The Future of Mortgage Banking

*Why the time is right for community and regional depository financial institutions to dominate market share and how they can effectively compete in the new market place*

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Community banks have a tremendous opportunity to seize market share in the mortgage lending business, following the collapse of non-depository mortgage banking lenders. The depository institutions now have several advantages they can exploit to fill the lending void— an influx of capital from increased deposits, superior reputations, and familiarity with rigid regulatory environments. In addition, new Web-based technology can provide even the smallest community banks with technology systems comparable to those used by Fortune 500 firms.

Community-based and regional depository financial institutions have traditionally participated in mortgage lending with varying degrees of intensity and profitability, depending on the economic and regulatory environments. Historically, community institutions were the natural choice for homebuyers seeking loans, and their conservative lending practices contributed to a stable mortgage economy. In many ways, the nation’s mortgage economy had evolved to accommodate communities’ depository institutions’ needs.

However, during the Great Depression, banks and savings and loans, fell into disfavor as a by-product of that era’s wave of foreclosures. Based in part on consumer disillusionment with traditional financial institutions and tight access to credit (because disillusioned consumers make reluctant depositors), non-depository lenders emerged to meet the growing demand for consumer loan alternatives.

Initially insurance companies and pension funds provided capital for many of these non-depository lenders. For the last two to three decades, the competitive advantage shifted even more to “pure play” mortgage lenders. These new players not only had access to the same government-backed mortgage loan programs as depository institutions, but could also tap a large number of private investors, which increased economies of scale, profitability and risk to unprecedented levels.

But recently, the landscape has been permanently altered. National commercial banks and non-depository mortgage bankers, which once dominated mortgage lending, have lost favor with mortgage industry regulators and borrowers. Their risky business models have brought about their demise while creating an ideal climate for hometown lending.
Community banks are poised to regain their role as primary providers of mortgage loans because they have for the most part remained true to conservative business practices.

According to an October 19, 2008, *New York Times* article:

“While national banks gorged on one another in recent years, growing ever larger and devising ever more exotic theories about how and to whom to lend money, smaller, state-chartered institutions watched skeptically from the sidelines, unconvinced that the basic laws of economics had suddenly changed, and husbanding assets that amounted to no more than loose change at their swaggering competitors. A wise strategy, as it turned out. Staying small and staying home has meant staying solvent.”

According to the Independent Community Bankers Association (ICBA), today there are nearly 8,500 community banks, including commercial banks, thrifts, stock and mutual savings institutions, with more than 50,000 locations throughout the United States. Assets may range from less than $10 million to a few billion dollars. Numerically, community banks constitute 98% of all banks.

**Seize the Advantages**

In short, community banks are at the right place at the right time to leverage their six primary advantages to expand or begin mortgage lending operations:

1. Additional capital from increased deposits,
2. Superior accountability for servicing and originations,
3. Familiarity with regulation and compliance,
4. Unprecedented availability of expertise through both seasoned mortgage professionals and specialized business process outsource providers,
5. Web-based imaging tools that provide higher levels of efficiency and department collaboration, and
6. Availability of Fortune 500 technology that enables high-quality mortgage operations with less expense and hassle than ever before.
Increased Deposits

Following well-publicized failures of large thrifts involved in risky mortgage lending practices, individuals and companies began dispersing their capital, primarily moving their deposits from larger banks to smaller community banks that continue to follow conservative lending practices. This risk dispersion has increased the depository base of community institutions, beefed up their capital coffers, and made more capital available to customers needing residential mortgage loans.

Community banks offer a mortgage banking business model fundamentally different from that of pure play mortgage lenders. Depository institutions can rely on their depository capital to profitably fund mortgage (and other) loans, keeping mortgage loans on their books and servicing them as part of a diversely mixed customer product relationship. While government-backed lending programs established by Fannie Mae, Freddie Mac, and HUD provide liquidity, their guidelines can often be restrictive in today’s market. With growing depository assets, banks now have capital for more diverse, yet common sense mortgage lending strategies.

