119086

BY THE COMPTROLLER GENERAL

# Report To The Congress

OF THE UNITED STATES

# Review Of The Federal Home Loan Mortgage Corporation's Financial Statements For The Year Ended December 31, 1981

GAO reviewed the report on the audit of the Federal Home Loan Mortgage Corporation's 1981 financial statements and the work of its independent public accountant.

GAO concurs with the opinion of the Corporation's accountant and transmits it to the Congress.

119086

GAO/AFMD-82-92
JULY 30, 1982

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COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON D.C. 20548

B-179312

To the President of the Senate and the
Speaker of the House of Representatives

This report summarizes the results of our review of the Arthur Andersen & Co. (AA & Co.) audit of the Federal Home Loan Mortgage Corporation's financial statements for the year ended December 31, 1981. The Corporation is a Government corporation established by the Congress in 1970 to increase housing availability by strengthening and further developing the secondary market in residential mortgages.

We reviewed the workpapers and audit report of AA & Co., the Corporation's independent certified public accountants, to determine the extent to which we could rely on the Corporation's financial statements. We performed such tests of its workpapers and audit report as we considered necessary to ensure that:

--The Corporation's financial statements were prepared in accordance with generally accepted accounting principles.

--AA & Co.'s audit was made in accordance with generally accepted government auditing standards.

--AA & Co. has established the necessary policies and procedures to comply with other applicable professional standards.

Our review was conducted at the Corporation's headquarters in Washington, D.C.

During our review of AA & Co.'s workpapers and audit report, nothing came to our attention that would indicate that its opinion on the Corporation's 1981 financial statements was inappropriate. We therefore concur with, and transmit to the Congress, AA & Co.'s opinion and the Corporation's 1981 financial statements. (See app. I.)

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We are sending copies of this report to the Director of the Office of Management and Budget; Chairpersons of the House and Senate

Banking Committees, the House and Senate Committees on Appropriations, the Senate Committee on Governmental Affairs, the House Committee on Government Operations; and the Chairman of the Board of Directors, Federal Home Loan Mortgage Corporation.

for Milton J. Socolar
Comptroller General
of the United States

ARTHUR ANDERSEN & CO.

1666 K STREET, N. W.
WASHINGTON, D. C. 20006
(202) 862-3100

To the Board of Directors of Federal Home
Loan Mortgage Corporation:

We have examined the balance sheets of Federal Home Loan Mortgage Corporation (a Federally chartered corporation exempt from income taxes) as of December 31, 1981, and 1980, and the related statements of income and retained earnings and changes in financial position for each of the three years in the period ended December 31, 1981. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of Federal Home Loan Mortgage Corporation as of December 31, 1981, and 1980, and the results of its operations and the changes in its financial position for each of the three years in the period ended December 31, 1981, all in conformity with generally accepted accounting principles applied on a consistent basis.

Arthur Andersen & Co.

February 12, 1982

ARTHUR ANDERSEN & CO.

1666 K STREET, N. W.
WASHINGTON, D. C. 20006
WRITER'S DIRECT DIAL NUMBER
(202) 862-3100

The Board of Directors
Federal Home Loan Mortgage Corporation:

We have examined the financial statements of the Federal Home Loan Mortgage Corporation (Corporation) for the year ended December 31, 1981, and have issued our report thereon dated February 12, 1982. As part of our examination, we made a study and evaluation of the system of internal accounting control of the Corporation to the extent we considered necessary to evaluate the system as required by generally accepted auditing standards. For the purpose of this report, we have classified the significant internal accounting controls in the following cycles:

(1) Treasury

(2) Expenditure

(3) Mortgage

(a) Loan Accounting
(b) Investor Accounting

(4) Financial Reporting

The purpose of our study and evaluation, which included the above listed cycles, was to determine the nature, timing, and extent of the auditing procedures necessary for expressing an opinion on the Corporation's financial statements. Our study and evaluation was more limited than would be necessary to express an opinion on the system of internal accounting control taken as a whole.

The management of the Corporation is responsible for establishing and maintaining a system of internal accounting control. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of control procedures. The objectives of a system are to provide management with reasonable, but not absolute, assurance that assets are safeguarded against loss from unauthorized use or disposition, and that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles.

