V. FY 2005 FINANCIAL STATEMENTS

Balance Sheets

September 30	2005	2004
(Dollars in thousands)		
Assets:		
Funds with U.S. Treasury	$ 3,711,400	$ 3,355,100
U.S. Government securities—Note B	7,921,000	7,539,800
Mortgages held for sale, net—Note C	30,400	37,200
Properties held for sale, net—Note D	7,300	4,500
Accrued interest on U.S. Government securities	49,800	59,200
Accrued fees and other receivables	27,800	24,600
Advances against defaulted Mortgage-Backed Security pools, net—Note E	2,400	1,600
Fixed assets—software, net of accumulated amortization	2,200	4,100
Other assets—Note A	382,300	385,200
Total Assets	$ 12,134,600	$ 11,411,300
Liabilities and Investment of U.S. Government		
Liabilities:		
Reserve for loss on Mortgage-Backed Securities Program—Note F	$ 538,500	$ 518,700
Deferred revenue	76,700	75,100
Deferred liabilities and deposits	1,800	4,900
Accounts payable and accrued liabilities	42,400	39,700
Other liabilities—Note A	382,300	385,200
Total Liabilities	$ 1,041,700	$ 1,023,600
Commitments and Contingencies—Notes G, H, and I		
Investment of U.S. Government	11,092,900	10,387,700
Total Liabilities and Investment of U.S. Government	$ 12,134,600	$ 11,411,300

See accompanying notes to financial statements.

Statements of Revenues and Expenses and Changes in Investment of U.S. Government

For the Years Ended September 30	2005	2004
(Dollars in thousands)		
Revenues:		
Mortgage-Backed Securities Program income	$ 327,500	$ 372,800
Interest income	458,800	442,700
Other income, net	200	–
Total Revenues	$ 786,500	$ 815,500
Expenses:		
Mortgage-Backed Securities Program expenses	$ 58,300	$ 63,300
Administrative expenses	10,600	10,600
Fixed asset amortization	2,400	3,900
Total Expenses	$ 71,300	$ 77,800
Provision for loss on Mortgage-Backed Securities Program - Note F	10,000	–
Excess of Revenues over Expenses	705,200	737,700
Investment of U.S. Government at Beginning of Year	10,387,700	9,650,000
Excess of revenues over expenses	705,200	737,700
Investment of U.S. Government at End of Year	$ 11,092,900	$ 10,387,700

See accompanying notes to financial statements.

Statements of Cash Flows

For the Years Ended September 30	2005	2004
(Dollars in thousands)		
Cash Flows From Operating Activities:		
Interest received	$ 468,200	$ 446,000
Mortgage-Backed Securities Program fees	324,300	374,300
Advances against defaulted Mortgage-Backed Security pools	(1,200)	(6,200)
Mortgage-Backed Securities losses and expenses	(50,600)	(54,600)
Other income received	1,800	(5,500)
Administrative expenses	(10,600)	(10,600)
Purchases of mortgages/properties, net of disposal	6,000	3,900
Net Cash Provided by Operating Activities	$ 737,900	$ 747,300
Cash Flows from Investing Activities:		
Purchase of U.S. Treasury Securities, net	(381,200)	(324,000)
Purchase of software	(400)	–
Net Cash Used by Investing Activities	(381,600)	(324,000)
Net Increase in Cash	356,300	423,300
Funds with U.S. Treasury at Beginning of Year	3,355,100	2,931,800
Funds with U.S. Treasury at End of Year	$ 3,711,400	$ 3,355,100
Net excess of revenues over expenses	$ 705,200	$ 737,700
Adjustments to Reconcile Net Excess of Revenues Over Expenses to Net Cash Provided by Operating Activities:		
Provision for loss on Mortgage-Backed Securities Program	10,000	–
Decrease in accrued interest Federal Investments	9,400	3,300
Increase in advances against defaulted Mortgage-Backed Security pools	(800)	(1,600)
(Decrease) increase in deferred liabilities and deposits	(3,100)	3,300
Increase in accounts payable and accrued liabilities	2,700	6,400
Increase (decrease) in deferred revenue	1,600	(5,500)
Increase (decrease) in Mortgage-Backed Securities Reserve, net of other assets, relating to operating activities	10,600	(200)
Fixed asset amortization	2,400	3,900
Total Adjustments	32,800	9,600
Net Cash Provided by Operating Activities	$ 738,000	$ 747,300

See accompanying notes to financial statements.