Conversely, for very large commercial institutions and mortgage banks, their access to liquidity has dried up. Private investment in mortgage-backed securities provided capital fluidity during the post 9/11 refinance boom and subprime phenomenon. However, with the collapse of private securitization, most non-agency secondary market outlets are now extinct.

As Federal Reserve Chairman Ben Bernanke observed at a Q4 2008 mortgage-related symposium in Berkley, “With the securitization market for private–label mortgage-backed securities shut down, Fannie Mae, Freddie Mac and Ginnie Mae are currently the only conduits through which mortgages can be securitized and sold to investors.” Self-capitalized community banks are well-positioned to fill the void for non-conforming loans.

Since community banks did not participate in subprime lending or other risky lending practices, the institutions are almost without exception in good shape. In addition, they are bolstered under the Emergency Economic Stabilization Act of 2008 that:

1. Temporary increases the Federal Deposit Insurance Corporation (FDIC) insurance limit on deposits from $100,000 to $250,000 through December 31, 2009;
2. Provides access to the Troubled Assets Relief Program (TARP) to purchase problem mortgage assets;
3. Allows them to take losses against ordinary income for Fannie Mae and Freddie Mac preferred share losses;
4. Offers benefits from SEC suspension of mark-to-market accounting rules;
5. Allows TARP to be used to assist community banks which suffered the most from losses on Fannie and Freddie preferred stock;
6. Prohibits future guarantee programs for money market mutual funds; and,
7. Allowed the Federal Reserve to begin paying interest on so-called bank “sterile reserves” beginning Oct. 1, 2008, three years earlier than previously permitted.

Today, community banks are better equipped to become profitable in mortgage lending, and their reputations are relatively unsullied. Although their depository model, which provides capital and dictates their regulated status, has largely led to their ability to adapt, reputation is their greatest competitive advantage.

Mortgage lending is a natural product for community banks, which tend to be well-known, trusted brands at a time when trust has become a significant industry business driver. Grounded in loyal local relationships, depositories’ reputations have the power to re-inject confidence in the mortgage industry, regain the trust of borrowers, and revive our home ownership economy.

**Accountability in Servicing and Originations**

Depository lenders view servicing as part of an end-to-end customer relationship continuum, holding it partly for risk management and partly to protect access to valuable customer profiles and metrics. Mortgage loan servicing is a key component to becoming a customer’s primary financial services provider.

During the heyday of large commercial banks and non-depository mortgage banks, loans for the most part were securitized, and often the servicing rights were “sold” as well. Ironically, industry metrics have for decades supported a direct correlation between servicing retention and loan performance. Historically, default rates of Fannie/Freddie loans that community financial institutions sold with servicing retained have been far lower due to greater institutional commitment and accountability for ongoing loan performance.
Community and regional financial institutions’ mortgage lending succeeds because of the
dynamic relationship between the lender and the customer as it applies to customer relationship,
profitability, and risk management strategies.

With each passing day, regulators are becoming more comfortable with a community-based
mortgage lending model that has natural risk firewalls and is less likely to impact the larger
economy. They also like the close relationship between community institutions and their
mortgage borrowers. Having acknowledged that third-party originations, a model used by many
non-depository lenders, can create additional default risk, regulators are now assessing the
appropriate pricing adjustments for loans originated by third-party brokers. Clearly, the broker
model is in flux, if not at risk. With established brands in their communities, community banks
need brokers far less than their non-depository competitors.

The ability to fund and service their own portfolios is a clear advantage of community
institutions. Since they are ultimately acting as the primary investors, community bank portfolio
lenders will become the most reliable source for non-conforming loan products. Community
banks will be able to serve the local real estate agent community and, when trust is proven,
brokers representing borrowers that may have:

1. Non-traditional income,
2. Less than perfect credit, and
3. Non-conforming properties.

Equity position, property condition and borrower ability to repay will mean much more to
portfolio lenders since they are inherently averse to making bad loans. The more unique the
terms are for a loan transaction, the more scrupulously it examines the deal to ensure common
sense applies to default risk.

