



December 23, 2009

Accounting Group - Interpretations
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

To Whom It May Concern:

In June 2009, the Financial Accounting Standards Board (FASB) issued Statement of Accounting Standards No. 166, *Accounting for Transfers of Financial Assets* (FAS 166), and Statement of Accounting Standards No. 167, *Amendments to FASB Interpretation No. 46(R)* (FAS 167). The Mortgage Bankers Association¹ (MBA) has been working with a task force of its members on various implementation issues relating to FAS 166 and FAS 167. A significant issue that is pervasive and impacts most of our members relates to the treatment under FAS 167 of securities guaranteed by the Government National Mortgage Association (Ginnie Mae).

MBA understands that the Securities and Exchange Commission (SEC) prefers that a registrant and its outside auditor bring such issues to the SEC on a pre-clearance basis. However, since there are approximately 400 approved Ginnie Mae issuers, we believe it is more expeditious for MBA to raise these industry-wide issues with the SEC on behalf of all of its members. We are not aware of any prior SEC staff positions related to this issue. This issue is time sensitive as many of our members are required to adopt FAS 167 on January 1, 2010. MBA notes that as of September 30, 2009, the amount of securities outstanding that are guaranteed by Ginnie Mae was over \$800 billion. This issue could have a significant impact on the balance sheets and capital requirements of banks and other issuers if the issuer/servicer were deemed to be the primary beneficiary of a variable interest entity (VIE). MBA has summarized below the Ginnie Mae mortgage-backed securities (MBS) program and accounting analysis of such program under FAS 167. MBA shared a draft of this letter with the Federal

¹ The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,400 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

Housing Administration (FHA), Ginnie Mae, and large accounting firms for comment, but not concurrence. MBA's members took the comments received into consideration in finalizing this letter.

Executive Summary

The issuance of Ginnie Mae MBS has several unique characteristics that require careful analysis under FAS 167. First, unlike substantially all of the securitization market, the issuance of a Ginnie Mae MBS is not completed through a trust vehicle. Second, Ginnie Mae is not the legal issuer. Rather, approved issuers (Issuers/Servicers) pool loans, assign rights to loans to Ginnie Mae through a pool custodian, and issue Ginnie Mae MBS. Third, the Ginnie Mae MBS is the only securitization vehicle specifically designed by a U.S. governmental organization. Finally, the interconnected involvement of multiple governmental organizations in designing and insuring the credit risk of the underlying mortgage loans creates a complex analysis of "power" under FAS 167.

MBA has concluded in the below analysis that the Ginnie Mae issuance is created through an "entity" as defined by FAS 167, because it is substantively equivalent to any asset-backed securitization. Further, MBA concluded that these entities might not be within the scope of FAS 167, because the entities can be viewed as financing entities established by a governmental organization. However, we continued our analysis under FAS 167, because of the alternative view that the entity created through a Ginnie Mae issuance is within the scope of FAS 167.

Assuming a Ginnie Mae issuance is created through an entity, MBA concluded that the entity is a variable interest entity under FAS 167, because there is no equity investment at risk. The MBS issued would be reported as debt on the entity's balance sheet. Therefore, we considered the design and variable interests of the entity to determine which party, if any, should consolidate. After considering all of the facts and circumstances, MBA believes that although the Issuer/Servicer has certain elements of power, the collective U.S. governmental organizations have power characteristics that have the most significant impact on the entity's economic performance, including the underlying design of the entity and the creation/periodic amendments of the Ginnie Mae and Insurer guidelines that must be followed in issuing MBS and servicing the underlying loans.

The following provides MBA's more detailed analyses and conclusions.

Summary of Ginnie Mae Transactions²

Background

In late 1970, the Ginnie Mae pass-through program was established, which provided a means for investors to invest in mortgages without the cumbersome process of acquiring individual loans. Ginnie Mae is a wholly-owned corporate instrumentality of the United States within the Department of Housing and Urban Development (HUD). Ginnie Mae is authorized by section 306(g) of the National Housing Act to guarantee the timely payment of principal and interest on securities that are based on and backed by pools composed of mortgages that are federally insured or guaranteed loans – mainly loans insured by the Federal Housing Administration (FHA) or guaranteed by the Department of Veterans Affairs (VA). Other guarantors or issuers of loans eligible as collateral for Ginnie Mae MBS include the Department of Agriculture's Rural Housing Service (RHS) and HUD's Office of Public and Indian Housing (PIH). The Ginnie Mae guarantee of MBS is backed by the full faith and credit of the United States.

Ginnie Mae has powers granted by its federal charter that makes its guaranteed mortgage securitization structures different and unique as compared to other issuers or securitizers. There is no trust holding the mortgages backing Ginnie Mae pass-through certificates. Rather, the Ginnie Mae MBS program calls for the establishment of custodial pools, whereby the Issuer/Servicer conveys to Ginnie Mae all the rights, title and interest to the mortgages in the pool. Ginnie Mae has the ability to legally isolate pools of mortgage loans without the use of a trust or other legal entity and to permit the issuance of pools of mortgage loans as securities through the U.S. Federal Reserve's book-entry system. The holder of the Ginnie Mae MBS owns undivided interests in the pool of mortgages. The scheduled cash flows from the pool of mortgages are passed through to the Ginnie Mae MBS holder, less the servicing and guarantee fees, regardless of whether such amounts are timely collected from the borrowers.

Ginnie Mae is not in the business of making or purchasing mortgage loans, nor does it buy, sell or issue securities. However, mortgages are assigned to Ginnie Mae under the program. Issuers, which are private lending institutions approved by Ginnie Mae, originate eligible government loans, pool them into securities, and issue Ginnie Mae MBS.

Ginnie Mae MBS represent undivided interests in pools of mortgages and are traded as securities in the secondary market. Ginnie Mae MBS are commonly referred to as "pass-through" certificates because the principal and interest of the underlying loans are "passed through" to investors. The interest rate of the

² See <http://www.ginniemae.gov/guide/guidtoc.asp?Section=Issuers> for all relevant documents of a Ginnie Mae issuance.

security is lower than the interest rate of the underlying loans to allow for payment of servicing and guarantee fees.

Ginnie Mae MBS are created when eligible mortgage loans (those insured or guaranteed by FHA, VA, RHS or PIH) are pooled by approved issuers and securitized in accordance with guidelines issued by Ginnie Mae. Ginnie Mae MBS investors receive a pro rata share of the resulting cash flows (net of servicing and guarantee fees). Ginnie Mae itself does not issue any securities, but instead guarantees the Ginnie Mae MBS issued by banks, thrifts and mortgage bankers that participate in Ginnie Mae's programs.

