Issue Date November 7, 2011
Audit Case Number 2012-FO-0001

TO: Theodore Tozer, President, Government National Mortgage Association, T

FROM: Thomas R. McEnanly, Director, Financial Audits Division, GAF

SUBJECT: Audit of Government National Mortgage Association's (Ginnie Mae) Financial Statement for Fiscal Years 2011 and 2010

In accordance with the Government Corporation Control Act as amended (31 U.S.C. 9105), the Office of Inspector General engaged the independent certified public accounting firm of Clifton Gunderson LLP (CG) to audit the fiscal years 2011 financial statements of the Government National Mortgage Association (Ginnie Mae). The contract required that the audit be performed according to Generally Accepted Government Auditing Standards (GAGAS). Ginnie Mae fiscal year 2010 financial statements were audited by other auditors; whose report dated November 5, 2010 expressed an unqualified opinion on those financial statements.

CG is responsible for the attached auditors' report dated November 2, 2011 and the conclusions expressed in the report. Accordingly, we do not express an opinion on Ginnie Mae's financial statements or conclusions on Ginnie Mae's internal controls or compliance with laws and regulations and government-wide policies.

This report includes both the Independent Auditors' Report and Ginnie Mae's principal financial statements. Under Federal Accounting Standards Advisory Board (FASAB) standards, a general-purpose federal financial report should include as required supplementary information (RSI) a section devoted to Management's Discussion and Analysis (MD&A) of the financial statements and related information. The MD&A is not included with this report. Ginnie Mae plans to separately publish an annual report for fiscal year 2011 that conforms to FASAB standards.

CG report on internal control identified certain deficiencies in internal control over financial reporting that they consider to be significant deficiencies. In addition, within 60 days of this report, CG expects to issue a separate letter to management dated November 2, 2011 regarding other matters that came to its attention during the audit.

We appreciate the courtesies and cooperation extended to the CG and OIG audit staffs during the conduct of the audit.

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Table of Contents

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Clifton Gunderson LLP
Certified Public Accountants & Consultants

INDEPENDENT AUDITOR'S REPORT

Inspector General
United States Department of Housing and Urban Development

President
Government National Mortgage Association

In our audit of the Government National Mortgage Association (Ginnie Mae), a wholly owned government corporation within the United States Department of Housing and Urban Development (HUD), for fiscal year (FY) 2011, we found:

- The balance sheet of Ginnie Mae as of September 30, 2011, and the related statements of revenues and expenses, changes in investment of U.S. Government and cash flows for the year then ended (hereinafter referred to as "financial statements") are presented fairly, in all material respects, in accordance with accounting principles generally accepted in the United States of America.
- No material weakness in internal control over financial reporting (including safeguarding of assets) and compliance with laws and regulations
- Two significant deficiencies related to a) the need to improve compliance control to ensure safety, completeness, and validity of collateral loan files, and b) strengthening internal control over risk-based issuer and document custodian reviews to improve the effectiveness of counterparty monitoring and oversight.
- No instance of noncompliance with selected provisions of laws and regulations tested.

The following sections (including Appendices A through C) discuss in more detail: (1) these conclusions, (2) our conclusions relating to the Management's Discussion and Analysis (MD&A) and other supplementary information, (3) management's responsibilities, (4) our audit objectives, scope and methodology, and (5) management's response and our evaluation of their response.

Opinion on Financial Statements

The financial statements including the accompanying notes, present fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America, Ginnie Mae's assets, liabilities, and investment of U.S. Government as of September 30, 2011, and revenues and expenses, changes in investment of U.S. Government, and cash flows for the year then ended. Ginnie Mae's financial statements as of and for the year ended September 30, 2010, were audited by other auditors; whose report dated November 5, 2010, expressed an unqualified opinion on those financial statements.

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INDEPENDENT AUDITOR'S REPORT, Continued

As discussed in Note H, Reserve for Losses on Mortgage-Backed Security (MBS) Program Guaranty, Ginnie Mae utilizes a statistically-based model that evaluate numerous factors, including, but not limited to, general and economic conditions, mortgage characteristics, and actual and expected future default and loan loss experience in establishing the reserve for losses. Deviations from these factors could have a material impact on the reserve.

Also, as discussed in Note N, Subsequent Events, Ginnie Mae defaulted two single family Mortgage-Backed Security (MBS) issuers with total mortgage loans' remaining principal balance of $901.9 million.

Consideration of Internal Control over Financial Reporting and Compliance

In planning and performing our audit, we considered Ginnie Mae's internal control over financial reporting and compliance (internal control) as a basis for designing our auditing procedures and to comply with Office of Management and Budget (OMB) audit guidance for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Ginnie Mae's internal control over financial reporting and compliance or on management's assertion on internal control included in Management's Discussion and Analysis (MD&A). Accordingly, we do not express an opinion on the effectiveness of Ginnie Mae's internal control over financial reporting and compliance nor on management's assertion on internal control included in the MD&A.

Our consideration of internal control over financial reporting and compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting and compliance that might be significant deficiencies or material weaknesses.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency or a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a control deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. We consider the deficiencies identified in Appendix A to be significant deficiencies in internal control over financial reporting and compliance.

We noted other nonreportable matter involving Ginnie Mae's internal control and its operation that we communicated in a separate letter to Ginnie Mae's management dated November 2, 2011.

Our consideration of internal control was for the limited purpose described in the first paragraph above and would not necessarily identify all significant deficiencies in internal control that are also considered to be material weaknesses. However, we do not believe the significant deficiencies listed below and described in Appendix A are material weaknesses.

1. Need to Improve Compliance Control to Ensure the Safety, Completeness, and Validity of Collateral Loan Files

INDEPENDENT AUDITOR'S REPORT, Continued

2. Strengthen Internal Control over Risk-Based Issuer and Document Custodian Reviews to Improve the Effectiveness of Counterparty Monitoring and Oversight

Compliance with Laws and Regulations

Our tests of Ginnie Mae's compliance with selected provisions of laws and regulations for FY 2011 disclosed no instance of noncompliance that are reportable under United States generally accepted government auditing standards or OMB audit guidance. However, the objective of our audit was not to express an opinion on overall compliance with laws and regulations or on management's assertion of compliance with laws and regulations included in the MD&A. Accordingly, we do not express such an opinion.

Consistency of Other Information

Ginnie Mae's MD&A contains a wide range of information, some of which is not directly related to the financial statements. We reviewed this information for consistency with the financial statements and discussed the methods of measurement and presentation with Ginnie Mae's officials. Based on this limited work, we found no material inconsistencies with the financial statements; accounting principles generally accepted in the United States, or OMB guidance. However, we do not express an opinion on this information.

Management's Responsibilities

Ginnie Mae's management is responsible for (1) preparing the financial statements in conformity with accounting principles generally accepted in the United States, (2) establishing, maintaining and assessing internal control to provide reasonable assurance that the broad control objectives of the Federal Managers Financial Integrity Act of 1982 (FMFIA) are met, and (3) complying with applicable laws and regulations.

Audit Objectives, Scope and Methodology

We are responsible for obtaining reasonable assurance about whether the financial statements are presented fairly in all material respects, in conformity with accounting principles generally accepted in the United States of America. We are also responsible for: (1) obtaining a sufficient understanding of internal control over financial reporting and compliance to plan the audit, (2) testing compliance with selected provisions of laws and regulations that have a direct and material effect on the financial statements and laws for which OMB audit guidance requires testing, and (3) performing limited work with respect to other information appearing in the MD&A.

In order to fulfill these responsibilities, we (1) examined, on a test basis, evidence supporting the amounts and disclosures in the financial statements; (2) assessed the accounting principles used and significant estimates made by management; (3) evaluated the overall presentation of the financial statements; (4) obtained an understanding of Ginnie Mae and its operations, including its internal control over financial reporting (including safeguarding of assets) and compliance with laws and regulations; (5) tested relevant internal controls over financial reporting and compliance; (6) considered the design of the process for evaluating and reporting

INDEPENDENT AUDITOR'S REPORT, Continued

on internal control and financial management systems; and (7) tested compliance with selected provisions of certain laws and regulations.

We did not evaluate all internal controls relevant to operating objectives as broadly defined by FMFIA, such as those controls relevant to preparing statistical reports and ensuring efficient operations. We limited our internal control testing to controls over financial reporting and compliance. Because of inherent limitations in internal control, misstatements due to error, fraud, losses or noncompliance may nevertheless occur and not be detected. We also caution that projecting our evaluation to future periods is subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with controls may deteriorate. In addition, we caution that our internal control testing may not be sufficient for other purposes.

We did not test compliance with all laws and regulations applicable to Ginnie Mae. We limited our tests of compliance to selected provisions of those laws and regulations that have a direct and material effect on the financial statements and those required by OMB audit guidance that we deemed applicable to Ginnie Mae's financial statements for the fiscal year ended September 30, 2011. We caution that noncompliance with laws and regulations may occur and not be detected by these tests and that such testing may not be sufficient for other purposes.

We performed our audit in accordance with auditing standards generally accepted in the United States; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB audit guidance as applicable to government corporations. We believe that our audit provide a reasonable basis for our opinion.

Ginnie Mae Comments and Our Evaluation

Ginnie Mae's management agreed with our recommendations but disagreed with certain conditions identified in our findings. We disagreed with Ginnie Mae's categorization of the findings' conditions and stand by the conclusions reached in our report. The full text of Ginnie Mae management's response is included as Appendix B. We did not perform audit procedures on Ginnie Mae management's written response. Accordingly, we express no opinion on it. Our assessment of Ginnie Mae management's response is included as Appendix C.

Distribution

This report is intended solely for the information and use of the management of Ginnie Mae and HUD, the HUD Office of Inspector General, OMB, the Government Accountability Office, and the United States Congress, and is not intended to be, and should not be, used by anyone other than these specified parties.

Clifton Gunderson LLP

Arlington, Virginia
November 2, 2011

Ginnie Mae
Independent Auditor's Report
Significant Deficiency
Appendix A

1. Need to Improve Compliance Control to Ensure the Safety, Completeness and Validity of Collateral Loan Files

In August 2009, Ginnie Mae defaulted one of its largest Mortgage-Backed Security (MBS) issuers. Ginnie Mae extinguished the issuer's interests and rights in the pooled mortgages and contracted with a financial institution to be its master sub-servicer for the defaulted issuer's MBS pools. The master sub-servicer began servicing to fulfill Ginnie Mae's guarantee to MBS investors in August 2009. Loans that are non-performing (loans with overdue mortgage payments for 120 days or more) are repurchased by Ginnie Mae from the defaulted MBS pools and hold them as Mortgages Held for Investments (MHFI). The MHFI from this defaulted issuer is approximately $6 billion out of the $6.6 billion MHFI at September 30, 2011. The mortgage loans from the same defaulted issuer being serviced are approximately $13.7 billion at September 30, 2011.