Accustomed to Regulatory Oversight
In an exchange of mutual benefit community banks are better positioned to offer mortgage loans
in their communities because of their government regulatory oversight and mandate. As part of
the U.S. regulated banking industry, community banks:

1. Enjoy cost effective access to warehouse line capital at rates far lower than mortgage
   bankers (currently 1 – 3% vs. 5 – 6% plus transaction fees);
2. Earn profit while holding salable loans prior to sale, while pure mortgage banks lose profit based on spread;
3. May leverage capital by making, holding in portfolio and servicing loans, which do not have to conform to Fannie, Freddie, or HUD guidelines, at a profit;
4. Can, when appropriate, sell loans on the secondary market for fee based revenue allowing them to offer a broader product mix.

Whereas large community financial institutions once received preferred guaranty fees from Fannie Mae and Freddie Mac, being “too big to fail” now presents such an imbalance that regulators are assessing the advantages of dispersing the risk among a broader population of smaller institutions.

Community banks are understandably motivated to accommodate regulations and assign accountability. In fact, some regulators view these financial institutions as the last bastions of accountability in the mortgage banking industry. In the last decade, non-regulated lenders frequently sold risky mortgage loans to the secondary market, often assigning third-party servicing vendors and bundling loans into securities with little regard to risk. Those securities, bundled with minimal regulations, are now impacting investors worldwide with substantial defaults and principle loss.

Compliance and risk management are familiar concepts for depository institutions – an attribute that prevented them from succumbing to the subprime exuberance. Their longtime, if not lifelong, connection to their communities bears witness to their stability and judgment. Regulation is a friend of community banks, and has helped shape a more disciplined atmosphere where process quality is a point of pride.

Whether originated loans are kept in portfolio, sold as a conforming government-backed loans or sold to private investors, community banks apply consistently high quality processing standards. They require that all loan files be properly documented, underwritten, closed and shipped according to applicable compliance guidelines and assess lending guidelines with a common sense approach. These institutions understand the words audit, regulator and compliance with an intimacy unfathomable to less regulated, non-depository lenders.

New regulations on mortgage bankers’ origination practices emerged in 2008 when, in its new oversight capacity, the Federal Reserve Board approved final revisions implementing the Truth in Lending Act (TILA) and the Home Ownership and Equity Protection Act (HOEPA), both
aimed at protecting consumers from unfair lending and servicing practices. Revised RESPA requirements are also waiting in the wings.

The heightened need to track applications, initial disclosures and state broker licenses places a burden on mortgage lenders to monitor and report specific information about each origination, even if an application is ultimately denied. Since most lenders operate in-house systems built upon disparate loan origination processes not unified by a single database, there promises to be a flood of new issues for lenders.

Currently, there are a minimum of 18 unique compliance requirements specific to mortgage banking operations, and will increase at both the federal and state levels as government intervention penetrates the financial industry. Complex compliance requirements can tax even the most sophisticated community bank, demanding expertise, accurate data management, and operational reports documenting their compliance.

Nonetheless, regulated depository financial institutions are masters of understanding, implementing and tracking compliance. Basic mortgage banking requirements include:

