail to make data corrections in a timely manner.
- 1B. [REDACTED]
- 1C. [REDACTED]
- 1D. [REDACTED]
- 1E. Assess the implementation of controls to test for [REDACTED]
- 1F. Assess the implementation of controls that identify loan characteristics that are indicators [REDACTED]
- 1G. Ensure that the Information Management Division for Ginnie Mae continues to be involved in the management of information system projects for the agency.
- 1H. Prepare detailed system documentation for the [REDACTED] process.
- 1I. Implement a procedure to perform the [REDACTED]
- 1J. Review and revise the programming code for the [REDACTED] to ensure that [REDACTED] loan records received are accounted for in the [REDACTED]

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SCOPE AND METHODOLOGY

We performed the audit

- From January through July 2008,
- At HUD headquarters in Washington, DC, and
- In accordance with generally accepted government auditing standards.

We reviewed Ginnie Mae's MBSIS and match process documentation to gain a basic understanding of the system configuration, policies and procedures, and the matching processes. We also interviewed Ginnie Mae management officials and contractors to understand the MBSIS processes, controls, and risks.

We obtained the computer-processed data used by the Ginnie Mae MBSIS contractor to perform the "match to terminated" matching process (2005, 2006, and 2007).

We obtained the computer-processed data sent to Ginnie Mae from FHA's SFIS system for use in the "match to terminated" process. The match compares [REDACTED]

To accomplish our objectives, we reviewed policies and procedures and interviewed staff from Ginnie Mae and its contractors. We interviewed Ginnie Mae management officials and its contractors to follow up on issues and/or observations noted during the course of our review. We interviewed FHA management officials to determine their responsibilities and processes as they related to data provided to Ginnie Mae from FHA's SFIS computer system.

Using ACL, we analyzed the MBSIS "active" loan data to [REDACTED]

[REDACTED] Additionally, we used ACL to compare electronic data on monthly pool and loan level data against the loan level data in FHA's Single Family Data Warehouse to identify anomalies or inconsistencies in the data.

We uploaded the [REDACTED] we identified in the loan level data supplied by Ginnie Mae into a data verification and analytical tool system for analysis. The data verification and analytical tool then returned the data with conditions and/or issues which we highlighted and summarized in the results section of this report. We did not verify nor confirm the results provided by the data verification and analytical tool for the 310 loans; the issues identified are red flags and may indicate problems with the subject loans.

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INTERNAL CONTROLS

Internal control is an integral component of an organization's management that provides reasonable assurance that the following objectives are being achieved:

- Effectiveness and efficiency of operations,
- Reliability of financial reporting, and
- Compliance with applicable laws and regulations.

Internal controls relate to management's plans, methods, and procedures used to meet its mission, goals, and objectives. Internal controls include the processes and procedures for planning, organizing, directing, and controlling program operations. They include the systems for measuring, reporting, and monitoring program performance.

Relevant Internal Controls

We determined the following internal controls were relevant to our audit objectives:

- Access controls,
- Input,
- Output, and
- Processing.

We assessed the relevant controls identified above for the match process to terminated loans.

A significant weakness exists if management controls do not provide reasonable assurance that the process for planning, organizing, directing, and controlling program operations will meet the organization's objectives.

Significant Weaknesses

Although we identified areas in which the internal controls could be strengthened, we did not identify any significant weaknesses within the processes.

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APPENDIXES

Appendix A

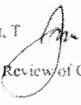
AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

Comment 1


U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20474-0001
November 7, 2008

MEMORANDUM FOR: Kenneth M. Donohue, Sr., Inspector General, G
FROM: Joseph J. Murn, President, T 
SUBJECT: Draft Audit Report on the Review of Controls Over Securitized Single Family Loans

Thank you for giving me an opportunity to comment on the draft audit report regarding Ginnie Mae's [REDACTED] "match to terminated" process. As you know, Ginnie Mae has implemented a number of important improvements to our risk management environment during 2008, and I am committed to working collaboratively with the Office of Inspector General (OIG) as we continue to make further changes. Ginnie Mae's responses to specific recommendations follow.