Ginnie Mae's master sub-servicer contracts with an independent document custodian to ensure the safety and completeness of the mortgage collateral documentation. The current custodian has not been able to provide a final certification within 12 months from transfer of the portfolio from the predecessor custodian as required by the Ginnie Mae MBS Guide (Guide). A significant portion (exceeding the required 20 percent pool threshold of the mortgage pools) could not be final certified due to the poor condition of the collateral loan files (for example, missing some or all documentation).

Under the Guide, the document custodian is required to certify to Ginnie Mae that loans constituting the pools of mortgages (as collaterals for Ginnie Mae securities) are supported by documents placed in the document custodian's control for the life cycle of the loans. The document custodian performs this function through safekeeping, a process of pool certification, and recertification and tracking controls. The Guide requires document custodian to final certify/recertify MBS pool within 12 months from the date of transfer. The transfer of the mortgage loan pool documentation from the former custodial bank to Ginnie Mae's master sub-servicer was in September 2009.

We understand that the default of one of the largest Ginnie Mae MBS issuers in August 2009 was unprecedented. Moreover, as published in various news media, Ginnie Mae's master sub-servicer is having significant problems with its mortgage servicing arm. We are also aware that Ginnie Mae is committed to correcting this issue and is working with the master sub-servicer to accelerate the review of the loan collateral files and documents with exceptions that are preventing the document custodian from issuing final certification. However, as of September 30, 2011, Ginnie Mae had not reached a final agreement for a timeline as to when the review of loan files/final certification of all loans will be completed. The delays in the review process caused by the poor condition of the loan files and the master sub-servicers problems will delay the processing of the loan modifications, prepayments, initiating foreclosures, and filing claims with the federal insuring agencies. As Ginnie Mae continues to purchase non-performing loans from the MBS pools, these delays result in additional costs to carry these non-performing loans. Moreover, in some cases where certain exceptions in the loan documents that could prevent filing claims with or obtaining payments from the federal insuring agency, Ginnie Mae's MHFI may be potentially overstated, and the reserve for losses potentially understated. Once loan files reviews/final certifications are completed, Ginnie Mae will be able to better assess the extent of any added costs to cure defective loans and/or losses incurred.

Ginnie Mae
Independent Auditor's Report
Significant Deficiency
Appendix A

Recommendation

1. We recommend that Ginnie Mae's Acting Vice-President for MBS hold the master sub-servicer accountable for delays by requiring an acceptable written timeline for completing the final review/certification of the loan documentation/pools.

2. Strengthen Internal Control over Risk-Based Issuer and Document Custodian Reviews to Improve the Effectiveness of Counterparty Monitoring and Oversight

Ginnie Mae, due to its personnel funding structure resulting in limited personnel resources, outsourced many of its operational, monitoring, and administrative functions and placed significant reliance on the performance and the reports of the outside consultants. One of the outsourced functions is the field reviews monitoring of issuers and document custodians' (contractors) compliance with the MBS guide and their implementation of internal control to minimize certain financial risks and potential losses to Ginnie Mae. We reviewed three completed field reviews conducted by the consultants in fiscal year 2011. We found that the workpapers for the completed reviews were incomplete in terms of documentation, meeting tests objectives, and performing applicable procedures that are outlined in Ginnie Mae's *Issuer and Document Custodian Risk Based Review Procedures Manual (*RBM). Ginnie Mae's contractor assessment reviews (CAR) conducted in fiscal year 2011 also identified similar deficiencies in the field reviews. Consequently, these reviews may be insufficient for Ginnie Mae to rely upon.

In addition, we noted that the last comprehensive update to the RBM was made on December 1, 2005. Ginnie Mae has changed and implemented numerous policies and procedures in response to the current financial crisis which started in 2008. These changes and enhancements such as new review procedures necessary to address the current environment are not incorporated in the RBM. A continuing failure to update the manual would increase the risk that deficiencies in the reviews could occur. Ginnie Mae self-identified this deficiency in fiscal year 2011 in its testing of internal control in accordance with OMB Circular A-123, *Management's Responsibility for Internal Control.*

The field reviews must be contractually performed according to the Ginnie Mae Issuer and Document Custodian Risk Based Review Procedures Manual and must conform to the overall Ginnie Mae monitoring standards for internal control sets forth in OMB Circular No. A-123, *Management's Responsibility for Internal Control.*

Recommendations

2a. Ginnie Mae's Acting Vice-President for MBS should increase its oversight and monitoring of the field reviews performed on issuers and document custodians to ensure the reviews meet management's objectives and are adequately and completely performed and properly documented.

Ginnie Mae
Independent Auditor's Report
Response to Auditor Report
Appendix A

2b. Ginnie Mae Executive Vice-President should allocate resources within MBS and Risk Management Division to accelerate the update to the *Issuer and Document Custodian Risk Based Review Procedures Manual* within the second fiscal quarter of 2012 if possible, so that new updated reviews are performed in second half of 2012 to eliminate this deficiency.

Ginnie Mae
Management's Response to Findings
Contained in the Independent Auditor's Report
Appendix B

U.S. DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
WASHINGTON, DC 20410-9000

PRESIDENT, GOVERNMENT
NATIONAL MORTGAGE ASSOCIATION

November 4, 2011

Ms. Mia Leswing, CPA
Clifton Gunderson LLP
4250 N Fairfax Drive, Suite 1020
Arlington, VA 22203

Dear Ms. Leswing:

Thank you for the opportunity to review and comment on Clifton Gunderson's (Clifton) draft audit report on Ginnie Mae's financial statement for Fiscal Year (FY) 2011.

We appreciate Clifton's acknowledgement that Ginnie Mae's financial statements, as of September 30, 2011, are presented fairly, in all material respects, in accordance with generally accepted accounting principles. Additionally, we appreciate Clifton's acknowledgement that for FY 2011, the audit disclosed no material weaknesses in internal controls over financial reporting, and no instance of noncompliance with laws and regulations.

Your report noted two significant deficiencies related to (a) the need to improve compliance control to ensure safety, completeness, and validity of collateral loan files, and (b) strengthening internal controls over risk-based issuer and document custodian reviews to improve the effectiveness of counterparty monitoring and oversight. We agree and have implemented your recommendation to establish an acceptable timeline for completing the final review/certification of the loan documentation. We also agree with your recommendation to increase the oversight and monitoring of the field reviews performed on issuers and document custodians, as well as accelerating the update to the *Issuer and Document Custodian Risk-Based Review Procedures Manual* (Risk-Based Manual). However, we believe that the assumptions presented in the report are fundamentally flawed. While Ginnie Mae acknowledges that there are some weaknesses in the overall execution of the underlying process, we do not believe such weaknesses indicate the presence of a significant deficiency.

Your report states that "in some cases where certain exceptions in the loan documents that could prevent filing claims with or obtaining payments from the federal insuring agency, Ginnie Mae's mortgage loans held for investment (MHFI) may be potentially overstated, and the reserve for losses potentially understated." Ginnie Mae and its master subservicer (MSS) have reviewed the pooled and non-pooled loans and identified approximately 1800 loans that are uninsured; this equates to less than one percent of the total loans in the defaulted portfolio at the time of extinguishment. These mortgage loans have been valued in accordance with ASC 310-30 and modeled in line with a significant severity assumption, and thus, any uncollectable amounts have been written off as loss on credit impairment mortgage loans held for investment.

Ginnie Mae
Management's Response to Findings
Contained in the Independent Auditor's Report
Appendix B

Through a process of matching Ginnie Mae loan level data with FHA data, there is no evidence that there are any additional uninsured loans in pools or mortgages held for investment.

The delays in filing the claims on these loans are a result of our MSS's legal problems. This has caused the MSS to delay filing and to be extra cautious in their actions with claims. We have accounted for lengthier timelines and the associated foreclosure costs (in excess of reimbursable costs) in our reserve for loss.

Given the facts stated above, we are confident that both the MHFI and reserve for loss are fairly stated. The loans in these pools have FHA insurance due to the fact that the defaulted issuer (defaulted August 2009) was a LI lender, a lender delegated by FHA to insure their loans. This means that under FHA regulations, FHA must honor the loan as insured, and FHA's recourse is with the orginator, not Ginnie Mae. Therefore, the remaining loans in the MBS pools and the MHFI that were not already identified as uninsured, are insured under the FHA regulations.

As of October 31, 2011, we have developed an agreed-upon timeline with our MSS to complete the final review and certification by June 2012. The following actions have been or will be completed:

- The MSS hired an expert subcontractor to perform the re-certification process.
- The subcontractor completed the search for missing documents on October 28, 2011.
- The subcontractor has delivered roughly 14,000 documents to the custodial bank.
- Exceptions are expected to increase in the short run as the custodial bank reviews the documents. The subcontractor will then begin to cure all unclear or indefinable documents.
- The MSS has instructed the custodial bank to keep appropriate staff on hand to deal with workload.
- The subcontractor is currently researching and correcting title issues on loans.
- The MSS expects all documents that were not found by the subcontractor to be recreated by February 20, 2012.
- The entire project is on track to be completed with the final certification of all pools by June 2012.
- The MSS will provide monthly updates to Ginnie Mae.

Regarding the issuer and document custodian reviews, we agree with your recommendation that Ginnie Mae should increase its oversight and monitoring of the field

Ginnie Mae
Management's Response to Findings
Contained in the Independent Auditor's Report
Appendix B

reviews; however, we have not found any evidence to support your assertion that "the workpapers for the completed reviews were incomplete in terms of documentation, meeting test objectives, and performing applicable procedures that are outlined in Ginnie Mae's Risk-Based Manual. We believe that the following points should be considered when determining whether or not this item(s) rise to the level of a significant deficiency. Please consider the following:

- We believe that our contractor adequately explained why certain "if applicable" test objectives were not performed (e.g. single asset multifamily pool not being tested for delinquency when the sole loan is current) and that these responses were not adequately considered in the final determination of issue severity;

- We highlight that when asked, our contractor made it clear that additional supporting documentation was available for the audit team's consideration. The audit team declined to review the additional material available and defaulted to their definition of what a "work paper" must contain; and

- Our monitoring staff has few occasions to leverage the work papers and instead relies on the report provided by the contractor for the day-to-day management of issuer compliance. In rare instances where further research is needed to resolve an issue with an issuer, work papers may be requested.

The above being said, we agree that a more conventional definition of work paper documentation standards will be adopted. Our contractor will provide a scope justification amendment to their work papers that will allow the work papers to stand on their own and clarify the applicability of certain tests. Additionally, this will provide an explanation as to why the compliance review had changes to test sample sizes and/or the exclusion of certain tests as they are not applicable to the review. The expected implementation date of this change is December 1, 2011.