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<thead>
<tr>
<th>Topic</th>
<th>Regulation(s)</th>
<th>Requirements</th>
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<tr>
<td>Tracking new loan applications and the action taken on them</td>
<td>Equal Credit Opportunity Act - Reg B (ECOA)</td>
<td>Clearly identifying when a loan application is taken. Typically, this includes one or more of the following: Credit data, debt ratio, property address or any discussion of available rates and terms. A decision needs to be made regarding the offering of credit within 30 days</td>
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<tr>
<td>Loan Closing Disclosures</td>
<td>Truth In Lending Act - Reg B (ECOA), Fair Credit Reporting Act (FCRA), Privacy Act, Home Mortgage Protection Act, Home Mortgage Disclosure Act (HMDA), Flood Disaster Protection Act (FDPA), E-Sign Act</td>
<td>Final Truth in Lending Disclosure, HUD-T Settlement Statement, Escrow/Impounds/Reserves Disclosure, Right of Rescission (For refineses)</td>
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<tr>
<td>Brokering Loans</td>
<td>Various state laws</td>
<td>Disclosures are required when the Lender is acting as a Broker. Information must include the fees being charged, when the fees are refundable, and the services being provided</td>
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<td>Hazard Insurance</td>
<td>Various state laws</td>
<td>Borrower must be informed that they have the right to select the hazard insurer of their choice, subject to the Lender's reasonable requirements</td>
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<td>Credit reporting access, disclosure, and tracking the sharing of reports</td>
<td>Fair Credit Reporting Act (FCRA), Fair and Accurate Credit Transactions Act (FACTA)</td>
<td>The regulatory guidelines require lenders to provide data from the credit reports to the applicant when credit has been denied. The disclosure and copies of credit reports must be archived for a minimum of two years. Notice must also be given that the Lender may provide negative credit information to credit reporting bureaus if the Borrower does not meet their obligations</td>
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<td><strong>Flood Zone determination, disclosure, and reporting</strong></td>
<td><strong>Flood Disaster Protection Act (FDPA)</strong></td>
<td>All federally regulated and/or insured lenders must notify prospective borrowers if the property they are financing is located within a federally designated flood area (SPHA). Properties located within a designated flood area have mandatory flood insurance requirements</td>
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<td><strong>Mortgage Insurance disclosure and termination requirements</strong></td>
<td><strong>Homeowner Protection Act (PMI Act)</strong></td>
<td>Lenders must disclose terms of mortgage insurance when provided to an applicant. Lenders must require applicants to have mortgage insurance based on specific equity/principal reduction guidelines</td>
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<tr>
<td><strong>Providing Appraisal Reports</strong></td>
<td><strong>Equal Credit Opportunity Act (ECOA)</strong></td>
<td>Lenders must provide a copy of the appraisal report used for underwriting or disclose that a copy will be provided upon request</td>
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<tr>
<td><strong>Predatory Lending and High Cost Loans</strong></td>
<td><strong>Home Ownership and Equity Protection Act (HOEPA), Section 32, State specific Net Tangible Benefits</strong></td>
<td>Borrowers must have the ability to repay. Refinances must be in the borrower's best interest, unnecessary insurance must not be required on a transaction. Special disclosures must be in place for loans with 8 percent or more in loan fees or if the rate is more than 8% higher than the comparable Treasury Security. Additional state, county, and city restrictions may apply</td>
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<tr>
<td><strong>State Licensing tracking</strong></td>
<td><strong>Loan Officer Licensing, Bricks and Mortar Laws, Continuing education</strong></td>
<td>Lenders are required to ensure their originators and third-party broker relationships are properly licensed with the appropriate physical office and educational requirements as established by the states in which they are lending</td>
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<tr>
<td><strong>Anti Terrorism and Money Laundering</strong></td>
<td><strong>USA Patriot Act, Office of Foreign Asset Control (OFAC)</strong></td>
<td>Lenders must obtain and document two forms of identification to validate applicants name, address, date of birth, and social security number to determine if the applicant is associated with terrorism and/or money laundering. Information must be archived for a minimum of 5 years</td>
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<td><strong>Loan Fraud</strong></td>
<td><strong>As established by US Department of the Treasury, Federal Bureau of Investigation, and State specific agencies</strong></td>
<td>Lenders are responsible for establishing and maintaining processes that validate the accuracy of data provided by applicants and the activities of their employees and third party originators relationships</td>
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<td><strong>HUD, Agency, and Investor Compliance</strong></td>
<td><strong>As established by the entities that set loan purchase/securitization requirements</strong></td>
<td>Product eligibility, price adjustments, verbal verification of employment, and product disclosures must be supported to ensure loans meet investor guidelines and are priced appropriately for income and risk</td>
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<tr>
<td><strong>Third-Party Audits</strong></td>
<td><strong>As established by FFIEC, HUD, and Correspondent Lenders</strong></td>
<td>Loan files (Pre and Post closing) should have random and independent validation of income, credit, asset, and collateral documentation as well as compliance processes/disclosures. Third-party service providers should have policies and procedures that support the requirements established for its customers. These policies and procedures should be validated with an independent SAS-70 report</td>
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<tr>
<td><strong>Reporting</strong></td>
<td><strong>Home Mortgage Disclosure Act - Reg C (HMDA), Community Reinvestment Act (CRA)</strong></td>
<td>Lenders are required to report on the credit provided to/denied based on Race/National Origin, Sex, Income, and property location</td>
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<td><strong>Protecting Your Customers Information</strong></td>
<td><strong>Privacy Act (Reg P), Sarbanes Oxley Act, Gramm-Leach Bliley, Red Flag rules</strong></td>
<td>Regulates the sharing of non-public personal information. Access provided on a “Need to know” basis. Data should be behind firewalls at all times. Employees should not have the right to remove data. Lenders must disclose their Privacy Policy and Opt Out option(s). Password policies must be implemented and maintained</td>
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<tr>
<td><strong>Data/File management, access, retention, and disposal</strong></td>
<td><strong>Various federal and state laws</strong></td>
<td>Data and images must be properly stored, made available for access, archived, and destroyed when appropriate. HMDA requires 3 years retention. PMI Act 3 years. Additional state laws may apply</td>
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**Abundant Expertise Available**