See Appendix I for a diagram of the Ginnie Mae MBS program.

Ginnie Mae guarantees a variety of securities tailored to investors with diverse needs. See Appendix II for a description of Ginnie Mae products, some of which are issued by trusts. This letter relates to Ginnie Mae I MBS and Ginnie Mae II MBS only.

Subject to Ginnie Mae's sole discretion, Ginnie Mae reviews applications from lenders and grants "Issuer" status, provides approved Issuers with commitment authority, approves issuances of securities, and monitors Issuers once they are approved to issue securities.

Refer to Appendix III for a description of the process of issuing Ginnie Mae MBS.

Ginnie Mae Securities

The rate on the Ginnie Mae I MBS securities is generally 50 basis points below the rate on the underlying mortgages. Ginnie Mae II MBS servicing fees can vary since Ginnie Mae II MBS allow a limited range of interest rates on the underlying loans. Of the 50 basis points, 6 basis points go to Ginnie Mae as their premium for the guarantee, and the other 44 basis points go to the Issuer/Servicer to cover the costs of servicing the mortgages. The Ginnie Mae guarantee ensures that the security holder receives the timely payment of principal and interest (at the prescribed security rate), whether or not those funds have been collected by the Issuer/Servicer. If a borrower on the underlying mortgage fails to make a timely payment on a mortgage, the Issuer/Servicer is required to make advances from its own funds to ensure that the security holders receive timely payment. If an Issuer/Servicer fails to ensure that the funds necessary to make timely payment are available or otherwise defaults in the discharge of its responsibilities, Ginnie Mae will make payments to the security holders. Ginnie Mae does not reimburse the Issuer/Servicer for any advances made. However, since all the mortgage loans are insured or guaranteed mortgage loans, including a vast

majority of the servicing advances,³ by the federal government (e.g., FHA or VA⁴), the risk borne by the Issuer/Servicer is very small in relation to the losses absorbed by the underlying insurance or guarantee.

The Issuer/Servicer of the Underlying Mortgages

For the life of the pool, the Issuer/Servicer is responsible for servicing the mortgages, administering the securities, and submitting periodic reports to Ginnie Mae. The Issuer/Servicer must service the pooled mortgages in accordance with FHA, VA, RHS and PIH guidelines, to the extent not inconsistent with Ginnie Mae's requirements and guidelines and to the extent not inconsistent with practices generally accepted in the mortgage lending and servicing industry. The Issuer/Servicer collects the mortgagors' monthly principal, interest and escrow payments and all other payments and recoveries with respect to the pooled mortgages and deposits them into its principal and interest and escrow custodial accounts for the pool.

No Issuer/Servicer or subcontract servicer may, without the written permission of Ginnie Mae, remove a loan from a pool or reduce a balance on a pooled loan for any reason not specifically authorized by the requirements in the applicable Guaranty Agreement or the Ginnie Mae Guidelines. However, Ginnie Mae has a standard servicer buyback option ("Default Call Option") feature as part of the securitization program. If a borrower makes no payment for three consecutive months, the Issuer/Servicer has the option to repurchase the loan from Ginnie Mae at par. It may be advantageous to the Issuer/Servicer to repurchase the delinquent loan out of the pool at par value, since the Issuer/Servicer advances and allowable costs will be reimbursed by the FHA at a "debenture rate" (e.g., the 10-Year Treasury yield) (established by FHA), which is typically lower than the pass-through rate required to be advanced to the Ginnie Mae MBS holders. The economics of the buyout decision are typically based upon the coupon of the Ginnie Mae pool versus the funding cost for the Issuer/ Servicer to buyout a loan. If the Issuer/Servicer's funding cost is lower than the Ginnie Mae MBS coupon for that pool, there is an incentive for the Issuer/Servicer to buy out loans once three consecutive payments are missed in order to stop the obligation to advance interest at the MBS coupon. In the current market, the funding costs for many large Issuer/Servicers are much lower than the average coupon of Ginnie Mae MBS. However, for smaller Issuer/Servicers, the funding costs for buyouts may be significantly higher, resulting in less buy-out incentive. If the delinquent loan

³ FHA guarantees 100 percent of the principal of the loans and a portion of the accrued interest based upon FHA guidelines, which are typically 80 to 100 basis points less than the contractual interest rate of the loan and two-thirds to three-quarters of the foreclosure costs.

⁴ Note that VA only insures a portion (up to 50 percent) of the principal amount, but is in a first-loss position.

is later cured, it may be resold into a new Ginnie Mae MBS pool, which may result in a gain if the interest rate is high relative to the current market.

Buyout activity is also influenced by a threshold on 90+ day delinquency rate imposed by Ginnie Mae. If an Issuer/Servicer fails to maintain delinquency rates on outstanding pools below the applicable threshold levels, Ginnie Mae may impose sanctions on the Issuer/ Servicer, including but not limited to the following:

- Denial of further commitment authority;
- Denial of approval of transfers of other issuer responsibility to the Issuer/Servicer;
- Denial of Issuer/Servicer's request to subcontract service for other issuers;
- Denial of authority to issue additional securities, even though Issuer/Servicer may have commitment authority outstanding;
- Imposition of civil money penalties; and
- Declaration of a default and termination of issuer status.

The threshold for 90+ day delinquencies is 5 percent of the Ginnie Mae servicing portfolio⁵. Therefore, as the 90+ day delinquencies approach the 5 percent threshold, Issuer/Servicers will generally buy out loans in order to avoid sanctions imposed by Ginnie Mae.

Differences Between Ginnie Mae and Fannie Mae/Freddie Mac

Ginnie Mae, Federal National Mortgage Association (Fannie Mae) and Federal Home Loan Mortgage Corporation (Freddie Mac) have similarities in their respective missions to work in the secondary mortgage markets to improve homeownership opportunities for American families. There are, however, significant differences in their structures, business models, and security guarantees, as follows:

- Ginnie Mae is a government corporation within HUD, wholly owned by the U.S. Government. Fannie Mae and Freddie Mac are corporations known as government sponsored enterprises (GSEs) that were chartered by Congress, but owned by private common and preferred stockholders.

⁵ For servicers/issuers with more than 1,000 loans.

However, on September 7, 2008, Fannie Mae and Freddie Mac were put under the conservatorship of the Federal Housing Finance Agency (FHFA) and it remains unclear what effect this will have on their respective structures.

