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BY THE COMPTROLLER GENERAL

Report To The Congress

OF THE UNITED STATES

Reviews Of The Audits Of The Federal Home Loan Mortgage Corporation's Financial Statements For The Years Ended December 31, 1983 And 1982

GAO reviewed the independent certified public accountants' audits of the Federal Home Loan Mortgage Corporation's financial statements for the years ended December 31, 1983 and 1982. GAO found nothing to indicate the opinion of the certified public accountants is inappropriate or cannot be relied on.

In the opinion of the Corporation's certified public accountants, the financial statements present fairly the Corporation's financial position as of December 31, 1983 and 1982, the results of its operations, and the changes in its financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

UNITED STATES GENERAL ACCOUNTING OFFICE

127147

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B-179312

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

This report presents the results of our reviews of Arthur Andersen & Co.'s audits of the balance sheets of the Federal Home Loan Mortgage Corporation as of December 31, 1983 and 1982, and the related statements of income, changes in retained earnings, and changes in financial position for the years then ended. Our reviews were made under provisions of the Federal Home Loan Mortgage Corporation Act (12 U.S.C. 1456(b)), which authorizes us to audit the Corporation's financial transactions and report the results of our audit to the Congress.

Our reviews were conducted in accordance with generally accepted government auditing standards. To avoid unnecessary duplication and expense and make the most efficient use of our available resources, we relied on the work and reports of the Corporation's independent certified public accountants rather than conduct financial audits ourselves. To review the reasonableness of the auditors' work and determine the extent to which we could rely on it, we

--interviewed the Corporation's officials to obtain information about the Corporation's operations, including the maintenance of its financial records and the preparation of its financial statements;

--interviewed the auditors to identify the audit approach used and the methods used to control the quality of audit work;

--obtained information about the qualifications and independence of the auditors;

--reviewed the Corporation's financial statements and the auditors' reports for compliance with the reporting requirements of generally accepted accounting principles and generally accepted government auditing standards; and

--reviewed the auditors' workpapers to determine:

- the nature, timing, and extent of audit work performed;

- whether the audit quality control methods identified by the auditor were actually used;

- whether there was a proper study and evaluation of the Corporation's internal controls; and
- whether the auditors tested transactions for compliance with applicable laws and regulations.

We found that the audits were conducted in accordance with generally accepted government auditing standards.

In the opinion of Arthur Andersen & Co., the Corporation's financial statements present fairly its financial position as of December 31, 1983 and 1982, the results of its operations, and the changes in its financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis. During our reviews, we found nothing to indicate Arthur Andersen & Co.'s opinion on the Corporation's 1983 and 1982 financial statements is inappropriate or that it cannot be relied on. The auditors' work did not disclose any material internal control weaknesses or noncompliance with laws and regulations. The opinion, statement on internal controls, statement on compliance with laws and regulations, and the financial statements are in appendix I.

We are sending copies of this report to the Director of the Office of Management and Budget, the Secretary of the Treasury, and the Corporation's Board of Directors.

for Milton J. Socolar
Comptroller General
of the United States

ARTHUR ANDERSEN & CO.
WASHINGTON, D. C.

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

We have examined the balance sheets of the Federal Home Loan Mortgage Corporation (a federally chartered corporation exempt from income taxes) as of December 31, 1983, and 1982, and the related statements of income, changes in retained earnings and changes in financial position for each of the three years in the period ended December 31, 1983. 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 the Federal Home Loan Mortgage Corporation as of December 31, 1983, and 1982, 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, 1983, all in conformity with generally accepted accounting principles applied on a consistent basis.

Arthur Andersen & Co.

February 15, 1984

ARTHUR ANDERSEN & Co.
WASHINGTON, D. C.