Because of inherent limitations in any system of internal accounting control, errors or irregularities may nevertheless occur and not be detected. Also, projection of any evaluation of the system to future periods is subject to the risk that procedures may become inadequate because of changes in conditions or that the degree of compliance with the procedures may deteriorate.

Our study and evaluation made for the limited purpose described in the first paragraph would not necessarily disclose all material weaknesses in the system. Accordingly, we do not express an opinion on the system of internal accounting control of the corporation taken as a whole or on any of the categories of internal accounting controls identified in the first paragraph. However, our study and evaluation disclosed no condition that we believe to be a material weakness.

This report is intended solely for the use of management of the Corporation; the General Accounting Office and other associated Federal organizations and should not be used for any other purpose.

Arthur Andersen & Co.

February 12, 1982

ARTHUR ANDERSEN & CO.

1666 K STREET, N. W.
WASHINGTON, D. C. 20006
WRITER'S DIRECT DIAL NUMBER

(202) 862-3100

The Board of Directors
Federal Home Loan Mortgage Corporation:

We have examined the financial statements of the Federal Home Loan Mortgage Corporation (Corporation) as of and for the year ended December 31, 1981, and have issued our report thereon dated February 12, 1982. Our examination was made in accordance with generally accepted auditing standards and the provisions of "Standards for Audit of Governmental Organizations, Programs, Activities and Functions" (Standards), promulgated by the Comptroller General as of February 27, 1981, which pertain to financial and compliance audits and accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In connection with our examination, we have reviewed the provisions of Title III of the Emergency Home Finance Act of 1970, as amended (PL 91-351) to determine compliance with the requirements which would have a material financial statement impact in the event of noncompliance.

In our opinion, the Corporation complied with the requirements of Title III of the Emergency Home Finance Act of 1970, as amended (PL 91-351) which would have a material financial statement impact in the event of noncompliance. As regards the requirements that are not material to the financial statements, nothing came to our attention to indicate noncompliance by the Corporation. However, it should be noted that our examination was not directed primarily toward obtaining knowledge of noncompliance with requirements that are not material to the financial statements.

Arthur Andersen & Co.

February 12, 1982

FEDERAL HOME LOAN MORTGAGE CORPORATION

# Financial Statements

## Balance Sheets

| | December 31, 1981 | 1980 |
|---|---|---|
| | (000 omitted) | |
| **Assets** | | |
| Mortgage loans, at unpaid principal balances (Note 3): | | |
| Insured by Federal Housing Administration (FHA) or guaranteed by Veterans Administration (VA) | $ 1,046,796 | $ 1,089,645 |
| Participation in conventional mortgages | 3,242,142 | 3,216,747 |
| Conventional mortgages | 948,322 | 749,964 |
| | 5,237,260 | 5,056,356 |
| Less—Unamortized mortgage purchase discount | 58,772 | 50,606 |
| —Portfolio valuation allowance (Note 4) | 9,000 | 9,000 |
| Total mortgage loans | 5,169,488 | 4,996,750 |
| Cash and temporary cash investments | 629,132 | 19,332 |
| Accrued interest receivable | 50,258 | 48,313 |
| Accounts receivable and other assets | 215,955 | 176,487 |
| Real estate owned | 17,997 | 8,212 |
| Unamortized mortgage sales discount | 243,292 | 229,300 |
| | $ 6,326,122 | $ 5,478,394 |
| **Liabilities and Stockholders' Equity** | | |
| Notes and bonds payable (Note 5): | | |
| Due within one year | $ 1,943,270 | $ 1,034,560 |
| Due after one year | 3,536,792 | 3,651,937 |
| | 5,480,062 | 4,686,497 |
| Other liabilities: | | |
| Accrued interest | 108,494 | 99,597 |
| Accounts payable and other accrued expenses | 2,553 | 2,168 |
| Principal and interest due to Mortgage Participation Certificate investors | 203,883 | 203,906 |
| | 5,794,992 | 4,992,168 |
| Reserve for uninsured principal losses (Notes 2 and 6) | 81,000 | 65,000 |
| Contingencies (Notes 2 and 7): | | |
| Mortgage Participation and Guaranteed Mortgage Certificates | 19,897,363 | 16,962,234 |
| Less—Underlying mortgage loans sold | 19,897,363 | 16,962,234 |
| | — | — |
| Subordinated borrowings and stockholders' equity: | | |
| Subordinated Capital Debentures (Note 8) | 200,000 | 200,000 |
| Stockholders' equity: | | |
| Common stock, nonvoting, $1,000 par value; no maximum authorization; 100,000 shares issued and outstanding | 100,000 | 100,000 |
| Capital in excess of par value | 100,000 | 100,000 |
| Retained earnings | 50,130 | 21,226 |
| | 250,130 | 221,226 |
| Total subordinated borrowings and stockholders' equity | 450,130 | 421,226 |
| | $ 6,326,122 | $ 5,478,394 |