- Fannie Mae and Freddie Mac support the conventional (conforming mortgage loan) mortgage market, Ginnie Mae supports the market for FHA, VA, RHS and PIH loans.
- Fannie Mae and Freddie Mac are able to purchase mortgages to hold in their own portfolios or to issue securities for sale to investors. Ginnie Mae is not in the business of purchasing mortgage loans, nor does it buy, sell or issue securities. Private lending institutions approved by Ginnie Mae issue the Ginnie Mae MBS.
- Ginnie Mae only guarantees securities for federally insured or guaranteed loans (mainly FHA and VA loans). Fannie Mae and Freddie Mac guarantee securities that are backed by mortgages that must meet certain standards. Fannie Mae and Freddie Mac may require private mortgage insurance on certain loans (generally loans with higher origination loan-to-value ratios) that insures a portion of the losses on a loan. Fannie Mae and Freddie Mac also guarantee bonds that are packaged and sold by others, as long as the underlying mortgages meet their standards.
- Although Ginnie Mae, Fannie Mae and Freddie Mac guarantee their MBS for the timely payment of principal and interest, Ginnie Mae MBS are explicitly backed by the full faith and credit of the U.S. Government.
- Fannie Mae and Freddie Mac utilize legal trusts to pool and segregate assets⁶ and they are the Trustee of the trusts, not an independent bank trust department.
- Fannie Mae and Freddie Mac are the named Master Servicer in their respective trusts.
- Fannie Mae and Freddie Mac have the option to repurchase delinquent loans from their respective Trusts. This option, among other things, allows the GSEs to protect themselves from further loss on the guarantee, because removal of the loan from the Trust gives the GSE additional loss

⁶ However, federal charters grant Fannie Mae and Freddie Mac the ability to legally isolate pools of mortgage loans without the use of a trust or legal entity.

mitigation options. Conversely, the Issuer/Servicer has the Default Call Option for a Ginnie Mae issuance.

- Fannie Mae and Freddie Mac have the unilateral right to remove the servicer. Ginnie Mae and the insurers may remove the Issuer/Servicer only for cause.

FAS 167 Analysis for Ginnie Mae MBS

Under FAS 167, the Primary Beneficiary is the party to a VIE that has the power, through voting rights or similar rights, to direct the activities of an entity that most significantly impact the entity's economic performance and either the obligation to absorb the expected losses of the entity or the right to receive the expected returns of the entity. The Primary Beneficiary so identified must consolidate the VIE's assets and liabilities in its balance sheet.

Question 1: Is a Ginnie Mae issuance created through an "entity" as defined by FAS 167?

As mentioned in the background material above, the Ginnie Mae MBS is not set up as a trust like Fannie Mae and Freddie Mac securities. Rather, it is set up by the Issuer/Servicer by sending the mortgage and other collateral documents to a Ginnie Mae approved document custodian. In discussions with staff at Ginnie Mae, it was determined that a legal entity or trust does not exist. However, FAS 167 does not require a conclusion that a legal entity exists; rather, paragraph 3 of FAS 167 defines an entity in relevant part as follows:

For convenience, this Interpretation uses the term *entity* to refer to any **legal structure** used to conduct activities or to hold assets. Some examples of such structures are corporations, partnerships, limited liability companies, grantor trusts, and other trusts. Portions of entities or aggregations of assets within an entity shall not be treated as separate entities for purposes of applying this Interpretation unless the entire entity is a variable interest entity. Some examples are divisions, departments, branches, and pools of assets subject to liabilities that give the creditor no recourse to other assets of the entity. [Emphasis Added]

The term "legal structure" does not have meaning in law. Although it is not clear what the FASB intended, it appears reasonable to conclude that the FASB meant the definition of an "entity" in FAS 167 to be broader than something that meets the narrower definition of a legal entity, and the Ginnie Mae MBS structure certainly is used to conduct activities and to hold assets. The MBA considered paragraph 2A of FAS 167, as follows:

Consideration of Substantive Terms, Transactions, and Arrangements

2A. For purposes of applying this Interpretation, only substantive terms, transactions, and

arrangements, whether contractual or noncontractual, shall be considered. **Any term, transaction, or arrangement that does not have a substantive effect** on (a) an entity's status as a variable interest entity, (b) an enterprise's power over a variable interest entity, or (c) an enterprise's obligation to absorb losses or its right to receive benefits of the entity **shall be disregarded when applying the provisions of this Interpretation**. Judgment, based on consideration of all the facts and circumstances, is needed to distinguish substantive terms, transactions, and arrangements from nonsubstantive terms, transactions, and arrangements. [Emphasis Added]

MBA's View:

MBA believes it would be inappropriate to conclude that a Ginnie Mae pool is not an *entity* when the transaction is substantively equivalent to any asset-backed security trust whether created by a GSE Trust or a private issuer. In fact, as discussed in the background, federal charters also grant the GSEs the ability to isolate pools of mortgage loans without the use of a trust or legal entity, and until recently, Freddie Mac did not use a trust to issue its Participating Interest Certificates MBS. MBA believes this supports its assertion that creation of a legal trust is a non-substantive issue. MBA further believes that a Ginnie Mae MBS is substantively equivalent to any asset-backed security trust whether created by Fannie Mae or Freddie Mac or by a private issuer. Therefore, MBA believes that a Ginnie Mae issuance should be treated as an *entity* as defined by FAS 167.

Other factors in support of a conclusion that a FAS 167 "entity" exists are that for Federal income tax purposes, the Ginnie Mae pool is considered to be a grantor trust and Ginnie Mae uses trusts for certain of their other mortgage-backed securities offerings (e.g., REMICs), and there does not appear to be any substantive difference in design or nature and purpose when compared to the MBS offerings that do not use legal trusts.

If the Ginnie Mae MBS were deemed not to be an entity for purposes of applying FAS 167, MBA has identified several implementation questions in applying the participation interest guidance of FAS 166 that would need to be addressed. In FAS 166, one of the issues relates to paragraph 8B(c), which requires that "participating interest holders have no recourse to the transferor..." Some members believe that this provision may prevent a transfer of a portion of the Ginnie Mae MBS to meet the definition of a participating interest, because of the Issuer/Servicer's obligation to advance unpaid principal and interest on a non-recourse basis.