February 15, 1984

To the Board of Directors of
the 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, 1983, and have issued our report thereon dated February 15, 1984. 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 and the standards for financial and compliance audits contained in the U.S. General Accounting Office "Standards for Audit of Governmental Organizations, Programs, Activities and Functions". For the purpose of this report, we have classified the significant internal accounting controls in the following cycles:

- Treasury
- Expenditure
- Mortgage Loan
- Mortgage Investor
- Financial Reporting

The purpose of our study and evaluation, which included all 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 or on any of the categories of controls identified above.

APPENDIX I

Board of Directors
Federal Home Loan Mortgage Corporation

February 15, 1984

The management of the Corporation is responsible for establishing and maintaining a system of internal accounting control. In fulfilling this responsibility, estimates and judgements 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 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.

ARTHUR ANDERSEN & Co.

WASHINGTON, D. C.

February 15, 1984

To the Board of Directors of
the 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, 1983, and have issued our report thereon dated February 15, 1984. 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," 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 (PL 91-351), as amended, 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 (PL 91-351), as amended, which would have a material financial statement impact in the event of noncompliance. With regard to 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.

Federal Home Loan Mortgage Corporation

FINANCIAL STATEMENTS

Balance Sheets	December 31, 1983	December 31, 1982
	(millions of dollars)	
Assets		
Mortgage loans, at unpaid principal balances (including approximately $360.0 million and $250.0 million held for sale at December 31, 1983 and December 31, 1982, respectively) (Notes 1 and 3):		
FHA/VA mortgages	$ 941.5	$ 1,008.7
Mortgages pledged for Collateralized Mortgage Obligations	1,669.6	—
Conventional mortgages	5,021.7	3,724.2
	7,632.8	4,732.9
Less—Unamortized mortgage purchase discount	147.5	53.8
—Portfolio valuation allowance (Note 4)	9.4	9.0
Total mortgage loans	7,475.9	4,670.1
Cash and temporary cash investments	711.9	755.1
Accrued interest receivable	81.6	50.2
Accounts receivable and other assets	399.4	305.4
Real estate owned	95.4	55.6
Unamortized mortgage sales discount	199.8	192.9
	$ 8,964.0	$ 6,029.3
Liabilities and Stockholders' Equity		
Notes and bonds payable, net (Note 5):		
Due within one year	$ 2,437.1	$ 1,595.6
Due after one year	4,345.1	2,925.8
	6,782.2	4,521.4
Other liabilities:		
Accrued interest and other accrued expenses	173.0	95.4
Principal and interest due to Mortgage Participation Certificate investors	952.8	546.7
	7,908.0	5,163.5
Reserve for uninsured principal losses (Note 6)	144.2	104.0
Contingencies (Notes 2 and 7):		
Mortgage Participation and Guaranteed Mortgage Certificates	57,990.1	42,952.4
Less—Underlying mortgage loans sold	57,990.1	42,952.4
	—	—
Subordinated borrowings (Note 8)	490.6	465.8
Stockholders' equity:		
Common stock, non-voting, $1,000 par value; no maximum authorization; 100,000 shares issued and outstanding	100.0	100.0
Capital in excess of par value	100.0	100.0
Retained earnings	221.2	96.0
Total stockholders' equity	421.2	296.0
	$ 8,964.0	$ 6,029.3

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

FINANCIAL STATEMENTS

Statements of Income	1983	1982	1981
	Year Ended December 31, (millions of dollars)		
Income from total portfolio:			
Interest and discount on mortgage loans	$615.1	$542.5	$561.0
Interest on temporary cash investments	118.7	78.4	29.3
Management and guarantee income (Notes 1 and 2)	132.1	77.0	36.2
	865.9	697.9	626.5
Interest and related expenses (Note 5):			
Long-term debt expense	496.0	406.0	412.5
Short-term debt expense	113.4	184.7	144.5
	609.4	590.7	557.0
Net interest margin on portfolio	256.5	107.2	69.5
Provision for mortgage loan losses (Notes 4 and 6)	46.4	26.3	16.4
Administrative expenses	52.5	37.1	30.3
	98.9	63.4	46.7
Other income, net (Note 1)	6.0	16.1	8.1
Income before extraordinary item	163.6	59.9	30.9
Extraordinary item: Loss on early retirement of debt (Note 5)	3.9	—	—
Net income	$159.7	$ 59.9	$ 30.9