Limited access to mortgage banking talent and expertise previously inhibited the expansion of community banks’ mortgage operations. Less risk averse, more volume focused and profit-driven mortgage companies have for decades lured mortgage banking professionals with big money and the promise of even bigger opportunities. Community institutions that wanted to start or expand mortgage lending operations were rarely the job of choice for mortgage professionals who saw them as slow, conservative, tightly regulated and lower-income career destinations.

Now, with thousands of well-qualified mortgage banking experts needing career adjustments, community financial institutions are well-positioned to explore aspects of mortgage lending previously avoided, partly due to lack of know-how.

Although community banks today focus heavily on portfolio lending, in most instances they are not prevented from establishing relationships with investors, and selling qualifying loans to them.

Most community institutions steered their mortgage operations away from the secondary market, including the relatively safe government-sponsored entities (Fannie Mae and Fredddie Mac), FHA, and VA products. However, in light of severe staff cullings at non-depository mortgage banks, community banks now have access to sharp investment skill sets, enabling them to expand mature mortgage banking objectives and become active in selling servicing rights for conforming loans and expanding their non-conforming mortgage business.

To compliment employee resources, many banks have now elected to outsource some mortgage lending activities. New outsource service providers can help regulated depository institutions by reducing costs and improving service. Community banks may elect to outsource elements of their mortgage lending operations to facilitate speedier market entry, improve borrower service, and support compliance and risk management. They will also discover that outsourcing delivers cost savings – a consideration not always appreciated by independent mortgage bankers who cared less about risk and more about how to “pump up the volume” in a growing market.

Outsourcing covers mortgage lending activities that could range from managing the entire loan process via call centers and/or web sites, to diverting specific activities such as tracking loan conditions, reviewing documentation, and uploading images or data. Other process opportunities and their advantages include:
1. Appraisal ordering: reduces the ability for the originator to influence valuation;
2. Title report order/tracking: validate that service and quality objectives are met;
3. Employment verifications: requires both written and verbal;
4. Loan Underwriting: objectivity;
5. Closing document preparation/signing: pure process orientation;
6. Loan shipping: timeliness and accuracy;
7. Post closing document tracking: shaves incremental erroneous costs;
8. Post closing audits: “fox can’t guard the chicken coop.” Third-party objective audit are expected from senior management, HUD, and secondary investors. Institutions cannot independently assess quality control problem if the institution does not have the expertise; and
9. Loan servicing: Higher levels of customer support and effective reporting.