Alternative View:

MBA considered an alternative view that a Ginnie Mae issuance represents "pools of assets subject to liabilities that give the creditor no recourse to other assets of the entity" as described in paragraph 3. MBA believes that such interpretation would be "form over substance." A Ginnie Mae issuance is much more than a pool of assets. Congress gave Ginnie Mae the right to have issuers

issue tradable securities backed by the government without requiring a legal trust structure. However, the assets are segregated into a custodial account separate from the other assets of the entity. MBA believes that the language in paragraph 2A should be considered by analogy. Paragraph 2A states, “For purposes of applying this Interpretation, only substantive terms, transactions and arrangements, whether contractual or non-contractual, shall be considered.” Although this provision is not specifically in reference to the definition of an “entity,” MBA believes that substance should prevail over form.

MBA also considered the alternative view that the FASB intended for the definition of entity to be narrow and anchored solely in a strict legal definition. This alternative view cites EITF Issue No. 07-1 (Codification reference topic 808-10-15), Accounting for Collaborative Arrangements (EITF 07-1) as an instance where the FASB referenced the use of virtual joint venture that was not an entity. EITF 07-1 provided guidance for these virtual joint ventures rather than applying FIN 46(R). The MBA does not believe EITF 07-1 is on point, because it addresses an instance where no resemblance of an entity exists, which does not allow for the creation of financial statements. Rather, it provides guidance for accounting for the counterparty’s involvement with a contractual operating agreement. A Ginnie Mae MBS issuance, in contrast, has defined assets and liabilities and income and expense that represent a distinct accounting entity for which financial statements can be prepared.

Question 2: Assuming a Ginnie Mae issuance is created through an entity, is the entity within the scope of FAS 167?

Paragraph 4 of FAS 167 provides limited exceptions to applying the standard. Paragraph 4(i) states:

An enterprise shall not consolidate a governmental organization and shall not consolidate a financing entity established by a governmental organization unless the financing entity (1) is not a governmental organization and (2) is used by the business enterprise in a manner similar to a variable interest entity in an effort to circumvent the provisions of this Interpretation.

This scope exception was added in the original revision of FIN 46 in December 2003. The FASB explained this addition in paragraphs D17-D18 of FIN 46(R):

D17. Respondents to the proposed Interpretation commented that governmental organizations should neither consolidate other entities nor be consolidated in accordance with Interpretation 46. However, those respondents believe that, in the absence of a specific scope exception, the introductory sentence in paragraph 4 of Interpretation 46 could be interpreted to require that consolidation. When a private (nongovernmental) enterprise receives financing from, or is otherwise involved with, a governmental organization or financing entity established by a governmental organization, that enterprise may currently be recording a liability for the debt or guarantee as a result of

that involvement. However, the application of Interpretation 46 to such an arrangement (a) would identify the governmental organization as a variable interest entity because of the lack of any equity investment and (b) could identify the private enterprise as the primary beneficiary.

D18. The Board observed that the accounting for and by federal, state, and local governmental organizations in the United States is promulgated by the Federal Accounting Standards Advisory Board (FASAB) and the Governmental Accounting Standards Board (GASB) and not the FASB. The FASAB, the GASB, or some other organization may decide to apply an FASB standard to a governmental organization, but that is not a decision made by the FASB. Because the FASB does not have the authority to establish accounting standards for governmental organizations, it is usually unnecessary for the FASB to state whether a particular standard applies to those organizations. However, the FASB acknowledges that confusion exists as to whether Interpretation 46 should be applied by an enterprise involved with the arrangements described because of the nature of those arrangements. Therefore, the Board decided to exempt an enterprise from consolidating, in accordance with this Interpretation, a governmental organization or financing entity established by a governmental organization. This provision does not apply to a financing entity created by a governmental organization that is used by a nongovernmental enterprise to circumvent this Interpretation if that entity is not itself a governmental organization.

MBA's View:

MBA first observes that Ginnie Mae is a governmental organization. MBA believes that the scope exception is met in substance and should be available to be relied on by Ginnie Mae MBS issuers. Although the Ginnie Mae MBS is *established* by the Issuer, it is only allowed to be created because of Ginnie Mae's charter. That is, the design of the program by a government entity creates the opportunity to establish each of the financing entities and the Issuer cannot establish unilaterally; Ginnie Mae must approve each MBS. Finally, the issuance of Ginnie Mae MBS obviously was not created to circumvent the provisions of FIN 46(R), because the program pre-dates the standard by several decades.

Alternative View:

MBA considered an alternative view that the paragraph 4(i) scope exception was not intended for entities created to provide liquidity to a non-governmental organization. In the case of a Ginnie Mae MBS, the Issuer is the party creating each individual pool for a substantive business purpose benefiting the Issuer. Such proponents further observe that there is no conceptual basis to provide a scope exception for an entity created with a Ginnie Mae guarantee when a GSE entity is substantively equivalent. MBA disagrees with this alternative view because Ginnie Mae is a governmental organization and the financing entities cannot be created without the Ginnie Mae creation of the program. Conversely, Fannie Mae and Freddie Mac are corporations that were chartered by Congress, and are designed to be owned by private stockholders. However, on September 7, 2008, Fannie Mae and Freddie Mac were put under the conservatorship of the FHFA and it remains unclear what effect this will have on their respective structures.

If the paragraph 4(i) scope exception is not available, the remaining questions are relevant.

Question 3: Assuming a Ginnie Mae issuance is created through an entity and is within the scope of FAS 167, is the entity a VIE?

Paragraph 5 of FIN 46(R), as amended by FAS 167, provides that if any of the criteria in paragraph 5(a), (b), or (c) exists, the entity is determined to be a VIE requiring the entity to be subject to consolidation in accordance with the interpretation. The paragraph 5(a) criterion states, in part:

The total equity investment⁶ at risk is not sufficient to permit the entity to finance its activities without additional subordinated financial support provided by any parties, including equity holders.

⁶ Equity investments in an entity are interests that are required to be reported as equity in that entity's financial statements.

MBA's View:

A Ginnie Mae issuance is a static vehicle that contractually requires all cash flows to be paid to the beneficial interest holders as principal and interest. The MBS issued would be reported as debt on the entity's balance sheet, not equity. As the entity has no equity investment at risk, the paragraph 5(a) criterion is met and, therefore, the entity is deemed to be a VIE.

Alternative View:

MBA does not believe there is an alternative view to this conclusion.

Question 4: Assuming a Ginnie Mae issuance is created through an entity, is within the scope of FAS 167 and is determined to be a VIE, which party, if any, is the primary beneficiary ("PB")?