Statements of Changes in Retained Earnings	1983	1982	1981
	Year Ended December 31, (millions of dollars)		
Retained earnings at the beginning of the period	$ 96.0	$ 50.1	$ 21.2
Net income	159.7	59.9	30.9
Dividends	34.5	14.0	2.0
Retained earnings at the end of the period	$221.2	$ 96.0	$ 50.1

The accompanying notes are an integral part of these statements.

FINANCIAL STATEMENTS

Statements of Changes in Financial Position	Year Ended December 31, 1983	1982	1981
		(millions of dollars)	
Funds provided:			
Net income before extraordinary item	$ 163.6	$ 59.9	$ 30.9
Charges (credits) to income not affecting funds:			
Amortization of mortgage purchase discount	(7.2)	(8.0)	(8.8)
Amortization of mortgage sales discount	50.2	36.6	33.6
Provision for mortgage loan losses	46.4	26.3	16.4
Funds provided from operations before extraordinary item	253.0	114.8	72.1
Extraordinary item: Loss on early retirement of debt	(3.9)	—	—
Mortgage loan principal repayments	451.7	132.4	125.0
Proceeds from issuance of notes and bonds, net of debt expense	2,278.8	254.8	399.2
Mortgage loans sold:			
Mortgage Participation Certificates:			
Guarantor program	15,538.5	21,900.4	2,305.4
Cash program	4,098.7	2,238.1	1,203.0
Decrease (increase) in cash and temporary cash investments	43.2	(125.9)	(609.8)
Increase (decrease) in short-term notes	663.4	(434.5)	756.6
Other items	232.4	76.3	(138.1)
Total funds provided	$23,555.8	$24,156.4	$4,113.4
Funds applied:			
Mortgage loans purchased:			
Guarantor program	$15,538.5	$21,900.4	$2,305.4
Cash program	7,300.5	1,749.3	1,417.1
Dividends	34.5	14.0	2.0
Notes and bonds retired	682.3	492.7	388.9
Total funds applied	$23,555.8	$24,156.4	$4,113.4

The accompanying notes are an integral part of these statements.

NOTES TO FINANCIAL STATEMENTS

For the Three Years Ended December 31, 1983, 1982 and 1981

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 non-voting 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 sold certificates have been accounted for as a sale of assets and, accordingly, the mortgage loans sold are excluded from the corporation's retained mortgage portfolio. Since the corporation guarantees the timely payment of interest at the PC and GMC certificate rate, 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 serves as Trustee and is primarily responsible for forwarding principal collections and interest to GMC investors and for conducting the 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 effective interest income to the corporation over that payable to the investor, is recognized as income over the life of the related mortgage loans and is reported as "Management and guarantee 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 losses on mortgage loans, either retained in portfolio or sold under the PC and GMC programs. Mortgage loan losses, net of gains, 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 interest 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 interest method. Amortization of sales discount is recorded as a reduction of "Management and guarantee income" in the accompanying financial statements.

Real Estate Owned

Real estate acquired in settlement of loans is recorded at the unpaid principal balance and accrued interest upon foreclosure. Costs of improving real estate owned are capitalized. The corporation recognizes losses currently on sales of real estate owned. These losses, net of gains, are charged against the appropriate reserve as incurred.

Amortization of Debt Expense

Debt expense is amortized over the period during which the related indebtedness is outstanding. Debt expense relating to the zero coupon capital debentures and the Collateralized Mortgage Obligations is amortized using the interest method. All other debt expense is amortized on a straight line basis.