Notes to the Financial Statements

September 30, 2005 and 2004

Note A: Organization and Summary of Significant Accounting Policies

The Government National Mortgage Association (Ginnie Mae) was created in 1968 through 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. The purpose of the program 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 mortgage institutions. The guaranty is backed by the full faith and credit of the United States Government. Ginnie Mae requires that the mortgages be insured or guaranteed by the Federal Housing Administration (FHA), the Rural Housing Service (RHS) (formerly Farmer's Home Administration), 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.

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 $3.7 billion in Funds with U.S. Treasury, $2.6 billion is in the Reserve Receipt Account, which is a non-interest-bearing account at the U.S. Treasury. For purposes of the Statements of Cash Flows, Funds with U.S. Treasury are considered cash.

U.S. Government Securities: Ginnie Mae classifies its investments in U.S. Government Securities based on its ability and positive intent to hold them to maturity. Therefore, Ginnie Mae's investment in U.S. Government Securities is recorded at amortized cost. Discounts and premiums are amortized, on a level yield basis, over the life of the related security.

Mortgages Held for Sale: Mortgages held for sale, which are purchased out of MBS pools, are carried at the lower of cost or fair value, with any unrealized losses included in current period earnings. The related allowance for loss is established to reduce the carrying value of mortgages held for sale to their estimated fair value, which is based on the amount Ginnie Mae expects to realize in cash upon sale of the mortgages.

Properties Held for Sale: Foreclosed assets are recorded at the lower of cost or fair value, less estimated costs to sell. The related allowance for loss is established to reduce the property carrying value to fair value, less costs to sell. Property related expenses incurred during the holding period are included in MBS Program expenses.

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 the MBS security holders. Such advances are reported net of an allowance for doubtful recoveries to the extent management believes they will not be recovered. The allowance for doubtful recoveries is estimated based on actual and expected recovery experience, and is adjusted for FHA, VA, and RHS claims that have been filed.

Fixed Assets: Ginnie Mae's fixed assets represent systems (software) that are used to accomplish its mission. Ginnie Mae defers significant software development project costs, and amortizes them over a three- to five-year period beginning with the project's completion.

Reserve for Loss on MBS Program: In the operation of its MBS programs, Ginnie Mae estimates the cost of liquidating its existing portfolio of mortgage servicing rights acquired from defaulted issuers and expected issuer defaults. Reserves are established to the extent management believes issuer defaults are probable and FHA, VA, and RHS insurance or guaranty are insufficient to recoup Ginnie Mae expenditures. The reserves are increased by provisions charged as an expense in the Statements of Revenue and Expenses and changes in Investment of U.S. Government, and reduced by charge-offs, net of recoveries.

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 to match the recognition of related administrative expenses. Losses on assets acquired through liquidation and claims against HUD/FHA and VA are recognized when they occur.

FIN 45: The Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 45 (FIN 45), *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, an interpretation of FASB Statements No. 5, 57, and 107, and Rescission of FASB Interpretation No. 34*, in November 2002. FIN 45 clarifies the requirements of FASB Statement No. 5, *Accounting for Contingencies*, relating to the guarantor's accounting for, and disclosure of, the issuance of certain types of guarantees. FIN 45 requires that upon issuance of a guarantee, the entity (i.e., the guarantor) must recognize a liability for the fair value of the obligation it assumes under that guarantee. The disclosure provisions of FIN 45 are effective for financial statements that end after December 15, 2002. FIN 45's provisions for initial recognition and measurement are to be applied on a prospective basis only to guarantees issued or modified after December 31, 2002. The guarantor's previous accounting for guarantees that were issued before the date of FIN 45's initial application may not be revised or restated to reflect the effect of the recognition and measurement provisions of FIN 45. We have completed an evaluation of our guarantees for disclosures required by FIN 45, and have disclosed an asset and liability of $382.3 million. There is no impact of adopting FIN 45 on the net financial position.

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

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 (reflects inflation compensation). The coupon rates of Ginnie Mae's holdings as of September 30, 2005 range from 0.88 percent to 7.00 percent, and as of September 30, 2004, the range was from 1.72 percent to 7.88 percent.