Although the current field review contractor is not required to be a Certified Public Accountant, the Statement of Work issued in the next recompete will make that a requirement. Additionally, Ginnie Mae will add additional Government Technical Monitors (GTM) to this contract in order to heighten the oversight on this important contract.

Ginnie Mae
Management's Response to Findings
Contained in the Independent Auditor's Report
Appendix B

As for the Risk-Based Manual, we agree that it is a best practice to update our procedures and procedures leveraged by our contractors on a routine basis. This documentation allows for new staff and contractor personnel to have clarity on what key steps are required. That being said, the combination of the content of the Risk-Based Manual, in conjunction with work orders executed by the GTR, represents a comprehensive set of tests that help to ensure issuer compliance with the program. The absence of this documentation update directly into the Risk-Based Manual in no way diminishes the power of the work program as performed. Ginnie Mae believes that, in light of the audit team not identifying significant gaps in the process as practiced, that this issue does not rise to the level of a significant deficiency. Ginnie Mae is committed to updating the Risk-Based Manual in FY 2012.

At Ginnie Mae, we believe in doing business right and are committed to being an open and transparent organization. We enjoyed working with Clifton and welcome the opportunity to further discuss the items presented.

Again, thank you for the opportunity to comment on the draft report.

Sincerely,

Theodore W. Tozer

Ginnie Mae
CG's Assessment of Management's Response
Contained in the Independent Auditor's Report
Appendix C

We obtained and reviewed Ginnie Mae's management response to the findings and recommendations, included as Appendix B, made in connection with our audit of Ginnie Mae's FY 2011 Financial Statements. We did not perform audit procedures on Ginnie Mae's written response to the findings and recommendations and, accordingly, we express no opinion on them. Our assessment of management's response is discussed below.

Assessment of management's response to significant deficiencies:

As indicated in Appendix B, Ginnie Mae's management agreed with our recommendations to the two significant deficiencies and has outlined their corrective actions that have started or soon to start with the implementation.

Ginnie Mae's management disagreed with certain conditions identified in the findings. Ginnie Mae also stated that they do not believe the findings rise to the level of significant deficiencies. We disagreed with Ginnie Mae's assessment and the categorizations provided in their response in support of their position. We stand by the findings and conclusions reached in our report.

Audit Report of Ginnie Mae's Fiscal Year 2011 Financial Statements

Ginnie Mae's Fiscal Year 2011 Financial Statements

Balance Sheets

September 30		**2011**		**2010**
(Dollars in thousands)				
Assets:				
Funds with U.S. Treasury	$	7,210,300	$	6,650,500
U.S. Government securities		2,126,800		3,551,200
Accrued interest on U.S. Government securities		11,800		20,400
Accrued fees and other receivables, net		62,500		54,900
Fixed assets--software, net of accumulated amortization		31,100		35,800
Mortgage loans held for investment, net		6,350,300		4,443,300
Accrued Interest on mortgage loans held for investment		83,400		181,300
Advances against defaulted Mortgage-Backed security pools		873,700		1,054,300
Less: Allowance for uncollectible advances		(220,500)		(212,200)
Advances against defaulted Mortgage-Backed security pools, net		653,200		842,100
Short sale claims receivables		38,600		-
Less: Allowance for uncollectible short sale claims receivables		(6,300)		-
Short sale claims receivables, net		32,300		-
Properties held for sale		7,400		49,200
Less: Allowance for losses on properties held for sale		(4,000)		(6,900)
Properties held for sale, net		3,400		42,300
Mortgage servicing rights		110,900		137,700
Guaranty Asset		2,175,100		1,103,800
Total Assets	$	18,851,100	$	17,063,300
Liabilities and Investment of U.S. Government:				
Liabilities:				
Reserve for loss on Mortgage-Backed Securities Program Guaranty		395,800	$	1,004,900
Deferred revenue		117,400		113,900
Deferred liabilities and deposits		35,700		1,200
Accounts payable and accrued liabilities		365,300		261,700
Guaranty Liability		2,175,100		1,103,800
Total Liabilities	$	3,089,300	$	2,485,500
Commitments and Contingencies				
Investment of U.S. Government		15,761,800		14,577,800
Total Liabilities and Investment of U.S. Government	$	18,851,100	$	17,063,300

The accompanying notes are an integral part of these financial statements.

Statements of Revenues and Expenses and Changes in Investment of U.S. Government				
For the Years Ended September 30		**2011**		**2010**
(Dollars in thousands)				
Revenues:				
Mortgage-Backed Securities Program income	$	856,500	$	742,900
Interest income		208,100		269,000
Total Revenues	$	1,064,600	$	1,011,900
Expenses:				
Mortgage-Backed Securities Program expenses		72,800		72,700
Administrative expenses		11,000		10,300
Fixed asset amortization		9,900		9,500
Total Expenses	$	93,700	$	92,500
Recapture of Provision for Loss on properties held for sale		2,900		-
Recapture of Provision for Loss on Mortgage-Backed Securities Program Guarantee		407,000		
Less: Provision for Loss on Mortagage-Backed Securities Program				730,000
Less: Provision for Loss on Uncollectible Advances		8,500		-
Less: Provision for Loss on Short Sale Claims and Other Receivables		6,800		-
Total Recapture of Provision / (Provision for Losses)	$	394,600	$	(730,000)
Gain on disposition of investment		24,000		214,400
Gain on acquisition mortgage servicing rights				137,700
Less: Loss on mortgage servicing rights		26,800		
Less: Loss on credit impairment of mortgage loans HFI, net		178,700		-
Total Gains / (Losses)	$	(181,500)	$	352,100
Excess of Revenues over Expenses		1,184,000		541,500
Investment of U.S. Government at Beginning of Year		14,577,800		14,036,300
Returned to U.S. Treasury		-		-
Investment of U.S. Government at End of Year	$	15,761,800	$	14,577,800

The accompanying notes are an integral part of these financial statements.

Statements of Cash Flows

For the Years Ended September 30	2011	2010
(Dollars in thousands)		
Cash Flow from Operating Activities		
Net Excess of Revenues over Expenses	$ 1,184,000	$ 541,500
Adjustments to reconcile Net Excess of Revenues Over Expenses to Net Cash from Operating Activities:		
Amortization	9,900	9,500
Decrease / increase in accrued interest on U.S. Government securities	8,600	20,900
Decrease / increase in accrued interest on mortgage loans held for investment	97,900	(181,300)
Decrease / increase in advances against defaulted MBS pools, net	188,900	(722,000)
Decrease / increase in mortgage servicing rights	26,800	(137,700)
Increase / decrease in deferred revenue	3,500	(500)
Increase / decrease in deferred liabilities and deposits	34,500	(1,400)
Increase / decrease in accounts payable and accrued liabilities	103,600	203,000
Increase / decrease in accrued fees and other receivables	(7,600)	(10,300)
Increase / decrease in short sale claims receivables, net	(32,300)	-
Decrease / increase in properties held for sale, net	38,900	(37,800)
Decrease / increase in reserve for loss on MBS program guaranty	(609,100)	445,000
Decrease / increase in MBS Reserve, net of other assets relating to operating activities	(610,100)	396,900
Total Adjustments	(136,400)	(412,600)
Net Cash from Operating Activities	$ 1,047,600	$ 128,900
Cash Flow from Investing Activities		
Increase / decrease in mortgage loans held for investment, net	(1,907,000)	(4,411,300)
Sale / purchase of U.S. Government securities, net	1,424,400	5,684,600
Purchase / sale of software	(5,200)	(5,500)
Net Cash (used for) from Investing Activities	$ (487,800)	$ 1,267,800
Cash Flow from Financing Activities		
Financing activities	-	-
Net Cash from (used for) Financing Activities	$ -	$ -
Net increase in cash & cash equivalents	559,800	1,396,700
Cash & cash equivalents - beginning of period	6,650,500	5,253,800
Cash & cash equivalents - end of period	$ 7,210,300	$ 6,650,500

Supplemental Schedule of Non-Cash Activities

For the Years Ended September 30	2011	2010
(Dollars in thousands)		
Transfer of Advances against Defaulted MBS pools to Mortgage Loans Held for Investment	$ 2,175,500	$ 4,467,000
Transfer from Mortgage Loans Held for Investment to Properties Held for Sale	$ 148,900	$ 118,700

The accompanying notes are an integral part of these financial statements.

Notes to the Financial Statements

September 30, 2011 and 2010

Note A: Organization and Summary of Significant Accounting Policies

The Government National Mortgage Association (Ginnie Mae) was created in 1968, through an amendment of Title III of the National Housing Act as a government corporation within the Department of Housing and Urban Development (HUD). The Mortgage-Backed Securities (MBS) program is Ginnie Mae's primary ongoing activity. Its purpose is to increase liquidity in the secondary mortgage market and attract new sources of capital for residential mortgage loans. Through the program, Ginnie Mae guarantees the timely payment of principal and interest on securities backed by pools of mortgages issued by private institutions. This guaranty is backed by the *full faith and credit of the U.S. Government*. Ginnie Mae requires that the mortgages be insured or guaranteed by the Federal Housing Administration (FHA), the U.S. Department of Agriculture (USDA), the Department of Veterans Affairs (VA), or the HUD Office of Public and Indian Housing (PIH). These MBS are not assets of Ginnie Mae, nor are the related outstanding securities liabilities; accordingly, neither is reflected on the accompanying balance sheets.

To ensure that adequate capital continues to flow, Ginnie Mae offers reliable solutions that meet the needs of a broad constituent base and provide sufficient flexibility to respond to market changes. At the core of its business model and its product offering menu is the simple pass-through security, which comes in the form of two product structures—Ginnie Mae I MBS and Ginnie Mae II MBS. Each of these Ginnie Mae product structures has specific characteristics regarding pool types, note rates, collateral, payment dates and geographical locations.

The underlying source of loans for the Ginnie Mae I MBS and Ginnie Mae II MBS comes from Ginnie Mae's following four main programs, which serve a variety of loan financing needs and different issuer origination capabilities:

- ***Single Family Program*** – The majority of Ginnie Mae securities are backed by single family mortgages predominantly originated through FHA and VA loan insurance programs.
- ***Multifamily Program*** **–** Safe and affordable rental housing is essential for millions of individuals and families. Ginnie Mae's mission of supporting affordable housing and promoting stable communities extends to ensuring that decent rental units remain within reach of those who need them. By guaranteeing pools of multifamily loans that are sold to investors in the global capital markets, Ginnie Mae enables lenders to reduce mortgage interest rates paid by property owners and developers of apartment buildings, hospitals, nursing homes, assisted-living facilities, and other housing options.