Hedging Transactions

In connection with management's strategy of hedging its position on debt issuances, optional contract settlements, PC pricing, inventory maintenance and retail sales activities, the corporation takes positions in cash market trades, futures contracts, futures options, and over-the-counter options. The gains and losses resulting from these hedging transactions are recognized over the lives of the related hedged items.

Other Income

Other income includes commitment fee income net of commitment fee expense. Nonrefundable commitment fees are recognized as income or expense when the commitments are made. Refundable commitment fees are returned upon loan purchase or recognized at the end of the commitment period if delivery is not made.

Other income also includes a $5.5 million non-recurring gain relating to inter-bank clearing activities in 1982 and a $5.2 million gain from the repurchase of mortgage-backed bonds to meet sinking fund requirements in 1981.

Application of Statement of Financial Accounting Standards No. 65

At December 31, 1983 and December 31, 1982 the corporation held approximately $7,116.0 million and $4,420.0 million, respectively (at cost), in mortgage loans for long-term investment. Transfers of mortgage loans to the long-term investment classification made during 1983 were made at cost (which approximated market value at the date of transfer).

At December 31, 1983 and December 31, 1982 the corporation held approximately $360.0 million and $250.0 million, respectively (at cost), in mortgage loans for sale. In the aggregate, the market value of these loans exceeded their cost for both years.

Proposed Legislation Regarding Federal Income Taxation

Legislation has been proposed that would eliminate the corporation's present exemption from federal income taxes. At present, it is not possible to predict the timing or likelihood of the enactment of such legislation, or the specific terms of any such legislation.

Reclassification of 1982 Balances

Reclassifications have been made to certain 1982 balances as previously reported in order to make them consistent with the presentation of 1983 balances.

2) Mortgage Loan Sales and Related Matters

PCs

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 $56.4 billion and $41.2 billion at December 31, 1983 and December 31, 1982, respectively. Based on the corporation's experience, management believes that the weighted average life of the conventional mortgage loans purchased by the corporation which have 25 or 30 year scheduled maturities is approximately 10 years. At December 31, 1983, December 31, 1982, and December 31, 1981 the effective interest income rate to the corporation over that payable to the PC investor was 0.42 percent, 0.43 percent, and 0.42 percent, respectively. After giving effect to the amortization of deferred charges, the net interest margin was 0.34 percent, 0.32 percent, and 0.15 percent, respectively. The effective interest income rate to the corporation and effective rate payable to the investor have been adjusted to a semiannual yield equivalent. Additionally, the effective rate payable to the PC investors has been adjusted for the effect of reinvestment of portfolio collections pending disbursement to PC holders.

GMCs

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, 1983 such optional repurchase dates range from March 15, 1990 to September 15, 2004. At December 31, 1983 and December 31, 1982 outstanding GMCs totaled $1.6 billion and $1.8 billion, respectively. At December 31, 1983, December 31, 1982 and December 31, 1981 the effective interest income rate to the corporation over that payable to the GMC investors was 0.39 percent, 0.37 percent and 0.37 percent, respectively. After giving effect to the amortization of deferred charges, the net interest margin was 0.25 percent, 0.24 percent and 0.23 percent, respectively. The effective interest income rate to the corporation has been adjusted to a semiannual yield equivalent. Additionally, the effective rate payable to the GMC investors has been adjusted for the effect of reinvestment of portfolio collections held in trust pending disbursement to GMC holders.

Contingencies

The maximum contingent liability of $58.0 billion and $43.0 billion at December 31, 1983 and December 31, 1982, 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 $94.8 million at December 31, 1983 and $36.5 million at December 31, 1982.