The amortized cost and fair values as of September 30, 2005 were as follows:

Dollars in Thousands	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury Overnight Certificates	$ 1,340,000	$ –	$ –	$ 1,340,000
U.S. Treasury Notes	1,687,400	23,600	(9,200)	1,701,800
U.S. Treasury Inflation-Indexed Securities	4,893,600	271,000	(6,000)	5,158,600
	$ 7,921,000	**$ 294,600**	**$ (15,200)**	**$ 8,200,400**

The amortized cost and fair values as of September 30, 2004 were as follows:

Dollars in Thousands	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
U.S. Treasury Overnight Certificates	$ 1,293,100	$ –	$ –	$ 1,293,100
U.S. Treasury Notes	1,998,700	99,800	–	2,098,500
U.S. Treasury Inflation-Indexed Securities	4,248,000	314,200	–	4,562,200
	$ 7,539,800	**$ 414,000**	**$ –**	**$ 7,953,800**

The amortized cost, fair value, and annual weighted average interest rates of U.S. Government Securities at September 30, 2005, by contractual maturity date, were as follows:

Dollars in Thousands	Amortized Cost	Fair Value	Weighted Average Interest Ratio
Due within one year	$ 2,029,900	$ 2,040,200	3.70%
Due after one year through five years	1,506,400	1,504,500	3.26%
Due after five years through ten years	4,384,700	4,655,700	1.65%
	$ 7,921,000	**$ 8,200,400**	**2.46%**

The amortized cost, fair value, and annual weighted average interest rates of U.S. Government Securities at September 30, 2004, by contractual maturity date, were as follows:

Dollars in Thousands	Amortized Cost	Fair Value	Weighted Average Interest Ratio
Due within one year	$ 2,102,700	$ 2,118,200	1.50%
Due after one year through five years	1,189,100	1,273,400	2.51%
Due after five years through ten years	4,248,000	4,562,200	1.59%
	$ 7,539,800	**$ 7,953,800**	**1.72%**

Note C: Mortgages Held for Sale, Net

Ginnie Mae acquires certain mortgages from defaulted issuers' portfolios to bring the pools into conformity with MBS program requirements. Ginnie Mae acquires mortgages ineligible to remain in pools when servicing rights are sold. Mortgages held for sale were as follows:

	September 30,	
Dollars in Thousands	2005	2004
Unpaid principal balance	$ 36,000	$ 44,700
Allowance for losses	(5,600)	(7,500)
Mortgages held for sale, net	**$ 30,400**	**$ 37,200**

Note D: Properties Held for Sale, Net

Ginnie Mae acquires residential properties by foreclosure out of the defaulted issuer portfolios in order to comply with MBS program requirements. Balances and activity in properties held for sale were as follows:

	September 30,	
Dollars in Thousands	2005	2004
Cost of properties, beginning of year	$ 7,700	$ 3,900
Additions	7,000	7,700
Dispositions and Losses	(4,300)	(3,900)
Cost of properties, end of year	10,400	7,700
Allowances for losses and costs to sell	(3,100)	(3,200)
Properties held for sale, net	**$ 7,300**	**$ 4,500**

Note E: Advances Against Defaulted Mortgage-Backed Security Pools, Net

Under its MBS guaranty, Ginnie Mae advanced $40.9 million in FY 2005, and $34.4 million in FY 2004 against defaulted MBS pools to ensure timely pass-through payments. Recoveries of advances, either from late payment remittances or through FHA insurance or VA guaranty proceeds were $39.9 million in FY 2005, and $28.2 million in FY 2004. No advances were written off in 2005, compared to $101.6 million written off in 2004.

	September 30,	
Dollars in Thousands	2005	2004
Advances against defaulted pools	$ 10,900	$ 7,400
Allowance for losses	(8,500)	(5,800)
Advances against defaulted pools	**$ 2,400**	**$ 1,600**

Note F: Reserve for Loss on MBS Program

Ginnie Mae establishes a reserve for losses through a provision charged to operations, when, in management's judgment, defaults of issuers of MBS become probable. The reserve for losses is based on an analysis of the MBS portfolio outstanding. 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.

