

The following best practices have proven successful in ensuring compliance with Freddie Mac's custodial account requirements. Freddie Mac compiled these best practices using input from Servicers during account reviews and meetings, and from feedback in our custodial account classes. Use these best practices, along with our Understanding Custodial Accounts workshop and manual, to help you

- Reconcile your custodial account.
- Resolve variances.
- Effectively manage your cash and custodial account process so you can meet the requirements detailed in Chapters 76 through 79 of the *Single-Family Seller/Servicer Guide* (the Guide).

Contact us at (800) FREDDIE to obtain a copy of our Understanding Custodial Accounts manual or to register for our Understanding Custodial Accounts workshop. You can also visit us on the Learning Center at www.FreddieMac.com/learn/.

Each month we randomly select and perform desktop reviews of Servicers' custodial account reconciliations to assess compliance with our requirements. If you are selected, we require that you submit three months of reconciliations with supporting documentation for review. We encourage you to review and test your procedures and processes to ensure they meet our requirements. Please contact your Freddie Mac Investor Accounting Specialist if you need assistance.

Handle Funds According to Requirements

- Immediately establish custodial accounts for both principal and interest and for escrow funds for Freddie Mac loans.
- Establish a demand deposit or interest bearing account and house the account at an eligible depository (see the Guide for eligibility requirements).
- Properly title accounts according to Section 77.11 of the Guide.
- Use escrow accounts for funds held in suspense pending proper distribution, such as funds held on behalf of the borrower and funds for partial payments and buydowns.
- Keep funds segregated at all times (for example, keep principal and interest separate from escrow, and keep Freddie Mac funds separate from other investors' funds).
- For bi-weekly mortgage payments (mortgages where the due date is every two weeks per the original mortgage note when the loan was sold to us), apply payments to the loan and deposit funds into the principal and interest account as payments are received.
- Establish disbursement clearing accounts, if applicable, for principal and interest and for escrow.
- Restrict all investments to interest bearing accounts, federal funds, and time deposits of no more than seven days.

Reconcile Your Accounts

- Ensure that you perform custodial account reconciliations within 45 days of each accounting cutoff.
- Ensure that you reconcile the following:
 - Principal and interest bank balance (as of the accounting cutoff) to the total liability due us (as of the accounting cutoff) from the Monthly Account Statement
 - Escrow bank balance (as of the accounting cutoff) to the total positive loan-level escrow liability per the trial balance (as of the accounting cutoff)
- Use the reconciliation worksheets (Form 59, *Principal and Interest Custodial Account Reconciliation Worksheet*, for principal and interest accounts, and Form 59E, *Escrow Custodial Account Reconciliation Worksheet*, for escrow accounts) available in the Understanding Custodial Accounts manual and in our Guide. Do not add or delete line items from the reconciliation worksheets.

Resolve Variances

- Minimize using corporate funds in your Freddie Mac custodial account by
 - Repaying advances timely
 - Reducing deposit errors
 - Ensuring overnight investments are maximized
 - Reducing fees payable
 - Limiting lockbox rejects
- Use the custodial account reconciliation process to identify reporting errors such as
 - Unreported payoffs
 - Unreported collections
 - Early or late inactivations
 - General reporting errors (i.e., interest miscalculated due to ANY discrepancies)
- Use the custodial account reconciliation process to detect the impacts of changes in your processes and to identify areas of mortgage servicing that require improvement. Track the following:
 - Changes in your delinquency accruals
 - Amortization differences
 - Swings in escrow advance activity and escrow management activities
 - Processes for suspense and unapplied funds, as appropriate
 - Interest on mortgages that you closed and then sold to us in the same reporting cycle
- Resolve and fund, within 90 days, identified and unidentified variances in the principal and interest and escrow custodial accounts.
- Always keep your custodial bank account properly funded (never have a negative balance), with sufficient funds available for the next remittance due to Freddie Mac.

Process Payments Correctly

- Ensure that you deposit funds into Freddie Mac custodial accounts no later than the first business day following your receipt of a borrower's payment. Lockbox payments should be deposited within two business days.
- Apply payments according to the security instrument.
- If a payment is deficient by more than \$25, credit the payment as unapplied or suspense funds until a full payment is received, or return the payment to the mortgagor. If a payment is within \$25, you may
 - Credit the payment to escrow as unapplied or suspense funds until a full payment is received.
 - Return the payment to the mortgagor.
 - Short the amount applied to escrow and apply a full payment to the loan.
- Apply curtailments according to Section 51.20 of the Guide.

Maintain Records

- Retain records which reflect the following:
 - Designation of the account
 - Account numbers
 - Amounts of the borrower's principal and interest and escrow funds remitted to you (the loan record)
 - Dates that monies were received and deposited
 - Freddie Mac's vested and ascertainable interest in monies deposited into each account
- Maintain your custodial account reconciliations in "stand-alone" packages with all supporting documentation for each line item attached to the reconciliation worksheets.

Fund Negative Escrow Balances

Advance funds on a daily basis (as necessary for payment of charges assessed) for each loan with an escrow balance falling below zero. Funds received for one loan cannot be used to offset a deficit for another loan.