- ***HMBS Program*** – In addition to traditional mortgages, Ginnie Mae's expanding Home Equity Conversion Mortgage (HECM) securities program provides capital and liquidity for FHA-insured reverse mortgages, an essential financial solution for a growing number of seniors. HECM loans can be pooled into HECM Mortgage Backed Securities (HMBS) within the Ginnie Mae II MBS program. Because Ginnie Mae enables a broad secondary market for HECM loans, the availability of HECM lending from multiple lenders has been deepened and broadened and related borrowing costs have been reduced.
- ***Manufactured Housing (MH) Program*** – Ginnie Mae's Manufactured Housing program allows the issuance of pools of loans insured by FHA's Title I Manufactured Home Loan Program.

Basis of Presentation: The accompanying consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP").

Funds with U.S. Treasury: All of Ginnie Mae's receipts and disbursements are processed by the U.S. Treasury, which in effect maintains Ginnie Mae's bank accounts. Of the $7.2 billion in Funds with U.S. Treasury, $5.5 billion is in the Reserve Receipt Account, which is a noninterest-bearing account at the U.S. Treasury. For purposes of the Statements of Cash Flow, Funds with U.S. Treasury are considered cash.

U.S. Government Securities: U.S. Government Securities are classified as held for investment as Ginnie Mae has both the ability and the intent to hold until maturity, and are carried at amortized cost. Interest income on such securities is included in Interest Income on the Statements of Revenues and Expenses. Discounts and premiums are amortized, on a level yield basis, over the life of the related security.

Fixed Assets: Ginnie Mae's fixed assets represent systems (software) that are used to accomplish its mission. Ginnie Mae capitalizes significant software development project costs per guidance in ASC Subtopic 350-40 *Intangibles—Goodwill and Other – Internal-Use Software* (ASC 350-40) and amortizes them over a three- to five-year period beginning with the project's completion. As of September 30, 2011, and September 30, 2010, Ginnie Mae's Fixed Assets – Software balance was $69.5 million, with accumulated amortization of $38.4 million, and $64.3 million, with accumulated amortization of $28.5 million, respectively.

Mortgage Loans Held for Investment: When a Ginnie Mae issuer defaults, Ginnie Mae is required to step into the role of the issuer and make the timely pass-through payments to investors and, subsequently, acquires the servicing rights and obligations of the entire Ginnie Mae guaranteed, pooled loan portfolio of the defaulted issuer. As the servicer Ginnie Mae assesses loans to determine whether the loan should be purchased out of the pool. Ginnie Mae will purchase mortgage loans out of the pool when:

a. Mortgage loans are uninsured by the FHA, USDA, VA or PIH, or
b. Mortgage loans were previously insured but insurance is currently denied (collectively with (a.), referred to as uninsured mortgage loans),
c. And may purchase mortgage loans that are insured but are delinquent for more than 120 days based on management discretion. This buyout policy was implemented in FY2010 and was a business decision since it prevents Ginnie Mae from continuing to pass through interest to investors at the note rate of the security when it is probable that Ginnie Mae will be reimbursed at the debenture rate in the case of FHA insured loans and not at all for VA and uninsured loans. Ginnie Mae's Guide states that loans can be repurchased at 90 day delinquency, however Ginnie Mae has decided to repurchase loans at 120 days delinquency as it is unlikely that these delinquencies will cure.

Ginnie Mae assesses the collectability of mortgage loans bought out of the pools of defaulted portfolios. During FY 2011, the majority of mortgage loans were bought out due to borrower delinquency of more than 120 days. Ginnie Mae evaluates the collectability of all loans and considers a loan as credit impaired at acquisition when there is evidence of credit deterioration subsequent to the loan's origination and it is probable, at acquisition, that Ginnie Mae will be unable to collect all contractually required payments receivable. Ginnie Mae considers guarantees and insurance from FHA, USDA, VA and PIH in determining whether it is probable that Ginnie Mae will collect all amounts due according to the contractual terms.

For non-VA insured loans, Ginnie Mae expects to collect the full amount of the unpaid principal balance and debenture rate interest (for months allowed in the insuring agency's timeline), when the insurer reimburses Ginnie Mae subsequent to filing a claim. As a result, these loans are under ASC Subtopic 310-20, *Nonrefundable Fees and Other Costs*. In accordance with ASC 310-20-30-5, these loans are recorded at the unpaid principal balance which is the amount Ginnie Mae pays to repurchase these loans. Accordingly, Ginnie Mae recognizes interest income on these loans on an accrual basis at the debenture rate for the number of months allowed under the insuring agency's timeline. After the allowed timeline, Ginnie Mae considers these loans to be non-performing as the collection of interest is no longer reasonably assured, and places these loans on non-accrual status.

Ginnie Mae assesses the collectability of mortgage loans bought out of the defaulted portfolios that are uninsured and defaulted loans that are VA insured for which Ginnie Mae only receives a portion of the original principal balance. Since the principal and interest payments are not fully guaranteed from the insurer or there is a lack of insurance, if these loans are delinquent at acquisition, it is probable that Ginnie Mae will be unable to collect all contractually required payments receivable. Accordingly, these loans are considered to be credit impaired and are accounted for under ASC Subtopic 310-30, *Loans and Debt Securities Acquired with Deteriorated Credit Quality*. At the time of acquisition, these loans are recorded at the lower of their acquisition cost or present value of expected amounts to be received. As non-performing loans, these loans are placed on nonaccrual status.

Ginnie Mae has the ability and the intent to hold these acquired loans for the foreseeable future or until maturity; therefore, Ginnie Mae classifies the loans as held for investment (HFI). These mortgage loans HFI are reported net of allowance for loan losses. Mortgage loans HFI include mortgage loans that are undergoing the foreclosure process. Upon completion of the foreclosure process, when Ginnie Mae acquires the title of the underlying properties, these properties are either conveyed to the insuring agency for claim and are reported as advances against defaulted MBS pools or are classified as properties held for sale.

The allowance for loss on mortgage loans HFI represents management's estimate of probable credit losses inherent in Ginnie Mae's mortgage loan portfolio. The allowance for loss on mortgage loans HFI is a contra asset account which when aggregated with the mortgage loans HFI, states the balance of loans that Ginnie Mae determines to be collectible. Ginnie Mae performs periodic and systematic reviews of its loan portfolios to identify credit risks and to assess the overall collectability of the portfolios. The allowance on certain homogeneous loan portfolios is based on aggregated evaluations.

Accrued Interest Mortgage Loans Held for Investment: Ginnie Mae records accrued interest on mortgage loans HFI for interest which Ginnie Mae determines that the ultimate collectability is probable. For non-VA insured loans, Ginnie Mae recognizes interest income on an accrual basis at the debenture rate for the number of months allowed under the insuring agency's timeline. After the allowed timeline, Ginnie Mae considers these loans to be non-performing as the collection of interest is not reasonably assured, and places these loans on non-accrual status. Ginnie Mae has assessed the collectability of VA and uninsured loans and determined that these loans are non-performing and hence, are placed on nonaccrual status.

Advances against Defaulted MBS Pools: Advances against defaulted MBS pools represent payments made to fulfill Ginnie Mae's guaranty of timely principal and interest payments to MBS security holders. Such advances are reported net of an allowance for uncollectible advances to the extent management believes they will not be recovered. The allowance for uncollectible advances is estimated based on actual and expected recovery experience including expected recoveries from FHA, USDA, VA, and PIH. Principal and Interest receivable for foreclosed properties that have been conveyed to the insuring agency are reported in the advance category while Ginnie Mae is awaiting payment of the receivable; these claims are reported net of allowance.

Short Sales Claims Receivable: As an alternative to foreclosure, a property may be sold for its appraised value even if such a sale results in a short sale where the proceeds are not sufficient to pay off the mortgage. These transactions are approved by Ginnie Mae's master sub-servicers and Ginnie Mae's MBS program office. Typically, the short sale occurs after Ginnie Mae has purchased the loan out of the pool and recorded the loan as Mortgage Loans HFI. However, in some circumstances, the short sale occurs while the mortgage loan is still in the pool.

Except for VA insured loans, for insured loans for which the underlying property was sold in a short sale, the insurer typically pays Ginnie Mae the difference between the proceeds received from the sale and the total contractual amount of the mortgage loan and interest at the debenture rate. Hence, Ginnie Mae does not incur any losses as a result of the short sale. Ginnie Mae records a Short Sale Claims Receivable while it awaits repayment of this amount from the insurer. For short sales claims receivable for which Ginnie Mae believes that collection is not probable, Ginnie Mae records an allowance for short sales receivable; the aggregate of the short sales receivable and the allowance for short sales receivable is the amount Ginnie Mae determines to be collectible.

Properties Held for Sale: Ginnie Mae acquires title of the underlying property when foreclosure is finalized. For instances in which Ginnie Mae does not convey the property to the insuring agency, Ginnie Mae holds the title until the property is sold. As the properties are available for immediate sale in their current condition and are actively marketed for sale, they are reported as properties held for sale on the Balance Sheets in accordance with ASC Subtopic 360-10, *Property, Plant, and Equipment – Overall*. Properties held for sale are initially recorded on the Balance Sheets at fair value less its estimated cost to sell. The fair value less estimated cost to sell on the date of foreclosure is deemed to be the carrying value of the foreclosed asset. Subsequent to initial measurement, the properties held for sale are reported at the lower of the carrying amount or fair value less estimated cost to sell.

Mortgage Servicing Rights: Mortgage servicing rights (MSRs) represent Ginnie Mae's right and obligation, obtained from issuers upon default, to service mortgage loans in mortgage backed securities. Ginnie Mae records a servicing asset or servicing liability each time it undertakes an obligation to service a financial asset by entering into a servicing contract in (among other situations) an acquisition or assumption of a servicing obligation that does not relate to financial assets held by Ginnie Mae.

Ginnie Mae records a mortgage servicing asset on its Balance Sheet when the present value of the estimated compensation for mortgage servicing activities exceeds adequate compensation for such servicing activities and records a mortgage servicing liability when the present value of the estimated compensation for mortgage servicing activities is less than the adequate compensation for such servicing activities. Ginnie Mae considers adequate compensation to be the amount of compensation that would be required by a substitute master sub-servicer should one be required. Market information is used to determine adequate compensation for these services.

Ginnie Mae has elected the fair value option for the MSRs to better reflect the potential net realizable or market value that could be ultimately realized from the disposition of the MSR asset or the settlement of a future MSR liability. Upon acquisition, Ginnie Mae measures its MSRs at fair value and subsequently re-measures them with changes in the fair value recorded in the Statements of Revenues and Expenses (see Note F for more information regarding the initial and subsequent valuations of Ginnie Mae's MSRs).

Fair Value: Ginnie Mae measures the fair value of its financial instruments in accordance with accounting guidance that requires an entity to base fair value on exit price and maximize the use of observable inputs and minimize the use of unobservable inputs to determine the exit price. Accounting guidance defines fair value as the price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Ginnie Mae's MSRs are carried at fair value in accordance with applicable accounting guidance.