Due to Hurricane Katrina, the pool income stream has been disrupted from destruction of the collateral, displacement of the FHA or VA loan borrowers, and the loss of borrower employment. Ginnie Mae has determined that there are about $6.5 billion of mortgages underlying the Ginnie Mae's MBS guaranteed program in the affected region. Most Ginnie Mae issuers in the affected region are currently able to advance funds when required. Ginnie Mae believes that the financial risk to the reserves to be limited. Ginnie Mae has identified approximately $500 million in MBS portfolios may be at risk of default. Ginnie Mae's past experience has shown that approximately 1% of defaulted portfolios are not covered by FHA insurance. Therefore, Ginnie Mae is adding additional funds to the Reserve for Loss. Ginnie Mae has estimated $5 million to cover the identified potential risk and an additional $5 million to cover unidentified financial risks.

Management also considers uncertainties related to estimations in the reserve setting process. The reserve is relieved as losses are realized from the disposal of the defaulted issuers' portfolios. Ginnie Mae recovers part of its losses through servicing fees on the performing portion of the portfolios and the sale of servicing rights. As Ginnie Mae's defaulted issuer portfolio decreases, original estimates are compared with actual results over time, and the adequacy of the reserve is assessed, and if necessary, the reserve is adjusted. Management believes that its reserve is adequate to cover probable losses from defaults by issuers of Ginnie Mae guaranteed MBS. Changes in the reserve for the years ended September 30, 2005 and 2004 were as follows:

Dollars in Thousands	Single Family	Multifamily	Manufactured Housing	Total
September 30, 2003	$ 218,000	$ 57,400	$ 243,900	$ 519,300
Recoveries	10,000	800	3,300	14,100
Realized Losses	(6,900)	(100)	(7,700)	(14,700)
Provision	–	–	–	–
September 30, 2004	$ 221,100	$ 58,100	$ 239,500	$ 518,700
Recoveries	15,800	600	5,700	22,100
Realized Losses	(8,600)	(100)	(3,600)	(12,300)
Provision	10,000			10,000
September 30, 2005	**$ 238,300**	**$ 58,600**	**$ 241,600**	**538,500**

Ginnie Mae incurs loss when FHA and VA insurance and guarantees do not cover expenses that result from issuer defaults. Such expenses include: (1) unrecoverable losses on individual mortgage defaults because of coverage limitations on mortgage insurance or guarantees; (2) ineligible mortgages included in defaulted Ginnie Mae pools; (3) improper use of proceeds by an issuer; and (4) non-reimbursable administrative expenses and costs incurred to service and liquidate portfolios of defaulted issuers.

During FY 2005, Ginnie Mae defaulted two of its single-family issuers. Ginnie Mae believes that the estimated reserve for loss was more than adequate to cover any non-insured loss sustained for these issuers and from unknown future losses from the occurrence of any normal periodic defaults.

Note G: Financial Instruments with Off-Balance Sheet Risk

Ginnie Mae is subject to credit risk for financial instruments not reflected in its balance sheet in the normal course of operations. These financial instruments include guarantees of MBS and commitments to guaranty MBS. 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 structure of the security, Ginnie Mae bears no interest rate or liquidity risk. Ginnie Mae's exposure to credit loss is contingent on the event of nonperformance by other parties to the financial instruments. Other than those issuers considered in the reserve for loss on the MBS program (see Note F), Ginnie Mae does not anticipate nonperformance by the counter parties.

Ginnie Mae guarantees the timely payment of principal and interest to MBS holders should the issuers fail to do so. The securities are backed by pools of insured or guaranteed FHA, RHS, or VA mortgage loans. On September 30, 2005, the amount of securities outstanding, which are guaranteed by Ginnie Mae, was $412.3 billion, and, in addition, $81.7 million of Ginnie Mae Guaranteed Bonds. However, Ginnie Mae's potential loss is considerably less because the underlying mortgages serve as primary collateral, and the FHA, RHS, and VA insurance or guaranty indemnifies Ginnie Mae for most losses.

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 outstanding securities, due in part, to Ginnie Mae's ability to limit Commitment Authority granted to individual issuers of MBS.