While recent additional requirements from the Federal Reserve Board increase the complexity of mortgage banking, existing compliance mandates are not adequately supported by traditional Loan Origination System (LOS) platforms. In truth, the renewed interest in loan processing procedures and compliance could not have come at a more opportune time for depository institutions that want to grow their mortgage lending acumen. Community lenders have never had what they really needed to support the complexities of loan processing. Small to mid-sized community-based lenders with volume between 20 and 500 loans a month are primarily interested in attracting and serving borrowers with whom they have longstanding depository relationships. In many cases the institution’s staff wears multiple hats, and mortgage expertise is spread thin.

Community banks differ from large commercial banks and mortgage banks in that they lack both resources and the single-minded focus to buy or build the systems needed. The required systems should trigger hard stops in the process to ensure data is gathered, reviewed, and the appropriate activities are completed to ensure profitability and compliance. But community banks are in a better position than ever to build successful mortgage lending operations thanks both to market opportunities emerging in the wake of the subprime crisis and loan processing systems that virtually eliminate traditional problems with loan technology.
Technologists for Hire

An increasingly popular form of Fortune 500 business outsourcing has also demonstrated its value and relevance to community-based mortgage lending – the practice of outsourcing technology. In its earlier incarnation, technology outsourcing fell under the terms application service provider (ASP) or “thin client server.” These models effectively shifted some of the more onerous technology functions to a central facility where software updates, administrative permissions and system patches were managed.

Recently, perhaps as far back as a decade ago, business process visionaries began developing web-native business process automation platforms that could be accessed via an Internet connection and managed by subscription to a meet a contractual service level agreement (SLA).

For the same reason that most institutions do not implement or support independent merchant account and credit card processing services, community and regional banks do not typically benefit from supporting an in-house technology staff in order to use mortgage lending technology. With today’s web-based systems, lenders have the ability to obtained fully hosted services and compliant services for a fraction of the cost of an independently managed system.

Whether tapping newly available mortgage professionals or outsourced services, processes or systems, community banks are in the enviable position of being able to take from the cream of the crop to build their operations.

Document Imaging and Management Support Compliance

Effective document imaging and management has recently become a requirement rather than an option. When properly implemented, imaging provides the hub for all employee and vendor collaboration. Additionally, it significantly streamlines all phases of the life cycle of mortgage lending. Documents from borrowers and service providers arrive in many formats and via multiple channels. Assembling and conveying a qualifying and compliant loan file requires the lender to serve as a clearinghouse for information requests, a destination for information delivery and a global traffic manager.

In most instances, a loan file combines both electronic elements (such as an online application or electronically transmitted appraisal) and copies of physical documents (such as pay-stubs or bank
statements). Requesting, updating and managing documents in multiple formats in a single loan file creates opportunities for errors and omissions that threaten compliance and quality lending practices. The solution is a soup-to-nuts imaging solution that allows all documents to be imaged, inserted in an electronic loan file and managed throughout the life of the loan with automated business logic.

For maximum benefit and reliability, imaging must be imbedded in the loan process from the start, must provide a repository for all documents, and must be accessible by all parties performing services on a loan transaction.

The ideal system allows every participant in the life of a loan, including the borrower, to contribute images. It also endows the system administrator with tools to provide loan file access and image upload permissions to specific roles associated with the loan process. These roles may be customized to support internal staff, outsource service providers or third-party vendors, depending on loan status. Document image additions will trigger workflow, while their absence will curtail the process.

With a completely image-enabled loan file, specialized teams of staff or outsourced service providers, either domestic or offshore, can seamlessly work together with remote originators and production branches. Further, image-enabled lending processes are by nature “greener” (have less environmental impact) and faster, and lend themselves to greater accountability and process visibility.

Institutions that sell some of their loans on the secondary market can significantly improve the delivery of investor files through document imaging and management solutions. These include services such as data and quality control reviews for documents received, data input into the LOS application, and linking incoming images to the specific status items/loan conditions.