Paragraph 14A. of FAS 167 states:

An enterprise with a variable interest in a variable interest entity shall assess whether the enterprise has a controlling financial interest in the entity and, thus, is the entity's primary beneficiary. This shall include an assessment of the characteristics of the enterprise's variable interest or interests and other involvements (including involvement of related parties and de facto agents),^{15a} if any, in the variable interest entity, as well as the involvement of other variable interest holders. Additionally, the assessment shall consider the entity's purpose and design, including the risks that the entity was designed to create and pass through to its variable interest holders. An enterprise shall be deemed to have a controlling financial interest in a variable interest entity if it has both of the following characteristics:

- a. The power to direct the activities of a variable interest entity that most significantly impact the entity's economic performance
- b. The obligation to absorb losses of the entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity. The quantitative approach prescribed in paragraph 8 of this Interpretation is not required and shall not be the sole determinant as to whether an enterprise has these obligations or rights.

^{15a} See paragraph 16 for guidance on related parties and de facto agents.

Only one enterprise, if any, is expected to be identified as the primary beneficiary of a variable interest entity. Although more than one enterprise could have the characteristic in paragraph 14A(b), only one enterprise, if any, will have the power to direct the activities of a variable interest entity that most significantly impact the entity's economic performance.

In short, to be the PB, the enterprise must have a variable interest and meet both of the criteria of paragraph 14A.

Design of the Entity

In order to make this determination, MBA first considered the design of the VIE, including the risks that the entity was designed to create and pass through to its variable interest holders. In making this assessment, the MBA determined the following:

- a. The primary purposes for the entity were (1) to provide the investors with the ability to invest in a pool of mortgage loans with credit protection from FHA, VA, and Ginnie Mae and (2) to provide cost-effective secondary market liquidity for FHA and VA loans, which provides issuers the ability to originate additional loans to low-to-moderate income households and to veterans. MBA notes that the design of the entity also provides a servicing fee for the Issuer/Servicer. However, MBA does not believe this is a "primary" purpose of the entity, because those cash flows inured to the Issuer/Servicer prior to the transfer. The Ginnie Mae issuance simply allows those fees to be capitalized to the extent sale accounting is achieved.
- b. The transaction was marketed to potential MBS holders as an investment in a portfolio of residential mortgage loans with exposure to the credit risk of FHA/VA, the Issuer and Ginnie Mae and prepayment risk associated with the underlying mortgage loans. From an investor perspective, the MBS trades on the strength of the Ginnie Mae guarantee.

- c. The principal risks to which the VIE is exposed include credit risk of the underlying assets, prepayment risk, and the risk of fluctuations in the value of underlying property. We considered whether the credit risk of the underlying assets should not be considered a risk of the entity. However, MBA believes that excluding the risk to the underlying borrower is inappropriate as it is the main risk of the combined transactions. The substance of the transactions contemplated at the time of origination and related nature of the guarantors are part of the design of a Ginnie Mae MBS. Loans included in a Ginnie Mae issuance were generally originated as “held-for-sale.” MBA notes that during the fiscal year ended September 30, 2009, 99 percent of FHA loans originated and 97 percent of VA loans originated were pooled into Ginnie Mae MBS. All parties involved understand the connective role that FHA, VA, and Ginnie Mae play in providing continued liquidity to this market.

Variable Interests Determination

MBA considered whether the following parties have a variable interest in the VIE:

Potential Variable Interest Holder	Variable Interest?	Analysis
MBS Investors	Yes	The MBS investors absorb substantially all of the risk of prepayment and the minor risk of guarantor default. In addition, the MBS holder absorbs the market risk that the value of its investment will fluctuate as interest rates fluctuate.
FHA/VA/RHS/PIH	Yes	As discussed in the Design of the Entity above, these governmental entities absorb substantially all of the risk of the underlying mortgage loans. Although this insurance is attached at the time of origination, MBA believes that these guarantees are absorbing the credit risk of the VIE based on the design of the related organizations.

Ginnie Mae	Yes	<p>If a borrower defaults, the first loss prevention is the value of the underlying property. Second, the FHA/VA/RHS/PIH insurance⁷ covers losses. Any loss not covered by the above must be advanced to the MBS holders by the Issuer, which is not reimbursable by Ginnie Mae. Ginnie Mae receives 6 basis points to absorb the credit risk of the Issuer not making good on its obligation to advance. Historically, this risk has been low, but has become a more substantial risk as Issuers have defaulted in the current economic environment.</p>
Issuer/Servicer	Yes	<p>The Issuer/Servicer can have multiple involvements in a Ginnie Mae issuance as follows:</p> <ul style="list-style-type: none"> • MBS Investor (see analysis above) • Servicer • Obligation to Advance Cash Shortfalls • Obligation for Standard Representations and Warranties • Holder of Default Call Option <p>MBA believes that the Issuer/Servicer is typically going to be determined to hold a variable interest. MBA analyzed whether the fees received as servicer would be a variable interest under paragraph B22 of FAS 167. The cash flows received from the assets of the entity are paid to three parties: Ginnie Mae for its guarantee fee, MBS Investors, and the Servicer for its servicing fee. As the Servicer is required to first pay the guarantee fee and advance principal and interest to the MBS Investors, its servicing fee is subordinate to all other payments. MBA believes this indicates that the Servicer is in a subordinate position as described in paragraph B22(b). Therefore, the Issuer/Servicer would be deemed to have a variable interest in the VIE⁸.</p> <p>MBA does not believe the Default Call Option absorbs variability of the VIE. The Issuer/Servicer is reimbursed the same</p>

⁷ The FHA insurance covers all principal loss, while the VA guarantee covers up to 50 percent of the principal amount, but is in a first-loss position.

⁸ Note that MBA analyzed B22 due to the Servicer's role as a "service provider," not as a "decision maker." See "Power Determination" below.

		amount from FHA or VA whether or not it elects to buy a loan in default out of a pool. In other words, the difference between the price of the call option and fair value still resides primarily with the underlying insurer. Rather, the Default Call Option is a creator of additional prepayment variability for the MBS Investors.
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Power Determination

Paragraph 14B of FAS 167 states:

An enterprise must identify which activities most significantly impact the entity's economic performance and determine whether it has the power to direct those activities. An enterprise's ability to direct the activities of an entity when circumstances arise or events happen constitutes power if that ability relates to the activities that most significantly impact the economic performance of the entity. An enterprise does not have to exercise its power in order to have power to direct the activities of an entity.