Ginnie Mae categorizes its financial instruments, based on the priority of inputs to the valuation technique, into a three-level hierarchy, as described below.

Level 1 Quoted prices in active markets for identical assets or liabilities. Level 1assets and liabilities include debt and equity securities and derivative contracts that are traded in an active exchange market, as well as certain U.S. treasury and other U.S. Government securities that are highly liquid and are actively traded in over-the-counter markets.

Level 2 Observable inputs other than Level 1 prices, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. Level 2 assets and liabilities include securities with quoted prices that are traded less frequently than exchange-traded instruments that are observable in the market or can be derived principally from or corroborated by observable market data. This category includes mortgages HFI, properties HFS, advances against defaulted MBS pools and guaranty assets and liabilities.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities. Level 3 assets and liabilities include financial instruments whose value is determined using pricing models, discounted cash flow methodologies, or similar techniques, as well as instruments for which the determination of fair value requires significant management judgment or estimation. This category includes mortgage servicing rights.

Reserve for Loss on MBS Program Guaranty: Reserve for Loss on MBS Program Guaranty is an accrual for loss contingency as a result of the guaranty provided on Mortgage Backed Securities portfolios when the following two conditions under ASC Subtopic 450-20, Contingencies – Loss Contingencies are met:

a. Information available before the issuance of the financial statements indicates that it is probable that a triggering event or condition has occurred at the date of the financial statements. It is implicit in this condition that it must be probable that one or more future events will occur confirming the fact of loss.

b. The amount of loss can be reasonably estimated.

Reserves are established to the extent management believes losses due to defaults are probable and estimable and FHA, USDA, VA, and PIH insurance or guarantees are insufficient to recoup Ginnie Mae expenditures. The reserve for loss on MBS program guaranty is a liability account on the Balance Sheets. Ginnie Mae recognizes the loss by recording a charge to the provision for loss on MBS program guaranty on the Statements of Revenue and Expenses. Ginnie Mae records charge-offs as a reduction to the reserve for loss on MBS program guaranty liability account when losses are confirmed and records recoveries as a credit to the reserve for loss on MBS program guaranty liability account. Accordingly, the reserves are increased by provisions recorded as an expense in the Statements of Revenues and Expenses and reduced by charge-offs, net of recoveries. Among other losses and recoveries, miscellaneous expenses related to foreclosure are not capitalized on the balance sheet and are charged off against the reserve for loss on MBS program guaranty and recoveries of these expenses through the claims process are shown as recoveries against the reserve for loss on MBS program guaranty.

Financial Guarantees: The Financial Accounting Standards Board's (FASB) Accounting Standards Codification (ASC) topic 460, *Guarantees* (ASC 460), formerly known as (FASB) Interpretation No. 45 (FIN 45), clarifies the requirements of accounting for *Contingencies* (ASC 450), relating to the guarantor's accounting for, and disclosure of, the issuance of certain types of guarantees. ASC 450 requires that upon issuance of a guaranty, the guarantor must recognize a liability for the fair value of the obligation it assumes under the guaranty. The issuance of a guaranty under the Mortgage-Backed Securities (MBSs) Program obligates Ginnie Mae to stand ready to perform over the term of the guaranty in the event that the specified triggering events or conditions occur.

At inception of the guaranty, Ginnie Mae recognizes a liability for the guaranty it provides on MBSs issued by third-party issuers. Generally, a guaranty liability is initially measured at fair value. However, Ginnie Mae applies the practical expedient in ASC 460-10-30-2a (ASC Topic 460, *Guarantees* (ASC 460)), which allows the guaranty liability to be recognized at inception based on the premium received or receivable by the guarantor, provided the guaranty is issued in a standalone arm's-length transaction with an unrelated party.

Ginnie Mae provides the guaranty of principal and interest payments to MBS holders in the event of issuer default and, in exchange, receives guaranty fees from the issuers. Ginnie Mae receives guaranty fees from the issuers on the unpaid principal balance of the outstanding MBSs in the non-defaulted issuer portfolio. These fees are paid on a monthly basis over the period that the guaranty is provided. As Ginnie Mae does not receive guaranty fees at inception of the guaranty, Ginnie Mae determines the initial measurement of the guaranty liability based on the expected present value cash flows to be received for the guaranty fee.

Ginnie Mae initially recognizes a guaranty liability at fair value for its obligation to stand ready to perform on these upon issuance of a guaranty. Subsequently, the guaranty liability is measured by a systematic and rational amortization method.

Additionally, as the guaranty is issued in a standalone transaction for a premium, Ginnie Mae records a guaranty asset (representing a receivable at net present value) for the guaranty fees as the offsetting entry for the guaranty liability in accordance with ASC 460-10-55-23a. Thus, there is no impact due to the guaranty liability and asset on the net financial position of Ginnie Mae.

The guaranty asset is calculated based on the present value of the expected future cash flows from the guaranty fees based on the unpaid principal balance of the outstanding MBSs in the non-defaulted issuer portfolio; this is the same calculation used to value the guaranty liability under the practical expedient method permitted in ASC 460-10-30-2a. In fiscal year 2011, Ginnie Mae's management updated the runoff variable in the model to use the runoff by year of issuance versus the runoff for the total portfolio as it was determined that using the runoff by year of issuance resulted in a more accurate valuation.

Recognition of Revenues and Expenses: Ginnie Mae receives monthly guaranty fees for each MBS mortgage pool, based on a percentage of the pool's outstanding balance. Fees received for Ginnie Mae's guaranty of MBS are recognized as earned. Ginnie Mae receives commitment fees as issuers request commitment authority, and recognizes the commitment fees as income as issuers use their commitment authority, with the balance deferred until earned or expired, whichever occurs first. Fees from expired commitment authority are not returned to issuers. Ginnie Mae recognizes as income the major portion of fees related to the issuance of multiclass securities in the period the fees are received, with the balance deferred and amortized over the weighted average life of the underlying mortgages.

Mortgage-Backed Securities Program Income on the Statements of Revenues and Expenses includes: $686.2 million of guaranty fees, $74.0 million of commitment fees, $52.5 million of multiclass fees, $42.3 million of interest income from mortgage loans held for investment and $1.5 million in other revenue. Mortgage-Backed Securities Program Expenses on the Statements of Revenues and Expenses are: $21.2 million of multiclass expenses, $17.2 million of MBS information systems and compliance expenses, $9.7 million of central paying agent expenses, $7.6 million of information technology and miscellaneous expenses, $5.1 million of Multifamily claims, and $12 million of other expenses.

Statements of Cash Flows: Ginnie Mae prepares the Statements of Cash Flows on an indirect basis. For purposes of the Statements of Cash Flows, Funds with U.S. Treasury are considered cash. Ginnie Mae classifies cash flows from operations related to its programs and overall business operations (accrued interest, deferred revenue and liabilities, accounts payable and reserves) as operating activities. Ginnie Mae classifies cash flows from securities that Ginnie Mae intends to hold for investment (U.S. Government securities and mortgage loans HFI) and capital expenditures and proceeds from sale of software as investing activities. Ginnie Mae classifies cash flows from any non-federal transactions necessary to finance or fund the operations of the agency as financing activities; of which there are none. Management determines the cash flow classification at the date of purchase of a loan, whether it intends to sell (operating activity) or hold the loan for the foreseeable future (investing activity). As of fiscal year 2010, Ginnie Mae has determined that mortgage loans are held for investment. Ginnie Mae has updated the fiscal year 2010 Statement of Cash Flow to break out the increase in mortgage loans HFI as a part of the cash flows from investing activities while keeping the increase in accrued interest on mortgage loans HFI in operating activities.

Use of Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the U.S. requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Ginnie Mae has made significant estimates in a variety of areas including, but not limited to, valuation of certain financial instruments and other assets and liabilities, and establishing the reserve for loss in MBS program guaranty. While Ginnie Mae believes its estimates and assumptions are reasonable based on historical experience and other factors, actual results could differ from those estimates.

Adoption of New Accounting Standard: Ginnie Mae adopted the new accounting standard, Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) 2010-6, Improving Disclosures about Fair Value Measurements, which was effective for annual reporting period beginning after December 15, 2009. The adoption of ASU 2010-6 did not affect the financial statement results since it amends only the disclosure requirements for fair value measurements.

Note B: U.S. Government Securities

The U.S. Government securities portfolio is held in special market-based U.S. Treasury securities that are bought and sold at composite prices received from the Federal Reserve Bank of New York. These securities are maintained in book-entry form at the Bureau of Public Debt and are made up of overnight certificates, U.S. Treasury notes, and U.S. Treasury inflation-indexed securities (reflecting inflation compensation). The coupon rates of Ginnie Mae's holdings, with a maturity of greater than one year, as of September 30, 2011, range from 0.63 percent to 2.0 percent. As of September 30, 2010, they ranged from 0.63 percent to 3.38 percent.

The amortized cost and fair values as of September 30, 2011, were as follows:

(Dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury Overnight Certificates	$ -	$ -	$ -	$ -
U.S. Treasury Notes	994,100	44,400	-	1,038,500
U.S. Treasury Inflation-Indexed Securities	1,132,700	56,300	-	1,189,000
Total	**$ 2,126,800**	**$ 100,700**	**$ -**	**$ 2,227,500**

The amortized cost and fair values as of September 30, 2010, were as follows:

(Dollars in thousands)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury Overnight Certificates	$ 239,500	$ -	$ -	$ 239,500
U.S. Treasury Notes	991,900	45,300	-	1,037,200
U.S. Treasury Inflation-Indexed Securities	2,319,800	121,300	-	2,441,100
Total	**$ 3,551,200**	**$ 166,600**	**$ -**	**$ 3,717,800**

The amortized cost, fair value, and annual weighted average interest rates of U.S. Government securities at September 30, 2011, by contractual maturity date, were as follows:

(Dollars in thousands)	Amortized Cost	Fair Value	Weighted Average Interest Rate
Due within one year	$ -	$ -	-
Due after one year through five years	2,126,800	2,227,500	0.16%
Due after five years through ten years	-	-	-
Total	**$ 2,126,800**	**$ 2,227,500**	**0.16%**

The amortized cost, fair value, and annual weighted average interest rates of U.S. Government securities at September 30, 2010, by contractual maturity date, were as follows:

(Dollars in thousands)	Amortized Cost	Fair Value	Weighted Average Interest Rate
Due within one year	$ 239,500	$ 239,500	0.12%
Due after one year through five years	3,311,700	3,478,300	0.07%
Due after five years through ten years	-	-	-
Total	**$ 3,551,200**	**$ 3,717,800**	**0.05%**

Although sales of investments are rare, Ginnie Mae liquidated one of its U.S. Government securities within three months of maturity. The par value of the security sold was $1.0 billion and the realized gain on the sale was $24.0 million. These funds were used to repurchase mortgage loans held for investment from defaulted issuer MBS pools. See note on mortgage loans HFI regarding loan repurchases.