The accompanying notes are an integral part of these balance sheets.

FEDERAL HOME LOAN MORTGAGE CORPORATION

## Statements of Income and Retained Earnings

| | Year Ended December 31, 1981 | 1980 | 1979 |
|---|---|---|---|
| | | (000 omitted) | |
| Income from total portfolio: | | | |
| Interest and discount on mortgage loans | $560,965 | $438,657 | $324,271 |
| Interest on temporary cash investments | 29,313 | 31,678 | 42,660 |
| Management and guarantee fee | 36,175 | 22,717 | 17,631 |
| | 626,453 | 493,052 | 384,562 |
| Interest and related expenses (Note 5): | | | |
| Long-term debt expense | 412,480 | 336,941 | 266,880 |
| Short-term debt expense | 144,459 | 79,585 | 44,685 |
| | 556,939 | 416,526 | 311,565 |
| Net interest margin on portfolio | 69,514 | 76,526 | 72,997 |
| Provision for uninsured principal losses (Note 6) | 16,413 | 22,758 | 19,724 |
| Administrative expenses | 30,298 | 26,098 | 19,434 |
| Other income, net | (8,101) | (5,916) | (1,771) |
| | 38,610 | 42,940 | 37,387 |
| Net income | 30,904 | 33,586 | 35,610 |
| Retained earnings at the beginning of the period | 21,226 | 37,640 | 27,030 |
| Dividends paid | (2,000) | (50,000) | — |
| Transfer to capital in excess of par value | — | — | (25,000) |
| Retained earnings at the end of the period | $ 50,130 | $ 21,226 | $ 37,640 |

The accompanying notes are an integral part of these statements.

# FEDERAL HOME LOAN MORTGAGE CORPORATION

## Statements of Changes in Financial Position

| | Year Ended December 31, 1981 | 1980 | 1979 |
|---|---|---|---|
| | | (000 omitted) | |
| **Funds Provided:** | | | |
| Net income | $ 30,904 | $ 33,586 | $ 35,610 |
| Charges (credits) to income not affecting funds: | | | |
| Amortization of mortgage purchase discount | (8,794) | (7,891) | (8,103) |
| Amortization of mortgage sales discount | 33,606 | 34,843 | 31,889 |
| Provision for losses | 16,413 | 22,758 | 19,724 |
| Funds provided from operations | 72,129 | 83,296 | 79,120 |
| Mortgage loan principal repayments | 124,960 | 208,548 | 234,631 |
| Proceeds from issuance of notes and bonds, net of debt expense | 399,150 | 1,048,337 | 648,723 |
| Mortgage loans sold: | | | |
| Mortgage Participation Certificates (including $2.3 billion in Guarantor Program volume in 1981) | 3,508,404 | 2,485,373 | 3,747,943 |
| Guaranteed Mortgage Certificates | — | — | 744,000 |
| Increase (decrease) in short-term notes | 756,631 | (78,098) | 591,910 |
| Total funds provided | $4,861,274 | $3,747,456 | $6,046,327 |
| **Funds Applied:** | | | |
| Mortgage loans purchased (including $2.3 billion in Guarantor Program volume in 1981) | $3,722,515 | $3,667,736 | $5,697,854 |
| Dividends paid | 2,000 | 50,000 | — |
| Notes and bonds retired | 388,894 | 215,083 | 326,122 |
| Increase (decrease) in cash and temporary cash investments | 609,800 | (213,923) | (101,596) |
| Other items | 138,065 | 28,560 | 123,947 |
| Total funds applied | $4,861,274 | $3,747,456 | $6,046,327 |

The accompanying notes are an integral part of these statements.