Outstanding MBS securities and commitments were as follows:

	September 30,	
Dollars in Billions	2005	2004
Outstanding MBS Securities	$ 412.3	$ 453.4
Outstanding MBS Commitments	$ 55.2	$ 42.9

Note H: Concentrations of Credit Risk

Concentrations of credit risk exist when a significant number of counter parties (e.g., issuers and borrowers) engage in similar activities, or are susceptible to similar change 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 as noted below, as of September 30, 2005:

	Single Family		Multifamily		Manufactured Housing	
Dollars in Billions	Number of Issuers	Remaining Principal Balance	Number of Issuers	Remaining Principal Balance	Number of Issuers	Remaining Principal Balance
Largest performing issuers	20	$ 347.5	9	$ 23.2	1	$ 0.1
Other performing issuers	134	29.1	62	12.0	3	0.1
Defaulted issuers	8	0.2	2	0.1	8	–

As of September 30, 2005, Ginnie Mae's single family, multifamily, and manufactured housing defaulted portfolio had remaining principal balances of $239.8 million, $34.0 million, and $26.1 million, respectively.

In FY 2005, Ginnie Mae issued a total of $57.1 billion in its multiclass securities program. The estimated outstanding balance of multiclass securities included in the total MBS securities balance in Note G as of September 30, 2005, was $187.6 billion. These guaranteed securities do not subject Ginnie Mae to additional credit risk beyond that assumed under the MBS program.

Note I: Commitments and Contingencies

As of September 30, 2005, Ginnie Mae was named in several legal actions, virtually all of which involved claims under the guaranty program. It is not possible to predict the eventual outcome of the various actions; however, in the opinion of management and counsel, the resolution of these claims will not result in adverse judgments to such an extent they would materially affect the financial position or results of operations of Ginnie Mae.

Note J: 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). Such 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 reimbursed HUD $10.6 million in FY 2005, and $10.6 million in FY 2004, for administrative expenses (office space, etc.) allocated to Ginnie Mae, including payroll and payroll-related costs. Payroll-related costs for which Ginnie Mae reimbursed HUD included matching contributions to the Civil Service Retirement System (CSRS), and the Federal Employees' Retirement System (FERS). Although Ginnie Mae funds a portion of pension benefits under these programs, it has no liability for future payments to employees under these programs and 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 the costs of such programs.

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 K: Fair Value of Financial Instruments

The following table shows the fair value of financial instruments to which Ginnie Mae has a contractual obligation to deliver, or a contractual right to receive cash from another entity as of September 30, 2005 and 2004:

	September 30, 2005		September 30, 2004	
Dollars in Thousands	Cost	Fair Value	Cost	Fair Value
Funds with U.S. Treasury	$ 3,711,400	$ 3,711,400	$ 3,355,100	$ 3,355,100
U.S. Government Securities	7,921,000	8,200,400	7,539,800	7,953,800
Advance against MBS pools	2,400	2,400	1,600	1,600
Other assets	115,300	115,300	125,500	125,500
Unrecognized financial instruments	–	1,056,000	–	1,248,000
Other liabilities	120,900	120,900	119,700	119,700

The fair value of Ginnie Mae's largest asset, U.S. Government Securities, is estimated based on quoted market prices for securities of similar maturity. The fair values of Funds with U.S. Treasury, advances against MBS pools, other assets, and other liabilities are not materially different from their carrying values.

Unrecognized financial instruments comprise the net fair value of the fee Ginnie Mae receives for the guaranty of timely payment of principal and interest. The value was derived by discounting the estimated future net cash flows relating to Ginnie Mae guaranteed MBS outstanding. The assumptions and estimates used in calculating the fair values of unrecognized financial instruments are based on management's evaluation of economic conditions, and therefore, are not subject to precise quantification.

These discounted cash flows consist of estimated future guaranty fees, taking into account estimated prepayments, in excess of: (1) projected losses relating to the MBS program, including projected losses on defaulted pools of MBS; and (2) projected administrative expenses. The discount rate approximates an interest rate for risk-free instruments of a type and duration similar to the Ginnie Mae guaranty. The fair value of Ginnie Mae's guaranty recognizes the present value of future fees, which are not recognized under accounting principles generally accepted in the United States of America, since to do so would record revenue prior to realization. The fair value of unrecognized financial instruments increased from FY 2004 to FY 2005, and is primarily attributable to the impact of interest rate volatility.