The underlying risks identified in the Design of the Entity and Variable Interests Determination above were (1) credit of the underlying assets, (2) prepayment risk, and (3) market risk. The only risks that can be managed by the parties involved with the VIE are credit and to a certain extent, prepayment⁹. MBA first identified the parties involved with the entity and their level of influence on impacting these risks as follows:

Variable Interest Holder	Power Consideration
MBS Investors	The MBS Investors do not have any power to direct the activities that impact credit or prepayment.
FHA/VA/RHS/PIH	These insurers set the guidelines for servicing, including forbearance, foreclosure, and collection processes. These guidelines can be changed at the discretion of the insurers as they see fit. Ultimately, the Issuer/Servicer is servicing on behalf of the insurers to minimize their loss. Although the respective Servicing Guides provide the Servicer a certain level of discretion within the guidelines, these guidelines are not static. This fact pattern is vastly different from a private label securitization in which the range of activities granted the servicer can't be unilaterally changed by any party. MBA notes that paragraph 14B specifically states that "an enterprise does not have to exercise its power in order to have the power to direct the activities of the entity". MBA believes that the powers the insurers have to direct the actions

⁹ Only certain risks of prepayment can be managed. A large driver of prepayments is borrower behavior, including defaults and voluntary payoffs. The timing of cash flows received by the MBS Investors in the event of default can be shaped somewhat based on the decisions around collections, loss mitigation, foreclosure, and REO disposition. Defaults are included in prepayment risk as those involuntary payoffs also impact timing of cash receipts.

	<p>that must be taken by a servicer and change those required actions (which have been previously demonstrated¹⁰) has a significant impact on the credit and prepayment risk of the VIE. The insurers also set the rate of Servicer interest and foreclosure expense reimbursement on loans in foreclosure.</p> <p>See Appendix IV for website references to Ginnie Mae and Insurer Servicer Guides.</p>
Ginnie Mae	<p>In general, Ginnie Mae’s MBS program defers to the respective guides of the insurers for the specification of servicing guidelines. Ginnie Mae has the power to approve issuers, and it monitors issuer’s financial and servicing performance. If an issuer fails to meet certain financial standards and performance standards, Ginnie Mae can impose a number of sanctions including denial of further commitment authority, denial of transfers of additional Ginnie Mae servicing to the issuer, denial of authority to issue additional securities even if the issuer has commitment authority outstanding, imposition of civil fines and penalties, and declaration of default and termination of issuer status. Ginnie Mae also approves document custodians and establishes the rules for initial and final pool certification. Ginnie Mae sets the rules for pass-through, pool buyouts and monthly investor accounting and reporting. In certain instances, Ginnie Mae has assumed the responsibilities of an Issuer/Servicer that has defaulted on its obligation.</p> <p>MBA also considered paragraph 14F of FAS 167, which states:</p> <p style="padding-left: 40px;">Although an enterprise may be significantly involved with the design of an entity, that involvement does not, in isolation, establish that enterprise as the enterprise with the power to direct the activities that most significantly impact the economic performance of the entity. However, that involvement may indicate that the enterprise had the opportunity and the incentive to establish arrangements that result in the enterprise being the variable interest holder with that power. For example, if a sponsor has an explicit or implicit financial responsibility to ensure that the entity operates as designed, the sponsor may have established arrangements that result in the sponsor being the enterprise with the power to direct the activities that most significantly impact the economic performance of the entity. [Emphasis Added]</p> <p>As stated in the Background, Ginnie Mae established the guidelines and provisions for issuing a Ginnie Mae MBS. In this design, Ginnie Mae created, among other things, provisions related to the Default Call Option and a mandatory obligation to repurchase loans before modification. These provisions impact the prepayment variability absorbed by the MBS investors.</p> <p>See Appendix IV for website references to Ginnie Mae and Insurer Servicer Guides.</p>

¹⁰ See <http://www.hud.gov/offices/hsg/sfh/nsc/Immltrs.cfm> for specific examples of FHA exerting its ability to change the servicers practices unilaterally, including Mortgagee Letter 00-5 and 09-35 regarding loss mitigation activities.

Issuer/Servicer	<p>The Issuer must service delinquent mortgages and manage foreclosure or assignment procedures in accordance with the servicing and claims collection requirements of FHA, VA, RHS, or PIH, as applicable, the Ginnie Mae Guarantee Agreement, and accepted mortgage lending and servicing practices, ethics and standards. The Issuer/Servicer performs normal servicing functions including the collection of principal and interest; the collection and disbursement of escrow amounts; and foreclosure, collection and forbearance activities. As stated above, these are all specified in servicing guidelines issued by FHA, VA, RHS and PIH. The Servicer also passes scheduled principal and interest on to investors. If borrowers are delinquent, the Issuer/Servicer is also permitted by Ginnie Mae to buy seriously delinquent loans out of pools. This allows the Issuer/Servicer to mitigate its loss on curtailments (by FHA and VA) of interest passed through to investors on loans in foreclosure. The Issuer/Servicer makes an economic decision based upon the Ginnie Mae MBS pass-through rate when compared with the Issuer/Servicer's own cost of funds related to the pool buyout. This buyout authority can impact the timing of payoffs to the pool related to loans in the foreclosure pipeline, thus impacting prepayment risk. Since servicing and pass-through procedures are specified by the respective guides of Ginnie Mae, FHA, VA, RHS and PIH, the only servicer discretion that the Issuer/ Servicer has is to exercise the discretion allowed by the respective guides, which change at the discretion of the insurers, and to buy loans out of the pool that are seriously delinquent. However, even that is done based upon the economics dictated by FHA and VA's curtailments of interest and within the constraints for pool buyouts specified by Ginnie Mae. Although an "option" to the Issuer, the decision to buyout a loan is heavily influenced by Ginnie Mae's design of the program, including the 5% threshold on 90+ day delinquency rate imposed by Ginnie Mae as discussed in the Background section of this letter.</p>
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Based on the above analysis, MBA has identified multiple parties that direct different activities that impact the entity's economic performance. Paragraph 14E of FAS 167 states, in part:

If the activities that impact the entity's economic performance are directed by multiple unrelated parties and the nature of the activities that each party is directing is not the same, then an enterprise shall identify which party has the power to direct the activities that most significantly impact the entity's economic performance. One party will have this power, and that party shall be deemed to have the characteristics in paragraph 14A(a).