Note C: Mortgage Loans Held for Investment, Net

Ginnie Mae acquires mortgage loans from defaulted issuers' portfolios to effectively manage the portfolio. Ginnie Mae owns single family mortgage loans, which are secured by four or fewer residential dwelling units, multifamily mortgage loans, which are secured by five or more residential dwelling units and manufactured housing loans which fall under FHA's Title I program. Ginnie Mae classifies these loans as held for investment and records these net of allowance at the net realizable value.

During fiscal year 2011, following the guidelines outlined in the Ginnie Mae MBS Guide, a large number of loans were repurchased out of pools due to delinquencies of greater than 120 days (see Note A). Ginnie Mae also acquires mortgages ineligible to remain in pools. In addition, Ginnie Mae bought loans out of pools in order to complete modifications in accordance with FHA guidelines. During fiscal year 2011, Ginnie Mae purchased $2.2 billion in mortgages loans out of pools, primarily in the single family defaulted portfolio and categorized these mortgage loans as HFI.

Mortgage loans HFI, net as of September 30, 2011 and 2010 were as follows:

	September 30	
(Dollars in thousands)	**2011**	**2010**
Single Family Mortgages	$ 6,350,300	$ 4,496,300
Single Family Mortgages Allowance for Loss	-	(53,000)
Single Family Mortgages HFI, net	**$ 6,350,300**	**$ 4,443,300**

	September 30	
(Dollars in thousands)	**2011**	**2010**
Multifamily Mortgages	$ -	$ -
Multifamily Mortgages Allowance for Loss	-	-
Multifamily Mortgages HFI, net	**$ -**	**$ -**

	September 30	
(Dollars in thousands)	**2011**	**2010**
Manufactured Housing Mortgages	$ -	$ 3,000
Manufactured Housing Mortgages Allowance for Loss	-	(3,000)
Manufactured Housing Mortgages HFI, net	**$ -**	**$ -**

	September 30	
(Dollars in thousands)	**2011**	**2010**
Total Mortgage Loans HFI	$ 6,350,300	$ 4,499,300
Total Mortgage Loans HFI Allowance for Loss	-	(56,000)
Total Mortgage Loans HFI, net	**$ 6,350,300**	**$ 4,443,300**

As discussed in Note A, Ginnie Mae assesses the collectability of mortgage loans HFI bought out of the pools of defaulted portfolios. In fiscal year 2010, Ginnie Mae did not have the ability to assess individual mortgage loans HFI and instead evaluated homogeneous loans for collectability. As such, Ginnie Mae did not consider any loans to be credit impaired in fiscal year 2010 and management did not record a loss on credit impairment on mortgage loans HFI. However, after assessing the quality of the mortgage loans in the portfolio, management determined the net recoverable value of loans was less than the gross value of mortgage loans HFI. Thus, an allowance for loan loss of $56.0 million was recorded as of fiscal year 2010.

In fiscal year 2011, Ginnie Mae developed a module within the Policy and Financial Analysis Model (PFAM) that allowed management to evaluate mortgage loans HFI on an individual basis. As of fiscal year 2011, the concerns noted in fiscal year 2010 had been resolved and an allowance for loss on mortgage loans HFI was not recorded. In fiscal year 2011, after evaluating the mortgage loans HFI on a loan by loan basis, Ginnie Mae recorded a loss on credit impairment on mortgage loans HFI of $178.7 million related to uninsured and VA-insured mortgage loans; this was net of the $56.0 million previously recorded allowance for loss that was recaptured.

The net balance of credit impaired loans was approximately, $457.6 million as of September 30, 2011.

As discussed in Note A, Ginnie Mae records accrued interest on mortgage loans HFI for interest which Ginnie Mae determines that the ultimate collectability is probable. For non-VA insured loans, Ginnie Mae recognizes interest income on an accrual basis at the debenture rate for the number of months allowed under the insuring agency's timeline. After the allowed timeline, Ginnie Mae considers these loans to be non-performing as the collection of interest is not reasonably assured, and places these loans on non-accrual status. Thus, it is important to note that non-VA insured mortgage loans HFI that are greater than 90 days delinquent continue to accrue interest during the timeline for which the insurer will reimburse Ginnie Mae. Ginnie Mae has assessed the collectability of VA and uninsured loans; these loans are non-performing and hence, are placed on nonaccrual status. In fiscal year 2011, Ginnie Mae recorded $42.3 million in interest income on mortgage loans HFI.

Note D: Advances against Defaulted Mortgage-Backed Security Pools, Net

Under its MBS guaranty, Ginnie Mae advanced $998.3 million in fiscal year 2011 and $2.3 billion in fiscal year 2010 against defaulted MBS pools to ensure timely pass-through payments. Recoveries of advances, either from late payment remittances or through insurance or guaranty proceeds, were $1.2 billion in fiscal year 2011 and $1.4 billion in fiscal year 2010. There were $0.1 million advances written off in fiscal year 2011 and $0.4 million fiscal year 2010.

	September 30	
(Dollars in thousands)	2011	2010
Advances against defaulted MBS pools	$ 873,700	$ 1,054,300
Allowance for uncollectible advances	(220,500)	(212,200)
Advances against defaulted MBS pools, net	**$ 653,200**	**$ 842,100**

Receivables for properties for which foreclosure is complete and that have been conveyed to the insuring agency are reported in the advance category. As of the fiscal year ended September 30, 2011, Ginnie Mae's foreclosure claims receivable balance was $714.5 million of the $873.7 million in gross advances. As of the fiscal year ended September 30, 2010, Ginnie Mae's foreclosure claims receivable balance was $816.8 million of the $1,054.3 million in gross advances. Ginnie Mae has calculated an allowance for uncollectible advances on the gross advances outstanding. Ginnie Mae believes the allowance for uncollectible advances is adequate to cover any potential losses related to advances against defaulted issuer pools or potential losses related to claims receivable.

Note E: Properties Held for Sale, Net

Properties held for sale represent assets that have been completely foreclosed upon, repossessed and Ginnie Mae has received the title of the underlying collateral. Properties held for sale, net consists of the foreclosed and repossessed property received in full satisfaction of a loan, net of a valuation allowance for declines in the fair value of foreclosed properties less estimated costs to sell. During fiscal year 2011, following guidelines outlined in the Ginnie Mae MBS Guide, $148.9 million of loans were repurchased out of pools, primarily for the defaulted single family portfolio and categorized as properties held for sale. Balances and activity for these acquired properties were as follows:

	September 30			
(Dollars in thousands)	2011		2010	
Balance of properties, beginning of year	$	49,200	$	16,600
Additions		148,900		118,700
Dispositions and Losses		(190,700)		(86,100)
Balance of properties, end of year	$	7,400	$	49,200
Valuation Allowance		(4,000)		(6,900)
Properties held for sale, net	**$**	**3,400**	**$**	**42,300**

Note F: Mortgage Servicing Rights

Mortgage servicing rights represent Ginnie Mae's right and obligation to service mortgage loans in mortgage backed securities obtained from defaulted issuers. Ginnie Mae contracts with multiple master sub-servicers to provide the servicing of its mortgage loans. The servicing functions typically performed by Ginnie Mae's master sub-servicer include: collecting and remitting loan payments, responding to borrower inquiries, accounting for principal and interest, holding custodial (impound) funds for payment of property taxes and insurance premiums, counseling delinquent mortgagors, supervising foreclosures and property dispositions, and generally administering the loans. Ginnie Mae receives a weighted average servicing fee of approximately 38 basis points annually on the remaining outstanding principal balances of the loans. The servicing fees are included in and collected from the monthly payments made by the borrowers. Ginnie Mae pays a servicing fee to the master sub-servicers in consideration for servicing the loans.

The following table presents activity for residential first mortgage MSRs:

	September 30	
(Dollars in thousands)	2011	
Balance, October 1, 2010	$	137,700
Additions		-
Changes in Fair Value		(26,800)
Balance, September 30, 2011	**$**	**110,900**

	September 30	
(Dollars in thousands)	2010	
Balance, October 1, 2009	$	-
Additions		137,700
Changes in Fair Value		-
Balance, September 30, 2010	**$**	**137,700**

The net balance of Ginnie Mae's MSRs of $110.9 million is included in a table in Note G: Fair Value Measurements. Ginnie Mae uses a valuation model that calculates the present value of estimated future net servicing income to determine the fair value of MSRs, which factors in prepayment risk. This approach consists of projecting servicing cash flows under multiple interest rate scenarios and discounting these cash flows using risk-adjusted discount rates.

The key economic assumptions used in valuations of MSRs include weighted-average lives and prepayment rates of the MSRs. The discount rate is used to discount expected cash flows in order to derive the fair value of the MSRs. The discount rate assumptions reflect the market's required rate of return adjusted for the relative risk of the asset type. Discount rates assumptions are derived from a range of observed discount rate assumptions in the industry to which a risk premium is added in order to account for current credit conditions. These variables can, and generally do, change from period to period as market conditions and projected interest rates change, and could have an adverse impact on the value of the MSRs and could result in a corresponding reduction in servicing income.

Key economic assumptions used in determining the fair value of the Ginnie Mae's MSR are as follows:

(Dollars in thousands)	September 30 2011	September 30 2010
Valuation at period end:		
Fair value (thousands)	$ 110,900	$ 137,700
Weighted- average life (years)	3.97	2.77
Prepayment rates assumptions:		
Rate assumption	20.62%	29.90%
Impact on fair value of a 10% adverse change	(6,245)	(9,000)
Impact on fair value of a 20% adverse change	(11,875)	(16,900)
Discount rate assumptions:		
Rate assumption	12.50%	12.51%
Impact on fair value of a 10% adverse change	(3,740)	(3,600)
Impact on fair value of a 20% adverse change	(7,251)	(7,200)

These sensitivities are hypothetical and should be considered with caution. Changes in fair value based on a 10% or 20% variation in assumptions generally cannot be extrapolated because the relationship of the change in assumptions to the change in fair value may not be linear. Also, the effect of a variation in a particular assumption on the fair value is calculated without changing any other assumption. In reality, changes in one factor may result in changes in another (e.g., increased market interest rates may result in lower prepayments and increased credit losses) that could magnify or counteract the sensitivities. Further, these sensitivities show only the change in the asset balances and do not show any expected change in the fair value of the instruments used to manage the interest rates and prepayment risks associated with these assets. The primary risk of Ginnie Mae's MSRs is interest rate risk and the resulting impact on prepayments. A significant decline in interest rates could lead to higher–than–expected prepayments that could reduce the value of the MSRs.

Ginnie Mae collected $73.0 million and $93.7 million in mortgage servicing fees for the years ended September 30, 2011 and 2010, respectively. This amount is recorded as a recovery in the reserve for loss on MBS program guaranty.