APPENDIX II

# Notes to Financial Statements

## December 31, 1981 and 1980

### 1) Summary of Significant Accounting Policies

The Federal Home Loan Mortgage Corporation (the corporation) is a federally chartered corporation whose capital stock consists solely of nonvoting common stock held by the 12 Federal Home Loan Banks.

*Accounting for Mortgage Loan Sales*

The corporation sells Mortgage Participation Certificates (PCs) and Guaranteed Mortgage Certificates (GMCs), representing undivided interests in conventional mortgage loans. The issued certificates have been accounted for as a sale of assets and the mortgage loans sold are accordingly excluded from the corporation's retained mortgage portfolio. Since the corporation guarantees the timely payment of interest at the PC and GMC certificate rates, the ultimate collection of principal on the PCs and the scheduled collection of principal on the GMCs, they are reflected in the balance sheets as contingent liabilities.

A separate Trust has been established for each GMC issue. The corporation, as Trustee, is primarily responsible for forwarding principal collections and interest to GMC investors and for conducting such other investment transactions prescribed in accordance with the terms of each Indenture of Trust.

*Recognition of Gain (Loss) on Mortgage Loans*

Interest margin, representing the excess of the effective interest income rate to the corporation over that payable to the investor, is recognized as earned over the life of the related mortgage loans and is reported as management and guarantee fee income in the accompanying financial statements.

The corporation recognizes losses (negative interest margin) currently on sales of mortgage loans and on outstanding commitments. The corporation provides currently for uninsured principal losses on mortgage loans, either retained in portfolio or sold under the PC and GMC programs. Uninsured principal losses are charged against the appropriate reserve as incurred.

*Mortgage Purchase and Sales Discount*

Discount on mortgage loans purchased is recorded as income over the life of the related mortgage loans, using the level yield method.

Discount on the sale of PCs is amortized over the life of the related underlying mortgage loans, and discount on the sale of GMCs is amortized over the period to the optional repurchase date, both using the level yield method. Amortization of sales discount is recorded as a reduction of management and guarantee fee income in the accompanying financial statements.

Effective January 1, 1981, the corporation decreased the rate of amortization of mortgage purchase and sales discount based on its revised estimate of the repayment pattern of mortgage loans in its conventional mortgage portfolio. The effect of this change was to increase net income by $6.8 million for the year ended December 31, 1981.

*Commitment Fees*

Commitment fees are recognized as income when the commitments are taken.

*Amortization of Debt Expense*

Debt expense is amortized on a straight line basis over the period during which the related indebtedness is outstanding.

### 2) Mortgage Loan Sales and Related Matters

Holders of PCs receive interest monthly at the certificate rate together with their pro rata share of principal payments received by the corporation. Unpaid balances of the outstanding certificates were approximately $17.9 billion and $14.8 billion at December 31, 1981, and December 31, 1980, respectively. Based on the corporation's experience, management believes that the weighted average life of the conventional mortgage loans purchased by the corporation ranges between nine and ten years. At December 31, 1981, and December 31, 1980, the effective interest income rate to the corporation over that payable to the PC investor was .42 percent and .41 percent, respectively. After giving effect to the amortization of deferred charges, the net interest margin was .11 percent and .04 percent, respectively. The effective interest income rate to the corporation and effective rate payable to the investor have been adjusted to semiannual yield equivalent. Additionally, the effective rate payable to investor has been adjusted for the effect of reinvestment of portfolio collections pending disbursement to PC holders.

Holders of GMCs are paid interest semiannually at the certificate rate and are paid annually their pro rata share of principal collected or the specified minimum annual principal reductions, whichever is greater. Any GMC holder may, at his option, require the corporation to repurchase such certificates on a designated optional repurchase date at the then unpaid principal balance. At December 31, 1981, such optional repurchase dates range from March 15, 1990, to September 15, 2004. At December 31, 1981, and December 31, 1980, outstanding GMCs totaled $2.0 billion and $2.2 billion, respectively, and the effective interest income rate to the corporation over that payable to the GMC investor was .37 percent at both dates. After giving effect to the amortization of deferred charges, the net interest margin was .23 percent and .21 percent, respectively. The effective interest income rate to the corporation has been adjusted to semiannual yield equivalent. Additionally, the effective rate payable to investor has been adjusted for the effect of reinvestment of portfolio collections held in Trust pending disbursement to GMC holders.