3) Mortgage Loans

As of December 31, 1983, 1982 and 1981 the effective net yields on retained mortgage loans, adjusted to a semiannual yield equivalent and adjusted for the effect of discount amortizations, less servicing fees, were as follows:

	December 31,		
	1983	1982	1981
FHA/VA mortgages...	7.76%	7.85%	7.93%
Mortgages pledged for Collateralized Mortgage Obligations	12.84%	—	—
Conventional mortgages...	12.02%	11.55%	11.73%
Total effective income	11.65%	10.72%	10.95%

4) Portfolio Valuation Allowance

An analysis of the portfolio valuation allowance for the years ended December 31, 1983, 1982 and 1981 follows:

	December 31,		
	1983	1982	1981
	(millions of dollars)		
Balance, beginning of period	$9.0	$9.0	$9.0
Provision for mortgage loan losses..	.9	1.7	—
Losses on sales of mortgage loans, net...	(.5)	(1.7)	—
Balance, end of period....	$9.4	$9.0	$9.0

5) Notes and Bonds Payable

	Maturity	December 31, 1983 Effective Interest Rate*	December 31, 1983 Balance (millions of dollars)	December 31, 1982 Effective Interest Rate*	December 31, 1982 Balance (millions of dollars)
Due within one year:					
Discount notes		9.28%	$1,398.4	8.51%	$ 670.8
Mortgage securities sold under agreements to repurchase		9.51	255.0	9.74	320.2
Current portion of long-term debt		12.30	750.1	11.87	608.2
Current portion of Collateralized Mortgage Obligations		10.71	36.3	—	—
			2,439.8		1,599.2
Unamortized discount and fees			(2.7)		(3.6)
Total due within one year		10.27	2,437.1	10.06	1,595.6
Due after one year:					
Bond payable to bank	1986	7.75	11.4	7.75	12.6
Notes to Federal Home Loan Bank	1984	—	—	10.41	500.0
(pass-through of Consolidated Federal	1985	8.32	640.0	8.32	640.0
Home Loan Bank Obligations)	1986	9.93	250.0	9.93	250.0
	1987	11.13	200.0	11.13	200.0
	1983/1993	7.41	400.0	7.41	400.0
	1987/1997	7.91	300.0	7.91	300.0
			1,790.0		2,290.0
Unamortized discount and fees			(1.3)		(2.3)
			1,788.7		2,287.7
Collateralized Mortgage Obligations					
Class A-1	1988	10.48	177.8	—	—
Class A-2	1995	11.16	350.0	—	—
Class A-3	2003/2013	11.80	435.0	—	—
			962.8		—
Unamortized premium and fees			13.9		—
			976.7		—
Class B-1	1988	11.36	137.8	—	—
Class B-2	1996	12.09	239.6	—	—
Class B-3	2003/2013	12.62	297.7	—	—
			675.1		—
Unamortized discount and fees			(18.8)		—
			656.3		—
Mortgage-Backed Bonds	1985	5.42	3.5	5.42	3.5
	1983/1995	8.68	70.0	8.68	77.0
	1984/1996	7.81	90.0	7.81	95.4
	1982/1997	7.25	150.0	7.25	150.0
			313.5		325.9
Debentures	1984	—	—	16.53	300.0
	1990	10.94	300.0	—	—
	1991	11.88	300.0	—	—
			600.0		300.0
Unamortized discount and fees			(1.5)		(.4)
			598.5		299.6
Total due after one year		10.09	4,345.1	9.62	2,925.8
Notes and Bonds Payable		10.15	$6,782.2	9.78	$4,521.4

* The effective interest rates above assume interest payments are made on a semiannual basis and are adjusted for the amortization of discounts or premiums, related hedging gains or losses and debt issuance costs, where applicable.

Scheduled principal payments (at par value) for all notes and bonds payable for each of the next five calendar years are as follows:

	(millions of dollars)
1984	$2,439.8
1985	$ 731.9
1986	$ 363.8
1987	$ 356.5
1988	$ 258.3

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. The discount notes outstanding at December 31, 1983 have no minimum credit line requirements. At December 31, 1983 the corporation had established lines of credit aggregating $.2 billion with various commercial banks.