Note G: Fair Value Measurements

Fair value measurement guidance defines fair value, establishes a framework for measuring fair value and expands disclosures around fair value measurements. This guidance applies whenever other accounting pronouncements require or permit assets or liabilities to be measured at fair value.

The guidance establishes a three-level fair value hierarchy that prioritizes the inputs into the valuation techniques used to measure fair value. The fair value hierarchy gives the highest priority, Level 1, to measurements based on unadjusted quoted prices in active markets for identical assets or liabilities. The next highest priority, Level 2, is given to measurements of assets and liabilities based on limited observable inputs or observable inputs for similar assets and liabilities. The lowest priority, Level 3, is given to measurements based on unobservable inputs.

Recurring Changes in Fair Value

The following table presents for each of these hierarchy levels, Ginnie Mae's assets that are measured at fair value on a recurring basis subsequent to initial recognition, including financial instruments for which Ginnie Mae has elected the fair value option:

	September 30, 2011			
(Dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets				
Mortgage Servicing Rights	-	-	110,900	110,900
Total Assets at Fair Value	$ -	$ -	$ 110,900	$ 110,900

	September 30, 2010			
(Dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total**
Assets				
Mortgage Servicing Rights	-	-	137,700	137,700
Total Assets at Fair Value	$ -	$ -	$ 137,700	$ 137,700

Total assets measured at fair value on a recurring basis and classified as Level 3 were $110.9 million or less than 1% of Total Assets, and $137.7 million or less than 1% of Total Assets, on the Balance Sheets as of September 30, 2011 and 2010, respectively.

The following table presents a reconciliation for all assets and liabilities measured at fair value on a recurring basis using significant unobservable inputs (Level 3) for the years ended September 30, 2011 and 2010:

(Dollars in thousands)	MSRs
Assets:	
October 1, 2010	$ 137,700
Net realized losses included in Excess of Revenue over Expenses (1)	(26,800)
September 30, 2011	**$ 110,900**
Unrealized gains (losses) still held	-
Assets:	
October 1, 2009	$ -
Net realized losses included in Excess of Revenue over Expenses (1)	137,700
September 30, 2010	**$ 137,700**
Unrealized gains (losses) still held	-

(1) Net realized/ unrealized gains (losses) included in Excess of Revenue over Expenses represent the periodic fair value changes of the MSR

The table below summarizes gains and losses due to changes in fair value, including both realized and unrealized gains and losses, recorded in excess of revenue over expenses for the fiscal year ended 2011 for Level 3 assets:

(Dollars in thousands)		Total Gains and Losses MSR
Classification of gains and losses (realized/unrealized) included in Excess of Revenue over Expenses for the period:		
	Loss on MSR	26,800
Total		**$ 26,800**

The following is a description of the valuation methodologies used for assets and liabilities measured at fair value on a recurring basis, as well as the basis for classifying these assets and liabilities as Level 1, Level 2 or Level 3. The estimated fair value was calculated using certain facts and assumptions, which vary depending on the specific financial instrument:

Mortgage Servicing Rights **–** Ginnie Mae elected fair value option for its MSRs and they are recorded on the Balance Sheets at fair value on a recurring basis. Ginnie Mae measures the fair value of MSRs based on the present value of expected cash flows of the underlying mortgage assets using management's best estimates of certain key assumptions, which include prepayment speeds, forward yield curves, adequate compensation, and discount rates commensurate with the risks involved. Changes in anticipated prepayment speeds, in particular, result in fluctuations in the estimated fair values of the master servicing rights. If actual prepayment experience differs from the anticipated rates used in the model, this may result in a material change in the fair value. MSRs are classified within Level 3 of the valuation hierarchy because significant inputs are unobservable.

Nonrecurring Changes in Fair Value

The following tables display assets measured on the Balance Sheets at fair value on a nonrecurring basis; that is, the instruments are not measured at fair value on an ongoing basis but are subject to fair value adjustments in certain circumstances (for example, when Ginnie Mae evaluates for impairment), and the gains or losses recognized for these assets and liabilities for the years ended September 30, 2011 and 2010, as a result of fair value measurements:

	September 30, 2011			
(Dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total Losses**
Assets:				
Properties held for sale			$ 3,400	-

	September 30, 2010			
(Dollars in thousands)	**Level 1**	**Level 2**	**Level 3**	**Total Losses**
Assets:				
Properties held for sale			$ 42,300	-

The following is a description of the valuation methodologies used for assets and liabilities measured at fair value on a nonrecurring basis, as well as the basis for classifying these assets and liabilities as Level 1, Level 2 or Level 3. The estimated fair value was calculated using certain facts and assumptions, which vary depending on the specific financial instrument. The same valuation methodologies are used to estimate the fair value of financial instruments not carried at fair value but disclosed as part of the fair value of financial instruments:

Properties Held for Sale, net – Properties held for sale, net represents foreclosed property received in full satisfaction of a loan net of a valuation allowance. Properties held for sale is initially recorded on the Balance Sheets at its fair value less its estimated cost to sell. Subsequent to initial measurement, the properties held for sale are reported at the lower of the carrying amount or fair value less estimated cost to sell. The fair value estimate is based on relevant current and historical factors available at the time of valuation. Acquired property is classified within Level 3 of the valuation hierarchy because significant inputs are unobservable.

Fair Value of Financial Instruments

The following table displays the carrying value and estimated fair value of Ginnie Mae's financial instruments as of September 30, 2011and 2010. The fair value of financial instruments disclosed in the table includes commitments to guaranty MBS, which are off-balance sheet financial instruments as described in Note I. The fair values of these commitments are presented as "unrecognized MBS commitment".

	September 30, 2011		September 30, 2010	
(Dollars in thousands)	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial Assets:				
Funds with U.S. Treasury	$ 7,210,300	$ 7,210,300	$ 6,650,500	$ 6,650,500
U.S. Government securities	$ 2,126,800	$ 2,227,500	$ 3,551,200	$ 3,717,800
Mortgages held for investment, net	$ 6,350,300	$ 6,350,300	$ 4,443,300	$ 4,443,300
Advances against defaulted MBS Pools, net	$ 653,200	$ 653,200	$ 842,100	$ 842,100
Short sales claims receivable, net	$ 32,300	$ 32,300	$ -	$ -
Properties held for sale, net	$ 3,400	$ 3,400	$ 42,300	$ 42,300
Mortgage servicing rights	$ 110,900	$ 110,900	$ 137,700	$ 137,700
Financial Liabilities:				
Guaranty liability	$ 2,175,100	$ 2,175,100	$ 1,103,800	$ 1,103,800
Unrecognized financial instruments:				
Unrecognized MBS commitments	$ 213,900	$ 213,900	$ 166,700	$ 166,700

The following are valuation techniques for items not subject to the fair value hierarchy either because they are not measured at fair value other than for the purpose of the above table or because they are only measured at fair value at inception:

Unrecognized MBS Commitment – During the mortgage closing period and prior to granting its guaranty, Ginnie Mae enters into commitments to guaranty MBS. The commitment ends when the securities are issued or the commitment period expires. Ginnie Mae's risk related to outstanding commitments is much less than for the outstanding balance of MBS commitments. Outstanding MBS commitments as of September 30, 2011 and September 30, 2010 were $102.6 billion and $80.0 billion, respectively. If the Outstanding MBS commitments were utilized in FY 2011, Ginnie Mae's corresponding guaranty liability, its obligation to stand ready to perform on these securities, would be approximately $213.9 million as of September 30, 2011 and $166.7 million, respectively; these are shown as unrecognized MBS commitments.

Guaranty Liability – Ginnie Mae initially recognizes a guaranty liability at fair value for its obligation to stand ready to perform on these upon issuance of a guaranty. The fair value of guaranty liabilities is measured based on the unpaid principal balance of the guaranteed MBSs outstanding in the non-defaulted issuer portfolio which results from new issuances of MBSs, scheduled run-offs of MBSs, prepayments and defaults. Subsequently, the guaranty liability is measured by a systematic and rational amortization method.

Ginnie Mae's standing as a federal government corporation whose guaranty carries the full faith and credit of the U.S. Government makes it difficult to determine what the fair value of its financial instruments would be in the private market. Therefore, the fair values presented in the table above do not purport to present the net realizable, liquidation, or market value as a whole. Furthermore, amounts Ginnie Mae ultimately realizes from the disposition of assets or settlement of liabilities may vary significantly from the fair values presented.

Note H: Reserve for Loss on MBS Program Guaranty

Ginnie Mae establishes a reserve for loss through a provision charged to operations when, in management's judgment, losses associated with existing defaulted issuers or new issuer defaults are probable and estimable. In estimating losses, management utilizes a statistically-based model that evaluates numerous factors, including, but not limited to, general and regional economic conditions, mortgage characteristics, and actual and expected future default and loan loss experience. Ginnie Mae's Reserve for Loss on MBS Program Guaranty is made up of the three components:

a. Reserve for currently defaulted issuers' pooled loans - loss contingency that arises from the guaranty obligation that Ginnie Mae has to the MBS holders subsequent to issuer default. Ginnie Mae is obligated to make timely principal and interest payments to investors subsequent to issuer default even if Ginnie Mae is unable to collect payments for the underlying loans from the homeowners or insuring agencies. Accordingly, GNMA records a reserve for the loss contingency that arises from the net present value of cash outflows being in excess of cash inflows as related to the defaulted issuer pooled loans.

b. Reserve for currently defaulted issuers' non-pooled loans – loss contingency related to any non-recoverable foreclosure costs that arise from the Mortgage Loans Held for Investment and Properties Held for Sale. Ginnie Mae records the net present value for the estimated non-recoverable foreclosure costs that arise as part of the guaranty fulfillment for the MBS program.

c. Reserve for probable issuer defaults – loss contingency that arises from the guaranty obligation that Ginnie Mae has to the MBS holders as a result of a probable issuer default. The issuers have the obligation to make timely principal and interest payments to investors, however, in the event whereby the issuer defaults, Ginnie Mae steps in and continues to make the contractual payments to investors. Ginnie Mae estimates the amount of reserve by determining the net present value of cash outflows and inflows for issuers that are determined to be probable defaults. For the issuers who are identified as probable defaults, Ginnie Mae records a contingent liability for the amount of these cash flows in the Reserve.

Management also considers uncertainties related to estimates in the reserve setting process. When losses are confirmed and realized on the defaulted issuers' portfolios, Ginnie Mae records the amounts as charged-off (debit) to the reserve. Ginnie Mae recovers part of its losses through servicing fees on the performing portion of the portfolios which are recorded as a recovery (credit) to the reserve. As Ginnie Mae's defaulted issuer portfolio changes, original estimates are compared with actual results over time and the reserve's adequacy is assessed and adjusted as necessary. Management believes that its reserve is adequate to cover probable and estimable losses on the MBS program guaranty.