The maximum contingent liability of $19.9 billion and $17.0 billion at December 31, 1981, and December 31, 1980, respectively, plus interest, is offset by a like amount of interest bearing mortgage loans underlying the PCs and GMCs, including principal collections held in the GMC Trusts of $39 million at December 31, 1981, and $84 million at December 31, 1980. In management's opinion, the $81 million reserve for uninsured principal losses is adequate to absorb any losses anticipated at December 31, 1981.

### 3) Mortgage Loans

As of December 31, 1981, and December 31, 1980, the effective net yields on retained mortgage loans, adjusted to semiannual yield equivalent and adjusted for the effect of discount amortizations, less servicing fees, were as follows.

| | December 31, 1981 | December 31, 1980 |
|---|---|---|
| FHA/VA mortgages | 7.93% | 8.02% |
| Participation in conventional mortgages | 11.48% | 11.62% |
| Conventional mortgages | 12.47% | 12.11% |
| Total effective income | 10.95% | 10.92% |

### 4) Portfolio Valuation Allowance

An analysis of the portfolio valuation allowance for the year ended December 31, 1981, and December 31, 1980, follows.

| | December 31, 1981 | December 31, 1980 |
|---|---|---|
| | (000 omitted) | |
| Balance, beginning of period | $9,000 | $9,000 |
| Provision charged to current earnings | 35 | 7,400 |
| Loss on sales of mortgage loans | (35) | (7,400) |
| Balance, end of period | $9,000 | $9,000 |

### 5) Notes and Bonds Payable

A summary of notes and bonds payable is as follows.

| | Maturity | December 31, 1981 Effective Interest Rate | December 31, 1981 Balance (000 omitted) | December 31, 1980 Effective Interest Rate | December 31, 1980 Balance (000 omitted) |
|---|---|---|---|---|---|
| **Due within one year:** | | | | | |
| Discount notes | | 11.94% | $ 982,275 | — % | $ — |
| Mortgage securities sold under agreements to repurchase | | 13.07 | 410,000 | 17.94 | 516,000 |
| Advances from Federal Home Loan Bank (pass-through of short-term discount notes) | | 15.53 | 58,300 | 12.61 | 103,950 |
| Notes payable to GMC Trusts | | — | — | 17.88 | 48,166 |
| Current portion of long-term debt | | 10.67 | 492,695 | 8.68 | 366,444 |
| Total due within one year | | 11.96 | 1,943,270 | 14.12 | 1,034,560 |
| **Due after one year:** | | | | | |
| Bond payable to bank | 1986 | 7.75 | 13,906 | 7.75 | 15,026 |
| Notes to Federal Home Loan Bank (pass-through of Consolidated Federal Home Loan Bank Obligations) | 1982 | — | — | 10.68 | 490,000 |
| | 1983 | 11.91 | 600,000 | 11.91 | 600,000 |
| | 1984 | 10.41 | 500,000 | 9.54 | 400,000 |
| | 1985 | 8.32 | 640,000 | 8.32 | 640,000 |
| | 1986 | 9.93 | 250,000 | 9.93 | 250,000 |
| | 1987 | 11.13 | 200,000 | 11.13 | 200,000 |
| | 1983/1993 | 7.41 | 400,000 | 7.41 | 400,000 |
| | 1987/1997 | 7.91 | 300,000 | 7.91 | 300,000 |
| | | | 2,890,000 | | 3,280,000 |
| Mortgage-Backed Bonds | 1985 | 5.30 | 3,461 | 5.30 | 3,461 |
| | 1983/1995 | 8.68 | 84,025 | 8.68 | 91,025 |
| | 1984/1996 | 7.81 | 95,400 | 7.81 | 112,425 |
| | 1982/1997 | 7.25 | 150,000 | 7.25 | 150,000 |
| | | | 332,886 | | 356,911 |
| Debentures | 1984 | 16.53 | 300,000 | — | — |
| Total due after one year | | 10.00 | 3,536,792 | 9.43 | 3,651,937 |
| **Notes and Bonds Payable** | | 10.70 | $5,480,062 | 10.47 | $4,686,497 |

Note: The effective interest rates above are on a semiannual basis.