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. Accordingly, the amount Ginnie Mae would realize upon sale of its financial instruments could differ, perhaps materially, from the amounts shown above.

Note L: Credit Reform

The primary purpose of the Federal Credit Reform Act of 1990, which became effective on October 1, 1991, is to more accurately measure the cost of Federal credit programs, and to place the cost of such credit programs on a basis equivalent with other Federal spending. Credit reform focuses on those 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, 2005, Ginnie Mae had reserves of $11.1 billion held in the U.S. Treasury. 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 in compliance with OMB implementation requirements for the Federal Credit Reform Act, as applicable to government corporations.

VI. AUDIT REPORT OF GINNIE MAE'S FY 2005 FINANCIAL STATEMENTS

The Office of Inspector General (OIG) of the U.S. Department of Housing and Urban Development is required to conduct an annual audit of Ginnie Mae under the provisions of the Chief Financial Officers Act of 1990 (the CFO Act). To fulfill that responsibility, the OIG conducted the audit for the year ended September 30, 2005. The complete OIG report (2006-FO-0001) is included in the separate management report Ginnie Mae prepared pursuant to the CFO Act which is available upon request fro the Ginnie Mae Office of Finance at (202) 401-2064

audit report

Issue Date: November 7, 2005 Audit Case
Number: 2006-FO-0001

TO: Michael Frenz, Acting President, Government National Mortgage Association, T

Randy W. McGinnis

FROM: Randy W. McGinnis, Director, Financial Audits Division, GAF

SUBJECT: **Audit of the Government National Mortgage Association's (Ginnie Mae) Financial Statements for Fiscal Years 2005 and 2004**

HIGHLIGHTS

What We Audited and Why

In accordance with the Government Corporation Control Act as amended (31 U.S.C. 9105), we audited the Government National Mortgage Association's (Ginnie Mae) Financial Statements. This report presents the results of our audit of Ginnie Mae's principal financial statements for the fiscal years ended September 30, 2005 and 2004. Also provided are assessments of Ginnie Mae's internal controls and compliance with laws, regulations, and provisions of contracts that could have a direct and material effect on its financial statements. Our report includes a copy of Ginnie Mae's principal financial statements for the fiscal years ended September 30, 2005 and 2004. The objective of our audit was to express an opinion on the fair presentation of these financial statements.

What We Found

Ginnie Mae's financial statements are presented fairly, in all material respects, in conformity with the United States generally accepted accounting principles. Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses under standards issued by the American Institute of Certified Public Accountants. However, we noted no matters involving the internal control and its operation that we considered to be material weaknesses. The results of our tests of compliance with certain provisions of laws and regulations disclosed no instances of noncompliance that are required to be reported herein under *Government Auditing Standards* and OMB Bulletin No. 01-02, *Audit Requirements for Federal Financial Statements*, as applicable to government corporations.

What We Recommend

We noted no matters material to the financial statements that require recommendations in this report. However, we noted other matters involving internal control over financial reporting and its operation that we are reporting to the management of Ginnie Mae in a separate letter.

INDEPENDENT AUDITOR'S REPORT

To the President,
Government National Mortgage Association

We have audited the accompanying balance sheets of Ginnie Mae as of September 30, 2005 and 2004 and the related statements of revenues and expenses and changes in investments of U.S. governments and of cash flows for the years then ended. These financial statements are the responsibility of Ginnie Mae management. The objective of our audit was to express an opinion on the fair presentation of the financial statements.

Opinion Statement

In our opinion, based upon our audit, the financial statements referred to above present fairly, in all material respects, the financial position of Ginnie Mae as of September 30, 2005 and 2004, and the results of its operations and the cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States of America.

Internal Control

Our consideration of internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses under standards issued by the American Institute of Certified Public Accountants. Material weaknesses are conditions in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements, in amounts that would be material in relation to the financial statements being audited, may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. However, we noted no matters involving the internal control and its operation that we considered to be material weaknesses as defined above.

We noted other matters involving internal control over financial reporting and its operation that we are reporting to the management of Ginnie Mae in a separate letter.

Compliance With Laws and Regulations

The results of our tests of compliance with certain provisions of laws and regulations disclosed no instances of noncompliance that are required to be reported herein under *Government Auditing Standards* or OMB Bulletin No. 01-02, as applicable to government corporations.