MBA notes that the insurers and Ginnie Mae are all governmental entities that are considered related parties when applying FAS 167. FHA, Ginnie Mae, and PIH are all divisions of the Department of Housing and Urban Development and included in HUD's consolidated financial reports. Therefore, we must consider whether the governmental entities, as a group, or the Issuer/Servicer have the power to direct the activities that most significantly impact the VIE's performance. Essentially, the governmental entities completely control the design of the VIE. They dictate the quality and nature of the collateral, require the underlying

insurance, set the servicing standards via the servicing guides (which are uniform rather than negotiated for each lender) and can change them at will, designed the program that makes Ginnie Mae issuance possible, and even "drive" certain prepayments by requiring a loan to be repurchased prior to significant modification. Conversely, the Issuer/Servicer chooses the specific collateral for each underlying pool (although FHA/VA single-family loans each could be viewed as fungible), makes decisions within the parameters of the servicing guides, and ultimately decides whether to exercise the Default Call Option.

MBA's View:

Considering all of the aspects of design and power, MBA believes that the governmental entities' power characteristics have a much more significant impact on the entity's economic performance than the power characteristics of the Issuer/Servicer. MBA believes that the power that the governmental insurers can and have exerted over the servicing of the underlying assets is compelling and much different than a private label securitization in which a servicer is typically deemed to have power.

Alternative View:

MBA considered the alternative view that the Issuer/Servicer should be deemed to have power, because it currently has certain discretion within the servicing guides. MBA believes this conclusion would be inappropriate as it ignores the design of the entity and the power the insurers have to unilaterally change the guides and level of discretion.

Primary Beneficiary Determination

MBA determined that the governmental entities as a related party group have the characteristics of paragraph 14A of FAS 167. Paragraph 17 of FAS 167 states:

In situations in which an enterprise concludes that neither it nor one of its related parties has the characteristics in paragraphs 14A(a) and 14A(b) but, as a group, the enterprise and its related parties (including the de facto agents described in paragraph 16) have those characteristics, then the party, within the related party group, that is most closely associated with the variable interest entity is the primary beneficiary. The determination of which party within the related party group is most closely associated with the variable interest entity requires judgment and shall be based on an analysis of all relevant facts and circumstances, including:

- a. The existence of a principal-agency relationship between parties within the related party group
- b. The relationship and significance of the activities of the variable interest entity to the various parties within the related party group
- c. A party's exposure to the variability associated with the anticipated economic performance of the variable interest entity

- d. The design of the variable interest entity.

The first sentence of paragraph 17 indicates that if one party in the related party group has both characteristics of paragraph 14A, that party is the primary beneficiary. If one party does not have both characteristics individually, the determination of which party is most closely associated to the VIE shall be based on the facts and circumstances.

MBA's View:

MBA believes that a strong argument can be made that an underlying insurer would have both characteristics of paragraph 14A. This conclusion might depend on the percentage of assets in each pool insured by a respective insurer. With that said, the identification of which governmental entity should consolidate a Ginnie Mae issuance is beyond the scope of MBA's letter, particularly since HUD prepares its financial statements in accordance with accounting standards established by the Federal Accounting Standards Advisory Board (www.FASAB.gov) not those established by the FASB.

The MBA appreciates the Staff's willingness to deal with these questions as an industry-wide issue on a pre-clearance basis. FASB staff recently contacted MBA and indicated that they are willing to assist the SEC in deliberating the issues raised in this letter. Please contact Ms. Holly Barker, Project Manager at the FASB.

Any questions about MBA's comments, assertions and questions in this letter should be directed to Jim Gross, Associate Vice President and Staff Representative to MBA's Financial Management Committee, at (202) 557-2860 or jgross@mortgagebankers.org. Thank you.

Sincerely,



John A. Courson
President and Chief Executive Officer

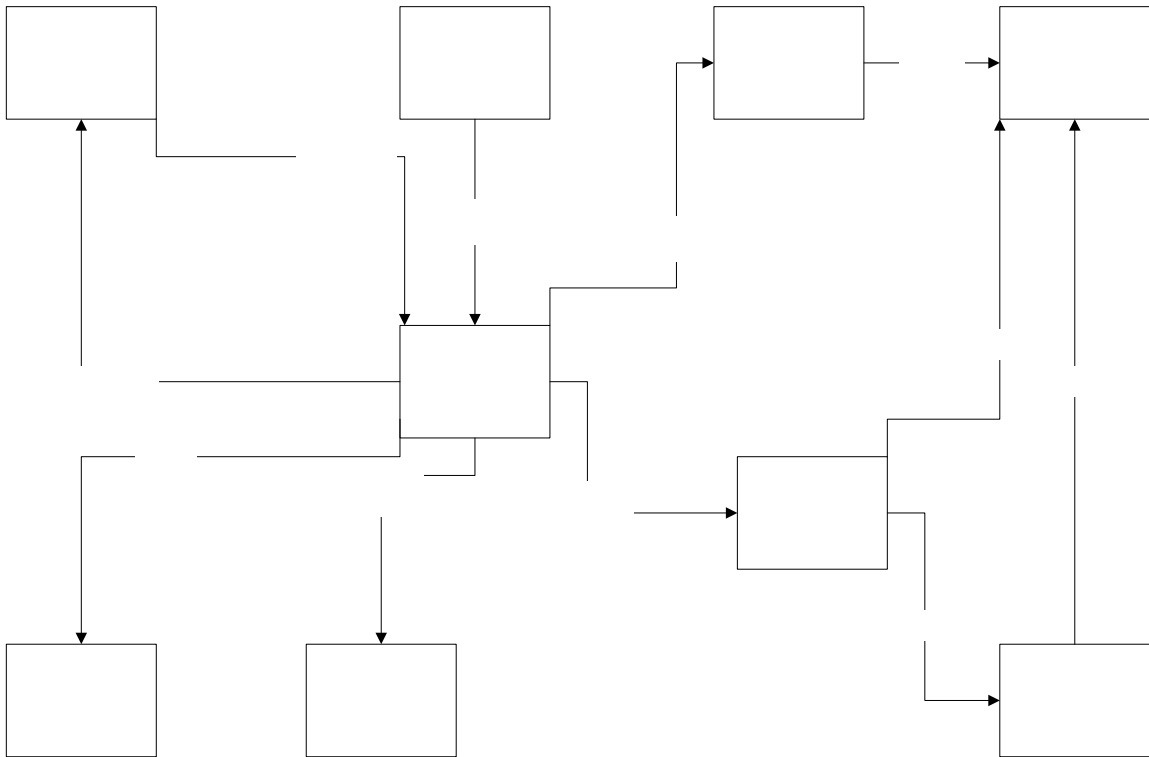
Cc: Mr. Russell G. Golden, Technical Director, Financial Accounting Standards Board

Cc: Ms. Holly Barker, Project Manager, Financial Accounting Standards Board

Cc: Mr. Michael J. Najjum, Jr., Chief Financial Officer, Ginnie Mae

Appendix I

Ginnie Mae MBS Chart



Ginnie Mae Products

Ginnie Mae has a variety of securities tailored to investors with diverse needs. At the core are two Ginnie Mae MBS products:

Ginnie Mae I MBS - requires all mortgages in a pool to be the same type (e.g., single-family, multi-family, etc.), be issued by the same entity, and have the same fixed interest rate.