Scheduled principal payments for all notes and bonds payable for each of the next five years are as follows:

| | (000 omitted) |
|---|---|
| 1982 | $1,943,270 |
| 1983 | $ 608,227 |
| 1984 | $ 813,717 |
| 1985 | $ 659,369 |
| 1986 | $ 274,455 |

*Discount Notes*
The discount notes are unsecured general obligations of the corporation. They are offered on a discounted basis and have maturities of one year or less.

At December 31, 1981, the corporation had established with various commercial banks lines of credit aggregating $518 million. For issues prior to March 23, 1982 these lines of credit are maintained so that the total face amount of outstanding Discount Notes does not exceed two times the aggregate unused commercial bank lines of credit. For issues on or after March 23, 1982 this coverage will be reduced to three times the aggregate unused lines.

*Mortgage Securities Sold Under Agreements to Repurchase*
Repurchase agreement programs have maturities ranging up to one year. The agreements outstanding at December 31, 1981 provide for the sale and repurchase of $484 million of PCs issued by the corporation. The agreements are accounted for as financing transactions and, accordingly, such mortgages are included in the corporation's retained mortgage portfolio on the accompanying balance sheets.

*Notes Payable to GMC Trusts*
The notes payable to GMC Trusts are collateralized by FHA/VA mortgages included in the corporation's retained mortgage portfolio.

*Bond Payable to Bank*
The bond payable to bank is collateralized by a like amount of FHA/VA mortgages and calls for specific annual principal repayments ranging from $1,120,000 to $1,408,000 over the remaining life of the bond, with the balance due at maturity.

*Notes to Federal Home Loan Bank*
The Federal Home Loan Banks are required to maintain certain assets equal to their outstanding consolidated obligations. With respect to the $300 million of these notes to a Federal Home Loan Bank maturing in 1982, $600 million maturing in 1983, $200 million maturing in 1984, $400 million maturing in 1985, $250 million maturing in 1986, and $200 million maturing in 1987, the corporation may be required to pledge a portion of its mortgages retained in portfolio and/or temporary cash investments to collateralize a portion or all of the $1.950 billion obligation for the periods during which the Federal Home Loan Banks do not meet this aforementioned requirement. The 1983/1993 and 1987/1997 notes are redeemable at the corporation's option commencing 1983 and 1987, respectively, at their face value.

*Mortgage-Backed Bonds*
The 1982/1997, 1983/1995, and 1984/1996 Mortgage-Backed Bonds are redeemable at the corporation's option commencing 1982, 1983, and 1984, respectively, at their face value. On the 1983/1995 and 1984/1996 bonds, a sinking fund provides for annual retirements of $7.0 million and $7.5 million of the principal amount of bonds, respectively, which commenced in 1976 and 1977. In addition, the corporation has a noncumulative option to increase the sinking fund amounts each year by an amount not to exceed the annual retirement amounts.

All Mortgage-Backed Bonds are guaranteed as to principal and interest by the Government National Mortgage Association (GNMA). Under the provision of a Trust Indenture with GNMA dated October 26, 1970, and supplements thereto, the corporation conveyed mortgages to the Trust as security for the Mortgage-Backed Bonds. As of December 31, 1981, and December 31, 1980, Trust assets of approximately $600 million and $650 million, respectively, constituting primarily principal balances of such mortgages, are restricted for the payment of principal and interest on the Mortgage-Backed Bonds and are included in the accompanying balance sheets. Gains from the repurchase of a portion of the Mortgage-Backed Bonds for the purpose of meeting sinking fund requirements were $5.2 million, $2.9 million and $1.2 million in 1981, 1980 and 1979, respectively.

*Debentures*
The debentures are unsecured general obligations of the corporation. They are issued in the minimum principal amount of $10,000 and are not subject to redemption prior to maturity date.