Mortgage operations can benefit from the interconnection between compliance, outsourcing and imaging by processing loans on an end-to-end enterprise mortgage lending platform that is image-enabled, securely hosted and kept current by mortgage lending experts.
Lending Automation Options

Lenders may elect to build or buy the technology components, although mortgage banking LOS systems and enterprise lending platforms generally available in three distinct variations. The typical variations include:

1. Network-based applications. These systems allow users to work together within an office network. This requires local installation, setup of tables, and regular maintenance.

2. Web-based applications. These systems allow users to have multiple locations, collaborate in one centralized database hosted by the lender or a third-party vendor. This type of system may be hosted by a third party but typically requires the lender to set up and maintain the tables and rules for the application.

3. Software as a Service (SaaS). These systems allow multiple users to collaborate in one centralized database and are hosted by a third-party vendor. The benefit of this service is that the system tables and business rules are preconfigured and supported with best business practices so lenders can easily support complex business processes.

Although SaaS is web based, it is fundamentally different from earlier web-based models such as the application as a service (ASP) model. The ASP model is typically just an out-of-the-box solution hosted by the vendor with greater security and easier implementations – offering no compliance support or expertise in mortgage lending processes. It’s just cheaper.

Systems hosted by in-house servers, while the most common, are the most outdated. They are only as secure as the server where they reside, and only as reliable on crucial compliance details as internal management expertise allows. When an institution hosts and manages its loan origination system in house, the margin for error is in direct proportion to how broadly its resources are spread. Lenders need to be aware of those limitations.

Software-as-a-Service: Changing the Game

SaaS, which offers fully hosted, Internet-based, on-demand technology, can be used to manage the loan-origination-to-loan-reconciliation lifecycle. Additionally, for a fraction of the cost, SaaS can provide community banks with automation on par with that used by Fortune 500 lenders.
SaaS is a software application delivery model where a software vendor develops a Web-native software application, then hosts and operates (either independently or through a third-party) the application for use by its customers over the Internet. Customers do not pay for owning the software itself, but rather for using it. The software vendor generally manages updates to the software, and can turn various modules on or off depending on an institution’s particular need.

SaaS vendors often provide a higher level of support and service than vendors using the earlier ASP model, in which the application is simply hosted by the vendor who has licensed the program. For example, operating in the SaaS environment, institutions can identify when and how they receive updates for complex processes such as loan disclosure or compliance updates.

Advanced SaaS providers are fully-hosted, Internet-based, on-demand loan systems that can:
1. Deliver best-of-breed tools;
2. Reduce the need for in-house loan technology support staff thereby eliminating implementation and training hassles;
3. Cut system costs (because of reduced support costs and because only smaller usage or transaction fees are charged); and
4. Help institutions provide high levels of service.

**Putting the Pieces Together**

Fully integrated SaaS mortgage solutions that are updated and maintained on secure, redundant servers provide service and performance guarantees that only the largest financial institutions can afford. But the beauty of a SaaS system is that institutions with mortgage operations can choose several—or all—of a vendor’s available modules. Ten core mortgage business elements must be fully integrated and automated to create a best practices enterprise mortgage lending system. These are:

- **Marketing**: Providing product, service and company information to prospective borrowers;
- **Point of sale**: Gathering borrower information and delivering an automated response;
- **Loan origination**: Managing loan, borrower and property data, as well as providing general status reporting, loan calculations, and standard mortgage forms;
- **Vendor/contact management**: Managing and communicating with providers of external data, such as mortgage insurance, flood determination, appraisals, credit reports, underwriting, title reports, and fraud detection;
? Documents: Generating applications, upfront disclosures, business processes, and closing documents;

? Loan program: Handling interest rate and fee distribution along with program qualifications;

? Automated loan underwriting: Imbedded business rules identify what is required to process and approve loans based on the borrowers credit, income, assets, and property data;

? Loan income/expense tracking: Lenders must have business logic to default and track the appropriate transaction fees, deposits, and third-party income/expenses to identify loan level profitability;

? Secondary marketing: Maintaining and reporting investor relationships, tracking income and costs for base price, price adjustments, servicing premiums, and impounds;

? Centralized reporting: Handling loan delivery, year-end fee reporting, and Home Mortgage Disclosure Act reporting for loan application disposition; and

? Imaging: Capturing and managing data with a complete centralized process, including softcopy delivery to investors, and archiving to meet regulatory compliance mandates.