Ginnie Mae II MBS – restricted to single family mortgages, but allows multiple-issuer pools to be assembled, which in turn allows for larger and more geographically dispersed pools as well as the securitization of smaller portfolios. A wider range of coupons is permitted in a Ginnie Mae II MBS pool, and issuers are permitted to take greater servicing fees — ranging from 25 to 75 basis points.

These two core MBS products may also serve as the underlying collateral for “multiclass products” such as Real Estate Mortgage Investment Conduits (REMICs), Callable Trusts, Platinum securities, and Stripped MBS, for which GNMA also guarantees the timely payment of principal and interest.

- **REMICs** are investment vehicles that reallocate the pass-through cash flows from underlying mortgage obligations into a series of different bond classes, known as tranches.
- **Callable Trusts** allow investors the flexibility to redeem or call a security prior to its maturity date under certain conditions, to hedge against fluctuating rate environments.
- **Platinum securities** allow investors who hold multiple pools of MBS to combine them into a single GNMA Platinum Certificate.
- **Stripped MBS** are custom-designed securities that redirect GNMA MBS cash flows to meet investors’ specific income needs around interest and principal payments.

These multiclass products allow the private sector to combine and restructure cash flows from GNMA MBS into securities that meet unique investor requirements in connection with yield, maturity, and call-option protection. The intent of the multiclass products is to increase liquidity in the secondary mortgage market and to attract new sources of capital for federally insured or guaranteed residential loans.

The Ginnie Mae Process

The Ginnie Mae process is as follows:

1. Mortgage lenders apply to Ginnie Mae for approval to become an Issuer of Ginnie Mae mortgage-backed securities. The applicant must meet certain eligibility requirements established by Ginnie Mae in order to become an approved Ginnie Mae Issuer. Ginnie Mae, in its sole discretion, may refuse to grant any application for Issuer status if Ginnie Mae determines that the applicant has failed to meet the specific requirements set forth in the Ginnie Mae MBS Guide or otherwise determine that the approval of the applicant would be detrimental to the Ginnie Mae MBS Program.
2. Once a mortgage lender becomes an approved Ginnie Mae Issuer, the Issuer would apply to Ginnie Mae for a guarantee commitment authority. The Commitment authority commits Ginnie Mae to guarantee the securities to be issued, and for pool and loan packages numbers. The Commitment authority allows an issuer to issue a specified maximum dollar amount of Ginnie Mae securities in either Ginnie Mae Programs, and in the various pool types for which it is eligible.
3. After obtaining the guarantee commitment from Ginnie Mae, the Issuer assembles a pool of single-family mortgages that are insured by the FHA, or guaranteed by the VA, RHS or HUD that it has originated or acquired.
4. The issuer then must:
 - a. Prepare and submit documents for each pooled loan to the Document Custodian. The Document Custodian is required to (1) review the pool loan documents and certify to Ginnie Mae that they accurately represent the pooled mortgages in accordance with Ginnie Mae requirements, and (2) to maintain control of the documents over the life of the pool, and
 - b. Establish with a Funds Custodian separate custodial accounts to hold principal and interest and escrow collections for pools;
5. The Issuer then forwards the pool and loan documents to the Pool Processing Agent (PPA). The PPA reviews and approves, on Ginnie Mae's behalf, the physical documents and/or electronic transmissions submitted by the Issuer that describe the pool of mortgages as a whole. Upon approving the pool, the PPA directs that the Ginnie Mae securities be issued.

6. Once the mortgage pool has been delivered by the originator and accepted by Ginnie Mae, the securities are printed by the Ginnie Mae Central Paying and Transfer Agent (CPTA). The CPTA acts as both Transfer Agent and Collection Agent.
 - a. Transfer Agent – In its capacity as Transfer Agent, the CPTA prepares all Ginnie Mae securities and delivers them to security holders. The CPTA registers a new issuance of securities in the name of the depository and issues the securities in uncertificated form through the depository's book-entry system. As Transfer Agent, the CPTA also handles exchanges of securities at the request of security holders, deals with missing or damaged certificates, and maintains a central registry of securities ownership and transfer information for all pools.
 - b. Collection Agent – Under the Ginnie Mae I Program, the CPTA acts as collection agent in connection with Ginnie Mae guarantee fee, automatically debiting each Issuer's central P&I custodial account in the amount necessary to pay Ginnie Mae its guarantee fee. Under the Ginnie Mae II Program, the CPTA acts as both the collection agent and paying agent in connection with monthly payments to security holders and to Ginnie Mae. The CPTA (1) automatically debits each Issuer's central P&I custodial account monthly in the amounts necessary to pay security holders and to pay Ginnie Mae its guarantee fee, (2) pays those amounts to security holders and Ginnie Mae, and (3) prepares and sends a remittance advice to security holders with their payments.
7. The Issuer may hold the mortgage pass-through certificates in its portfolio, can sell the mortgage pass-through certificates to investors or to dealers, or it can use the mortgage pass-through certificates as collateral for a loan.

Appendix IV

References to Ginnie Mae and Insurer Servicer Guides

For Ginnie Mae guidelines:

<http://www.ginniemae.gov/guide/guidtoc.asp?Section=Issuers>

For FHA servicer guidelines:

portal.hud.gov/pls/portal/url/PAGE/FHA_HOME/LENDERS/servicing_guidance

For periodic FHA guidance updates:

<http://www.hud.gov/offices/hsg/sfh/nsc/1mmltrs.cfm>

For VA servicer guidelines:

www.homeloans.va.gov/docs/sg.pdf

For Rural Housing servicer guidelines:

<http://www.rurdev.usda.gov/WI/programs/rhs/library/WI-Rural-Development-GRH-Loan-Servicing-Guide.pdf>