### 6) Reserve for Uninsured Principal Losses

As of January 1, 1981, the corporation prospectively lowered its rate of provision for uninsured principal losses.

This change in accounting estimate increased income for 1981 by $8.4 million. An analysis of the reserve for uninsured principal losses for the year ended December 31, 1981, and December 31, 1980, follows.

| | December 31, 1981 | December 31, 1980 |
|---|---|---|
| | (000 omitted) | |
| Balance, beginning of period | $65,000 | $50,000 |
| Provision reflected in current earnings | 16,413 | 15,358 |
| Uninsured principal losses | (413) | (358) |
| Balance, end of period | $81,000 | $65,000 |

### 7) Commitments

*Commitments to Purchase*
The average effective income rate on commitments to purchase mortgages is determined after deducting servicing fees. Delivery of mortgages under the forward commitment program is at the option of the seller. Delivery is mandatory under all other commitment programs and must occur within 60 days of the contract date.

| | Outstanding Commitments | | | |
|---|---|---|---|---|
| | December 31, 1981 | | December 31, 1980 | |
| | Average Effective Income Rate* | Amount (000 omitted) | Average Effective Income Rate* | Amount (000 omitted) |
| Conventional Mortgages: | | | | |
| Home | 16.93% | $244,117 | 14.85% | $230,047 |
| Multi-family | 17.47 | 3,553 | 14.90 | 21,874 |
| Forward programs | 18.57 | 123,038 | 14.76 | 194,665 |
| Commitments to purchase | | $370,708 | | $446,586 |

*Commitments to Sell*
The corporation's PCs are continuously offered for sale under both mandatory and optional delivery programs. Delivery periods range from seven to 150 days under the mandatory program. Settlements occur a minimum of 270 days from the date of contract where delivery is at the option of the corporation.

| | Outstanding Commitments | | | |
|---|---|---|---|---|
| | December 31, 1981 | | December 31, 1980 | |
| | Average Effective Rate Payable To Investor* | Amount | Average Effective Rate Payable To Investor* | Amount |
| | | (000 omitted) | | (000 omitted) |
| Mandatory | 16.52% | $ 65,000 | 14.65% | $142,100 |
| Optional | 18.10 | 117,650 | 14.39 | 181,800 |
| Commitments to sell | | $182,650 | | $323,900 |

*Commitments—Guarantor Program*

Under this program mortgage originators sell mortgages to the corporation at par and in exchange simultaneously purchase PCs equal to the unpaid principal balance of the mortgages sold to the corporation. This program was not in effect prior to 1981.

| | Outstanding Commitments December 31, 1981 | |
|---|---|---|
| | Average Effective Rate* | Amount |
| | | (000 omitted) |
| Commitments to purchase | 9.36% | $3,128,591 |
| Commitments to sell | 8.87% | $3,128,591 |

*The average effective income rate and the average effective rate payable to investor are on a semiannual basis and have been adjusted for discounts and fees. Such rates have been computed based on management's estimate of mortgage loan repayments, which incorporates historical experience, using the level yield method. The effective rate payable to investor has been adjusted for the effect of reinvestment of portfolio collections pending disbursement to PC holders. If actual mortgage loan repayments or reinvestment rates vary from the assumptions, the average effective income rate and the average rate payable to investors will also vary.

## 8) Subordinated Capital Debentures

Subordinated capital debenture issues at December 31, 1981, and December 31, 1980, consisted of:

| | December 31, 1981 | | December 31, 1980 | |
|---|---|---|---|---|
| Maturity | Effective Interest Rate | Balance | Effective Interest Rate | Balance |
| | | (000 omitted) | | (000 omitted) |
| 1987 | 11.50% | $ 50,000 | 11.50% | $ 50,000 |
| 1988 | 9.41 | 150,000 | 9.41 | 150,000 |
| | | $200,000 | | $200,000 |

The debentures are subordinated to all obligations and liabilities of the corporation, including obligations of others that the corporation has guaranteed, whether existing at the date of issuance or thereafter incurred or created. The $50 million debentures which were issued to the Federal Home Loan Banks on June 20, 1980 are also subordinated to the $150 million debentures.

(916612)

22648

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