Recommendation 1A: *Implement specific policies and procedures that define the actions to be taken by [REDACTED] data errors and when issuers fail to make data corrections in a timely manner.*

Response: Ginnie Mae agrees with this recommendation.

[REDACTED]

[REDACTED] Match Notification Process", is a new quarterly process that will begin in December 2008.

Simultaneously with implementation of these improvements, Ginnie Mae will be developing new policies and procedures for inclusion in the Ginnie Mae Desk Manual.

Recommendation 1B: [REDACTED]

www.hud.gov epanot.hud.gov

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APPENDIXES

Appendix A

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

Comment 2

2

Response: [REDACTED]

Each Ginnie Mae issuer submits a loan level record for every loan in its Ginnie Mae portfolio on a monthly basis. These loan level records consist of 18 fields, some of which are typically static (borrower name, address, etc.) and some of which change from month to month (last payment date, remaining principal balance, etc.). As this data is uploaded into MBSIS, it is subjected to an edit process [REDACTED]

[REDACTED]

[REDACTED] These data edits are performed on all loan level records submitted by all issuers.

[REDACTED]

[REDACTED] would serve no business purpose given that [REDACTED]. It would also have adverse consequences with regard to risk analysis, data disclosure and other business functions that rely on loan level data, since for these business purposes many of the other [REDACTED] in order to achieve accurate reporting.

[REDACTED]

Recommendation IC: [REDACTED]

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APPENDIXES

Appendix A

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

Comment 3

Response: [REDACTED]

Prior to implementation of its loan matching program in 2003, Ginnie Mae performed a [REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

Comment 4

Recommendation 1D: [REDACTED]

Response: Ginnie Mae agrees with this recommendation.

[REDACTED] Over the next 60 days, Ginnie Mae will be conducting an analysis of this data to determine whether to modify or add an additional component [REDACTED] program that was announced in the [REDACTED].

Comment 5

Recommendation 1E: Assess the implementation of controls to [REDACTED]

Response: Ginnie Mae agrees with this recommendation for use on a limited, or "exception" basis.

As discussed in the response to [REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

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APPENDIXES

Appendix A

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

Comment 6

Recommendation 1F: Assess the implementation of controls that [REDACTED]

Response: Ginnie Mae agrees with this recommendation for use on a limited, or "exception" basis.

As discussed in the response to Recommendation 1E, Ginnie Mae is currently evaluating a [REDACTED]

Recommendation to 1G: Ensure that the Information Management Division for Ginnie Mae continues to be involved in the management of information system projects for the agency.

Response: The Information Management Division has always been, and will continue to be involved in the management of information system projects for the corporation.

Comment 7

Recommendation 1H: Prepare detailed system documentation for the [REDACTED] process.

Response: Ginnie Mae agrees with this recommendation.

Comment 8

[REDACTED] Ginnie Mae implemented [REDACTED] process within a production environment that includes detailed system documentation.

Recommendation 1I: Implement a procedure to perform the [REDACTED]

Comment 9

Response: Ginnie Mae agrees with this recommendation.

As discussed in the response to [REDACTED]

Recommendation 1J: Review and revise the programming code for the [REDACTED] to ensure that [REDACTED] loan records received are accounted for in the [REDACTED]

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APPENDIXES

Appendix A

AUDITEE COMMENTS AND OIG'S EVALUATION

Ref to OIG Evaluation

Auditee Comments

Comment 10

5

Response: Ginmie Mae does not agree with this recommendation because [REDACTED]
[REDACTED]

Ginmie Mae receives [REDACTED]
[REDACTED]. These controls were reviewed in [REDACTED]
[REDACTED] on behalf of Ginmie Mae and were found to be satisfactory.

Although we do not agree with all of the recommendations contained in the report, we agree in principle, as our actions have shown, that we need to improve certain of our risk management practices, including the creation of specific policies and procedures [REDACTED] on high risk issuers and loans, the placement of the [REDACTED] process into a monthly production environment, and the use of automated tools to detect loans ineligible for FHA insurance. In conclusion, I want to reemphasize our commitment to a healthy, collaborative relationship with the OIG. I would be happy to meet with you to discuss this further if you would like.



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OIG Evaluation of Auditee Comments

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

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[REDACTED]

[REDACTED]

[REDACTED]