Mortgage Securities Sold Under Agreements to Repurchase

Repurchase agreement programs have maturities ranging up to one year. The agreements outstanding at December 31, 1983 provide for the sale and repurchase of $274.0 million of PCs issued by the corporation as collateral for the $255.0 million in borrowings. 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.

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 of $1.3 million in 1984 and $1.4 million in 1985, with the balance due at maturity.

Notes to Federal Home Loan Banks

The notes of the Federal Home Loan Banks (Banks) represent a pass-through of the Banks' obligations. The Banks are required to maintain certain assets equal to their outstanding consolidated obligations. In this regard, 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 $1.1 billion of these obligations (which consists of $.2 billion maturing in 1984, $.4 billion maturing in 1985, $.3 billion maturing in 1986, and $.2 billion maturing in 1987) for any periods during which the 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.

Collateralized Mortgage Obligations

The Collateralized Mortgage Obligations (CMOs) are general obligations of the corporation. Each series of CMOs is secured by a single pool of conventional mortgages owned by the corporation and such mortgages are included in the retained portfolio. Mandatory semiannual sinking fund payments are allocated to the various classes of each CMO series in the order of the maturities of the classes. Each of the 1983 CMO issues has three classes. If principal payments are recieved on the mortgages at a rate in excess of the rate indicated in the minimum sinking fund schedule, the corporation will be required to make additional mandatory sinking fund payments. The Class A-3 and Class B-3 bonds are each redeemable at the corporation's option commencing 2003 and at the holders' option in 2008 at the unpaid principal balance, plus accrued interest.

A Trust has been established for each CMO issue. The corporation serves as Trustee and is responsible for forwarding principal and interest payments to CMO holders and for conducting the investment transactions prescribed in accordance with the terms of the Indenture and Declaration of Trust. Principal collections held in the CMO Trusts at December 31, 1983 aggregated $12.3 million.

In February 1984 the corporation issued $525.0 million of CMOs, Series C. This CMO issue has four classes. The conventional mortgage collateralization and minimum sinking fund schedule are similar to those of the 1983 CMO issues. On each semiannual payment date, additional principal payments will be made to the other Series C classes in an amount equal to the interest accrued on the Class C-4 bonds. The unpaid principal balance of the Class C-4 bonds will be increased by the amount of interest accrued but not paid out. Semiannual payments of interest to the Class C-4 bond holders will commence upon payment in full of the other Series C classes. The Class C-4 bonds are redeemable at the option of the corporation commencing 2004 and at the option of the holders in 2004. As of December 31, 1983 the corporation had purchased $409.0 million of the mortgages that were subsequently financed long-term by the issuance of CMOs, Series C. (These mortgages were financed temporarily with short-term debt.) These mortgages were purchased at a discount of $86.8 million. The mortgages and discount are included as "Conventional mortgages" and "Unamortized mortgage purchase discount", respectively, in the accompanying financial statements. At December 31, 1983 the corporation had outstanding commitments to purchase an additional $283.8 million of mortgages related to CMOs, Series C.

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 Government National Mortgage Association (GNMA). Under the provision of a Trust Indenture with GNMA dated October 26, 1970, and

 APPENDIX I

supplements thereto, the corporation conveyed mortgages to the Trust as security for the Mortgage-Backed Bonds. As of December 31, 1983 and December 31, 1982 Trust assets of approximately $537.9 million and $577.8 million, respectively, constituting primarily the 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 $.2 million, $.3 million and $5.2 million for the years ended December 31, 1983, 1982 and 1981, 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.

The corporation incurred an extraordinary loss of $3.9 million in September 1983 on the early retirement of $63.6 million of its debentures. These debentures had an average effective rate of 16.53 percent and were due in October 1984.