Changes in the reserve for the years ended September 30, 2011, and 2010 were as follows:

(Dollars in thousands)	Single Family	Multifamily	Manufactured Housing	Total
Reserve for Loss September 30, 2009	**$ 445,300**	**$ 58,700**	**$ 55,900**	**$ 559,900**
Provision for losses	721,100	1,500	7,400	730,000
Charge-offs	(541,800)	(122,600)	(10,700)	(675,100)
Recoveries	261,500	123,700	4,900	390,100
Reserve for Loss September 30, 2010	**$ 886,100**	**$ 61,300**	**$ 57,500**	**$ 1,004,900**
Provision for losses	(287,400)	(61,300)	(58,300)	(407,000)
Charge-offs	(296,200)	-	(1,300)	(297,500)
Recoveries	91,700		3,700	95,400
Reserve for Loss September 30, 2011	**$ 394,200**	**$ -**	**$ 1,600**	**$ 395,800**

Ginnie Mae incurs losses when FHA, USDA, VA, and PIH insurance and guaranty proceeds do not cover losses that result from issuer defaults.

In fiscal year 2011, Ginnie Mae recaptured a portion of its previous Reserve for Losses on MBS Program Guaranty. The recapture was the result of an assessment of the adequacy of the reserve. In addition, as loans were bought of pools and recognized on the balance sheet, losses for credit impairment and allowances were recorded to depict these assets at the amounts that were collectible.

During fiscal year 2011, Ginnie Mae defaulted one single family issuer with a portfolio of $0.5 million. Ginnie Mae has included this issuer in its calculation of the reserve for loss for existing defaulted issuers. Ginnie Mae believes that the Reserve for Loss on MBS Program Guaranty is adequate to cover probable and estimable guaranty related losses.

Note I: Financial Guarantees and Financial Instruments with Off-Balance Sheet Risk

Ginnie Mae guarantees the timely payment of principal and interest to MBS holders in the event of issuer defaults and, in exchange, receives guaranty fees from the issuers. The guaranty fee is calculated based on the unpaid principal balance of outstanding MBS in the non-defaulted issuer portfolio and is Ginnie Mae's compensation for taking on the risk. The MBS securities are backed by pools of insured or guaranteed FHA, USDA, VA, or PIH mortgage loans. Ginnie Mae recognizes a guaranty asset upon issuance of a guaranty and also recognizes a guaranty obligation for its obligation to stand ready to perform on these guarantees. The guaranty liability recognized on the Balance Sheets is $2,175.1 million and $1,103.8 million as of September 30, 2011 and 2010, respectively. In addition to the guaranty obligation, Ginnie Mae recognizes a reserve for loss on MBS program guaranty for estimable and probable losses in relation to these guarantees (See Note H).

For those guarantees recognized on the Balance Sheets, Ginnie Mae's maximum potential exposure under these guarantees is primarily comprised of the amount of MBS securities outstanding. On September 30, 2011, the amount of securities outstanding, which is guaranteed by Ginnie Mae, was $1.2 trillion, including $8.8 million of Ginnie Mae-guaranteed bonds. However, Ginnie Mae's potential loss is considerably less because of the financial strength of our issuers. Additionally, in the event of default, the underlying mortgages serve as primary collateral, and FHA, USDA, VA, and PIH insurance or guaranty indemnifies Ginnie Mae for most losses. The Ginnie Mae guaranteed security is a pass-through security whereby mortgage principal and interest payments, except for servicing and guaranty fees, are passed through to the security holders monthly. Mortgage prepayments are also passed through to security holders. As a result of the security's structure, Ginnie Mae bears no interest rate or liquidity risk. Ginnie Mae's exposure to credit loss is contingent on the nonperformance of Ginnie Mae issuers. Other than those issuers considered in the reserve for loss on the MBS program, Ginnie Mae does not anticipate nonperformance by the counterparties.

Ginnie Mae is also subject to credit risk for its outstanding commitments to guarantee MBS which are not reflected in its Balance Sheets in the normal course of operations. During the mortgage closing period and prior to granting its guaranty, Ginnie Mae enters into commitments to guarantee MBS. The commitment ends when the securities are issued or the commitment period expires. Ginnie Mae's risk related to guarantee commitments is much less than for the commitment amount authorized, due in part to Ginnie Mae's ability to limit commitment authority granted to individual MBS issuers.

Outstanding MBS and commitments were as follows:

	September 30			
(Dollars in billions)	2011		2010	
Outstanding MBS	$	1,221.7	$	1,046.2
Outstanding MBS Commitments	$	102.6	$	80.0

The Ginnie Mae MBS serves as the underlying collateral for multiclass products, such as Real Estate Mortgage Investment Conduits (REMICs), Callable Trusts, Platinums, and Stripped Mortgage-Backed Securities ("SMBS"), for which Ginnie Mae also guarantees the timely payment of principal and interest. These structured transactions allow the private sector to combine and restructure cash flows from Ginnie Mae MBS into securities that meet unique investor requirements for yield, maturity, and call-option features.

In fiscal year 2011, Ginnie Mae issued a total of $153.0 billion in its multiclass securities program. The estimated outstanding balance of multiclass securities included in the outstanding MBS balance as of September 30, 2011, was $547.5 billion**.** These guaranteed securities do not subject Ginnie Mae to additional credit risk beyond that assumed under the MBS program.

Note J: Concentrations of Credit Risk

Concentrations of credit risk exist when a significant number of counterparties (for example, issuers and borrowers) engage in similar activities or are susceptible to similar changes in economic conditions that could affect their ability to meet contractual obligations. Generally, Ginnie Mae's MBS pools are diversified among issuers and geographic areas. No significant geographic concentrations of credit risk exist; however, to a limited extent, securities are concentrated among issuers. It is important to note that many of Ginnie Mae's largest performing issuers are regulated institutions and as such are subjected to regulation and reviews by other government entities in addition to monitoring by Ginnie Mae.

Concentrations of credit risk are as noted below, as of September 30, 2011:

	Single Family		Multifamily		Manufactured Housing		Home Equity Conversion (HECM/HMBS)	
(Dollars in billions)	Number of Issuers	Remaining Principal Balance	Number of Issuers	Remaining Principal Balance	Number of Issuers	Remaining Principal Balance	Number of Issuers	Remaining Principal Balance
Largest performing issuers	25	$ 1,069.2	17	$ 49.3	1	$ 0.3	8	$ 27.8
Other performing issuers	145	$ 51.9	39	$ 8.8	2	$ -	0	$ -
Defaulted issuers	21	$ 14.9	1	$ -	3	$ -	0	$ -

As of September 30, 2011, Ginnie Mae's single family, multifamily, and manufactured housing defaulted portfolio had remaining principal balances of $14.9 billion, $60.8 thousand, and $1.3 million, respectively**.**

Note K: Commitments and Contingencies

As of September 30, 2011, and as of this report, Ginnie Mae's Office of General Counsel has identified one pending or threatened action or unasserted claim or assessment in which Ginnie Mae's exposure is $1,000,000, individually, or in the aggregate for similar matters. Additionally, Ginnie Mae's Office of General Counsel has determined that there are no pending or threatened actions or unasserted claims or assessments in which Ginnie Mae's potential loss exceeds $3,000,000 in the aggregate for cases not listed individually or as part of similar cases that could be material to the financial statements. In the opinion of Ginnie Mae's management and Office of General Counsel the likelihood of an unfavorable outcome is remote in the case. It is the opinion of Ginnie Mae that the disposition or ultimate resolution of the case will not have a material adverse effect on the financial position of Ginnie Mae. Ginnie Mae's management recognizes the uncertainties that could occur in regard to potential defaulted issuers and other indirect guarantees.

Note L: Related Parties

Ginnie Mae is subject to controls established by government corporation control laws (31 U.S.C. Chapter 91) and management controls by the Secretary of HUD and the Director of the Office of Management and Budget (OMB). These controls could affect Ginnie Mae's financial position or operating results in a manner that differs from those that might have been obtained if Ginnie Mae were autonomous.

Ginnie Mae was authorized to use $12.8 million during fiscal year 2011 for payroll and payroll-related costs only. During fiscal year 2011, Ginnie Mae incurred $11.0 million, net, for Salaries and Expenses including payroll and payroll-related costs. This covered the payroll-related costs to HUD including the contributions to the Civil Service Retirement System (CSRS) and the Federal Employees' Retirement System (FERS). Ginnie Mae has no liability for future payments to employees under the retirement systems. Ginnie Mae does not account for the assets of CSRS or FERS nor does it have actuarial data with respect to accumulated plan benefits or the unfunded pension liability relative to its employees. These amounts are reported by the Office of Personnel Management (OPM) and are allocated to HUD. OPM also accounts for the health and life insurance programs for federal employees and retirees and funds the non-employee portion of these programs' costs.

Cash receipts, disbursements, and investment activities are processed by the U.S. Treasury. Funds with U.S. Treasury represent cash currently available to finance purchase commitments and pay current liabilities. Ginnie Mae has authority to borrow from the U.S. Treasury to finance operations in lieu of appropriations, if necessary.

Note M: Credit Reform

The Federal Credit Reform Act of 1990, which became effective on October 1, 1991, was enacted to more accurately measure the cost of federal credit programs and to place the cost of these credit programs on a basis equivalent with other federal spending. Credit reform focuses on credit programs that operate at a loss by providing for appropriated funding, within budgetary limitations, to subsidize the loss element of the credit program. Negative subsidies, calculated for credit programs operating at a profit, normally result in the return of funds to the U.S. Treasury. OMB specifies the methodology an agency is to follow in accounting for the cash flows of its credit programs.

Ginnie Mae's credit activities have historically operated at a profit. Ginnie Mae has not incurred borrowings or received appropriations to finance its credit operations. As of September 30, 2011, the U.S. Government has an investment of $15.8 billion in Ginnie Mae. Pursuant to the statutory provisions under which Ginnie Mae operates, its net earnings are used to build sound reserves. In the opinion of management and HUD's general counsel, Ginnie Mae is not subject to the Federal Credit Reform Act.

Note N: Subsequent Events

Ginnie Mae management has evaluated subsequent events through November 4, 2011, the date through which the financial statements were made available to be issued.

On October 11, 2011, Ginnie Mae defaulted a single family issuer with a remaining principal balance of $490.5 million. The contingent liability associated with this default has been included in the reserve for loss on MBS program guaranty recorded on the Balance Sheets as of September 30, 2011.

On November 1, 2011, Ginnie Mae defaulted, without extinguishment, a single family issuer with a remaining principal balance of $411.4 million.

During October 2011, Ginnie Mae repurchased approximately $345.3 million of loans out of the defaulted MBS pools. Ginnie Mae management has determined that the repurchase will not have a material adverse effect on the financial position of Ginnie Mae.