In short, SaaS helps businesses focus on their core competencies and profit drivers while allowing expert providers to supply the information and technology component. Business process automation outsourcing, SaaS, offers important advantages – primarily technology expertise specializing in mortgage lending processes.

Community banks that want to offer mortgage lending services have been, and will continue to be, the “early adopters” of business process automation outsourcing. Although non-depository mortgage banks may have viewed best practice SaaS services as too restrictive to provide a competitive advantage and may have distrusted third-party data management, their existing systems failed to eliminate the funding of “borderline” loans.

**SaaS Selection Criteria**

When selecting a fully hosted, on-demand mortgage lending solution, community institutions must ensure that their existing staff can understand, implement and, most importantly, control the technology and associated data. The key technology concerns facing community institutions are implementation, compliance, security and maintenance. Community banks contemplating
creating or growing mortgage lending operations should consider the following criteria when exploring their technology options:

**Implementation:** Solutions that require more than 60 days to fully implement are not only quite costly, but are also exponentially more likely to fail.

**Compliance:** An automation strategy must include data integrity checks that make sure data entered makes sense, access to historical data (ability to identify when and what data was changed), and configurable security rights for various users based on the status of a loan record. Additionally, rules-based disclosures should be provided on loan terms, changes to the annual percentage rate, and mortgage insurance.

Data collection requirements for key activities, such as printing, interfaces, dates, closing docs, must be driven by business logic rules based on user roles and loan status. Users should be assigned system rights that permit a user to accomplish specific activities within a shared data environment.

**Maintenance:** Systems should be designed to require an absolute minimum of support for regulatory and functionality upgrades. The lending industry requires a constant technology and systems vigilance to ensure that loans are properly originated, approved, and closed within the guidelines established by Federal, State, HUD, and investor specific requirements.

**Support and Training:** Systems should simplify the administrative and user support processes. Advance systems provide the ability to reach dedicated support specialists familiar with the system functionality and mortgage industry standards. Training should be available on demand or on a regular basis on via online tutorials, videos, or classroom webinars. This allows lenders to identify and expand usage of existing system features and quickly implement future tools and services.

**Security:** Documented and proven controls are becoming more critical as threats and new government mandates evolve. Service providers should have third-party audits such as a SAS 70 to ensure controls are implemented and followed. Controls are needed to address software development, system support, and physical security. These generally include access, climate control, redundancy, disaster recovery, and business resumption. Additionally, internal controls must also deal with network/data security, including encryption, authentication, and data integrity based on user roles and loan file status.
Conclusion

In summary, community banks have an open door to restoring their primacy in mortgage lending. With the demise of non-depository mortgage banks, both homebuyers and existing homeowners seeking refinances are looking for dependable and honest lenders. Community banks would be well advised to make the most of their many advantages to meet this demand.

Capitalization from depositors provides a funding source that their mortgage banking competitors lack. Community banks boast responsible yet effective originations and servicing divisions, and they are well versed in operating in highly regulated environments like mortgage lending. While mortgage banking veterans are waiting on the sidelines, ready and willing to offer their skills, outsource providers are also prepared to provide their specialized services. Community banks can use imaging tools, capable of integrating document images from many sources and in multiple formats, to enhance collaboration among staff outsource providers.

They can also draw on the cost effective abilities of SaaS to tap best-of-breed tools to provide first-class service without an in-house technology staff. When considering a technology platform, the lenders must seek one that their employees can understand and control. Lenders should be able to set up the system within a reasonable timeframe, and the system must complete data checks throughout the loan process and must feature adequate levels of maintenance, security, compliance, and support and training. Community banks should also check if the technology vendor has completed successful implantations for other lenders, especially community banks like themselves. When community banks follow these steps they will be on the road to growing their market share of the single-family real estate finance business and solidifying their role as the customers primary financial institution.