By Rick Seehausen

# The Tides Do Change

Every area of the mortgage industry has endured change in its approach to doing business. Along with reconstruction of the secondary market, other facets such as origination, processing, underwriting and servicing will never be the same.

And as federal mandates are handed down and more companies explore new ways of creating efficiencies, the lines have been blurred as to whose job it is to manage the different life stages of a loan. This complex new operating environment has required more companies to enlist the help of trusted business partners.

## HAMP

Some of the most sweeping changes in the mortgage industry have been spurred by this year's federally mandated Home Affordable Modification Program (HAMP). Lenders and servicers have found themselves outside of their business comfort zone with the program requiring loan modifications on assets in their portfolios or loans being serviced as "government risk" loans, which means the loans are backed by Fannie Mae or Freddie Mac. Modifying loans under these program requirements is an activity very similar to origination, full of newly mandated processes and responsibilities typically unfamiliar to a loan servicer. For this reason, many companies have turned to niche service providers to outsource specific functions of the process not core to a typical servicing operation.

As an example, qualification under the HAMP guidelines requires borrower outreach programs, an accurate and verifiable calculation of the borrower's debt-to-income (DTI) ratio, a net present value (NPV) comparison of the modification path versus the costs of foreclosure, and collection and review of the borrowers' income and hardship documentation.

For those borrowers qualifying for HAMP and who have fulfilled the trial-plan requirements, a servicer is able to modify the terms of the loan. But to do so, the servicer must understand why and when certain modification loans must be recorded and subordinated, including the accurate preparation of a recordable modification agreement specific to the local jurisdiction.

Because service providers can offer expertise in specific areas, they can help with almost every aspect of the mortgage process. Additionally, they can better manage cost and capacity fluctuations all while enhancing the quality of these modified loans.

## Contract underwriting services

Mortgage insurance companies (MIs) have also undergone a significant transformation during recent times. In the days of hyper-origination, MIs provided contract underwriting to their clients because it ensured them more opportunity for providing required mortgage insurance. But adversely, in the new mortgage atmosphere, MIs have been exiting this particular area because it was not the main focus of their business and did not always guarantee mortgage insurance orders—especially in a lending climate where loans with less than 80 percent debt-to-income ratios are the norm.

Some MIs have sought out trusted service providers to endorse as a source of contract underwriting services. For example, PMI Mortgage Insurance Co. (PMI), Walnut Creek, California, now endorses LenderLive Network Inc., referring contract underwriting business to our company.

Pete Pannes, PMI senior vice president, explains that engaging LenderLive provides PMI's customers "an alternative that they could rely on." Having a business partner provide contract underwriting services is a cost-effective way to meet the fluctuating demands of the mortgage market. LenderLive is delegated to underwrite for mortgage insurance and offers secure online loan submission with a full underwriting staff.

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## Increased market share

Contract underwriting is not the only service being placed in the hands of fulfillment service providers. Small to midsized institutions are developing these partnerships as well to decrease static costs and, at the same time, be in a position to have inherent capacity for overall surges in volume.

More community banks and credit unions are growing their origination market share, displacing what traditionally belonged to mortgage brokers. And as this business increases, these financial institutions are looking for solutions to best manage that growth.

Consider that large, well-known financial institutions can cast a wide net to attract mortgage loan customers. But they typically struggle at reaching into communities where consumers value trusted local relationships. Also, their cost to originate can be higher than community-based institutions because of the increased marketing costs needed to maintain their far-reaching footprint and generate that business.

The group that previously filled the community lending need was typically mortgage brokers. Since broker originations have subsided as more and more wholesale lenders have exited the market and the appetite for third-party origination has waned, community banks and credit unions are well-positioned to inherit much of that business as trusted institutions to meet those community lending needs.

As these community institutions grow their businesses, they have a build-or-rent decision to make when it comes to the technology, other infrastructure and staffing needed to help with increased volume. Business partners help in this process because they can convert fixed costs to variable costs. Mortgage

service providers typically operate on a per-transaction charge, so if the number of loans originated fluctuates, so does the cost. This helps to reduce unnecessary overhead. Better yet, a true variable-cost model means that the expense of an activity is also associated with a revenue-offsetting opportunity for the bank.

Fundamentally, community banks and credit unions take in deposits and make loans on those deposits. The secondary market for mortgage originations has largely been reduced to Fannie Mae, Freddie Mac and Ginnie Mae. So the next tier of liquidity is a bank's ability to portfolio niche mortgage products and their willingness to put these loans on their balance sheets. What makes this more palatable for institutions is having confidence in the quality of loans. Working with experienced business partners possessing proven origination outsourcing expertise can help ensure loan quality. Such relationships can give community banks and credit unions the opportunity to maintain newly gained market share while keeping costs low and quality high.

**Broker to banker**

Another trend making outsourced origination business partnerships more attractive is that of larger, more established brokers converting to mortgage bankers. This is happening because the number of wholesale lenders has been so greatly reduced and the liquidity of third-party origination has all but disappeared. But this trend is also being fed by the fact that some former lenders are re-establishing their warehouse lines of credit, as more and more banks begin to see analysis that warehouse lending can once again be profitable.

These newly formed and returning mortgage bankers have new responsibilities for process functions that they did not have as brokers or that did not exist before this new era of government-mandated lending requirements. Their options: hire individuals with those competencies or outsource to a third-party business partner mortgage service provider.

In addition, as more brokers make the migration to mortgage bankers, many of the warehouse-line providers are interested in ensuring consistent delivery and accuracy in the closing process, as the warehouse lender shares significant risk in each transaction with the lender. Warehouse lenders want to see standardization in the closing processes, which has triggered them to refer "new" bankers to companies such as LenderLive for lender closing services. Both the mortgage banker and warehouse lender benefit when quality is increased and costs are kept variable and low.

A changing tide has left the economy in turmoil. That distress has been amplified by the regulatory reaction to the downturn. And, as evidenced by just the total number of lenders, brokers, banks and vendors left standing, it has left very little room for error. An experienced fulfillment service provider can help lenders adjust to the new environment and initiate new ventures arising from the rebirth of liquidity. It can also help improve speed to market and cost ratios, while making the process more efficient overall.

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