6) Reserve for Uninsured Principal Losses

An analysis of the reserve for uninsured principal losses for the years ended December 31, 1983, 1982 and 1981 follows:

	December 31,		
	1983	1982	1981
	(millions of dollars)		
Balance, beginning of period	$104.0	$ 81.0	$65.0
Provision for mortgage loan losses	45.5	24.6	16.4
Uninsured principal losses, net	(5.3)	(1.6)	(.4)
Balance, end of period	$144.2	$104.0	$81.0

7) Commitments

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.

	Outstanding Commitments			
	December 31, 1983		December 31, 1982	
	Basis Point Spread	Amount	Basis Point Spread	Amount
		(millions of dollars)		(millions of dollars)
Mandatory	31.2 bp	$ 2,230.8	40.9 bp	$6,202.4
Optional	31.7	13,761.1	—	—
Commitments—Guarantor program		$15,991.9		$6,202.4

Commitments to Purchase

The average effective income rate on commitments to purchase mortgages is determined after deducting servicing fees. Delivery of mortgages under the optional commitment program is at the option of the seller. Delivery is mandatory under all other commitment programs.

	Outstanding Commitments			
	December 31, 1983		December 31, 1982	
	Average Effective Income Rate*	Amount	Average Effective Income Rate*	Amount
		(millions of dollars)		(millions of dollars)
Mandatory	13.46%	$577.4	13.57%	$1,143.1
CMOs (Note 5)	12.49	283.8	—	—
Optional	14.62	110.7	15.17	203.3
Commitments to purchase		$971.9		$1,346.4

Commitments to Sell

The corporation's PCs are continuously offered for sale under both mandatory and optional delivery programs. Delivery periods range from 7 to 150 days under the mandatory program. Settlements occur a minimum of 140 days and a maximum of 260 days from the date of contract where delivery is at the option of the corporation.

	Outstanding Commitments			
	December 31, 1983		December 31, 1982	
	Average Effective Rate Payable To Investor*	Amount	Average Effective Rate Payable To Investor*	Amount
		(millions of dollars)		(millions of dollars)
Mandatory	13.29%	$324.0	12.09%	$807.4
Optional	14.43	105.9	15.07	116.6
Commitments to sell		$429.9		$924.0

* The average effective income rate and the average effective rate payable to investors 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 interest method. The effective rate payable to investors 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 Borrowings

Subordinated borrowings at December 31, 1983 and December 31, 1982 consisted of:

	December 31, 1983		December 31, 1982	
Maturity	Effective Interest Rate*	Balance	Effective Interest Rate*	Balance
		(millions of dollars)		(millions of dollars)
Capital Debentures				
1987	11.50%	$ 50.0	11.50%	$ 50.0
1988	9.41	150.0	9.41	150.0
1989	12.69	100.0	12.69	100.0
		300.0		300.0
Unamortized discount and fees		(3.1)		(3.7)
		296.9		296.3
Zero Coupon Capital Debentures				
1992		600.0		600.0
Unamortized discount and fees		(406.3)		(430.5)
	13.79	193.7	13.79	169.5
Total subordinated borrowings		$490.6		$465.8

*The effective interest rates above assume interest payments are made on a semiannual basis and are adjusted for the amortization of discounts or premiums, related hedging gains and losses and debt issuance costs, where applicable.

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 zero coupon capital debentures rank equally with the 9.41 percent and the 12.69 percent capital debentures and all are senior in right of payment to the 11.50 percent capital debentures.

9) Pension Plan

The corporation has a defined-benefit pension plan covering substantially all of its employees. The corporation makes periodic contributions to the plan equal to the amounts accrued for pension expense.

The weighted average assumed rate of return used to determine the actuarial present value of accumulated plan benefits was eight percent for both 1983 and 1982. A comparison of accumulated plan benefits and plan net assets for the corporation's pension plan appears to the right.

	January 1,	
	1983	1982
	(millions of dollars)	
Actuarial present value of accumulated plan benefits:		
Vested	$2.9	$2.2
Non-vested	.8	.6
	$3.7	$2.8
Net assets available for benefits	$7.2	$5.4

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