Management's Responsibilities

The *Government Management Reform Act of 1994* (GMRA) requires each federal agency to report annually to Congress on its financial status and any other information needed to fairly present its financial position and results of operations. To meet the GMRA reporting requirements, Ginnie Mae prepares annual financial statements. Ginnie Mae is a wholly owned government corporation within the U.S. Department of Housing and Urban Development (HUD).

Management is responsible for the financial statements, including:

- Preparing the financial statements in conformity with accounting principles generally accepted in the United States of America;

- Establishing and maintaining internal controls over financial reporting, and preparation of the Management's Discussion and Analysis; and
- Complying with laws and regulations.

In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control policies. Because of inherent limitations in internal control, misstatements, due to error or fraud may nevertheless occur and not be detected.

Auditor's Responsibilities

Our responsibility is to express an opinion on the fiscal year 2005 and 2004 financial statements of Ginnie Mae based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America, the standards applicable to audits contained in *Government Auditing Standards* and OMB Bulletin No. 01-02, as applicable to government corporations. Those standards and OMB Bulletin No. 01-02 require that we plan and perform audits to obtain reasonable assurance about whether the financial statements are free of material misstatement.

Our audit was not designed to test the requirements of OMB Bulletin No. 01-02 relating to the *Federal Financial Management Improvement Act of 1996* (FFMIA); they are not considered applicable at the Ginnie Mae level. Our audit was also not designed to test the requirements of the *Federal Credit Reform Act of 1990*, because Statement of Federal Financial Accounting Standards No. 2, *Accounting for Direct Loans and Loan Guarantees*, has not been considered in preparing these financial statements.

An audit includes:

- Examining on a test basis, evidence supporting the amounts and disclosures in the financial statements;
- Assessing the accounting principles used and significant estimates made by management; and
- Evaluating the overall financial statement presentation.

We believe that our audit provides a reasonable basis for our opinion.

Distribution

This report is intended for the information and use of the management of HUD and Ginnie Mae, OMB, and the U.S. Congress, and is not intended to be and should not be used by anyone other than these specific parties.

James A. Heist

James A. Heist
Assistant Inspector General
For Audit

November 7, 2005

Ginnie Mae Employees in FY 2005

Aganad, Angela E.
Anderson, George S.
Anderson, Pershing J.
Beddoe, Karen P.
Bizzell, Leonora D.
Blagburn, Damasque J.
Blaylock, Linda D.
Bryant, Carlotta C.
Buckley, Philip H.
Burch, Justin D.
Carr, Terry M.
Cira, Dan
Correa, Victor M.
Cousin, Janie R.
Cowan, Ernest E.
Coward, Corey C.
Dougherty, Patricia A.
Ebba, Tisa I.
Ellis, David L.
Etheridge, Linda F.
Faunce, Helen E.
Foreman, Barbara A.
Foster, Theodore B.
Freeman, Kirk D.
Frenz, Michael J.
Garcia, Michael C.
Gibson, Monica A.
Griffin, Paulette M.
Hackett, Jeannette
Hawkins, Merlene S.
Holmes, Deborah V.
Hooper, Bryan
Imbraguglio, Paul A.
Jones, Wesley E.
Kahn, Daniel E.
Khandpur, Chitranjan
Korn, Carolyn L.
Kozak, John
Kumi, Thomas
Ledbetter, Stephen L.
Mares, Steven J.
McMaster, Sean K.
McQueen, Maria M.
Milhouse, J. Dion
Moses, Sharolyn D.
Murphy, Debra L.
Murphy, LaShonia M.
Najjum, Michael J.
Owens, Cheryl W.
Pessagno, Keri L.
Ripley, Ingrid
St. Laurent, Paul R. III
Smith, Tamara P.
Sterling, Herbert L.
Stewart, Marcus L.
Sturdivant, Lindsay L.
Suarez, Sonya K.
Thompson, James A.
Usher, Sandra J.
Vargas, Victoria
Vilsack, Carol M.
Waller, LaKevia S.
Washington, Richard J.
Weakland, Thomas R.
Young, Karmen L.

Staff as of September 30, 2005

Ginnie Mae®
U.S. Department of Housing and Urban Development
Washington, DC 20410-9000

December 2005
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