Getting the Design Right Before You Adopt an LOS

By Lionel Urban

In technology, we use the term "architecture" in pretty much the same sense it is used in constructing a building. Careful engineering goes into preparing a project, consisting of many steps that will result in a solid design that can be created to last for years. In the construction industry, nothing is more important than the foundation, as the entire structure depends on a solid base. The same is true in the mortgage industry, and the most important component of a lender's success is the loan origination system, the LOS.

One notable building that has been in the news lately is the pricey condominium in San Francisco, the Millennium Tower. *The San Francisco Chronicle* reported in August, "The Millennium Tower, a leading symbol of San Francisco's new high-rise and high-end living, is sinking—setting the stage for what could be one of the most contentious and costly real estate legal battles the city has ever seen." The units range from $1.6 million to $10 million-plus, and are owned by the likes of Joe Montana. Incredibly, the building has sunk 16 inches and taken on a northwest tilt of two inches, which is potentially disastrous given its 58-story height. It is hard to imagine a building constructed to rigid California earthquake standards suffering such a foundational problem, but there it is. And it's a vivid illustration of the importance of getting the design right before you adopt.

Homework is required

For lenders of all sizes, the choice of an LOS is a major decision that impacts everyone in the organization, from ownership and senior management all the way to the most junior members of the team. The effects of the right choice can last for decades, and a poor choice can have adverse effects lasting three to five years or more, depending on how quickly action is taken to correct it. The process can be complex and one that requires significant reflection. Do you take the safe choice that many have followed? Do you buy into marketing hype and publicity that might mask shortfalls in real functionality? Do you approach the decision with sufficient due diligence and analysis? No doubt about it—homework is required, particularly in at least five key areas:

- Components–features and functionality
- Vendors
- Resource requirements
- Vendor strategy
- Price

Components

This is the obvious place to start when considering an LOS, just as features and equipment would be the best starting point when looking at a new automobile. Understanding the essential components includes gaining knowledge and insight on basic items like the point of sale capabilities (does the system handle retail only, or can it also provide the lead management and follow up required for the consumer direct channel?) The LOS must be intuitive, flexible, customizable and completely reliable. The back office operations have to be fully supported and based on best practices across the industry—which means the system was designed not just by technologists, but by mortgage professionals.

Imaging has become essential over the last few years, and all imaging systems are not created equal, especially when it comes to time-consuming steps like document recognition and classification. And reporting is also critical, given the unavoidable climate of regulation; it's not a matter of if a company will be audited by someone, it's when. So in addition to full management reporting on an everyday basis, it is important that lenders have reporting capabilities that let them be fully transparent when auditors arrive. One of the best ways to feel comfortable about the components is to include your company's operators in the evaluation process, not merely the tech staff.

Vendors

No lender can operate without third-party vendors, so the LOS has to be able to include them in the technology environment. This is accomplished with integrations, a process that has vastly improved over the years, but is one where gremlins delight in creating problems. Does the LOS already have a working slate of vendors integrated, and is it simple to seamlessly integrate the lender's preferred vendors? Are data and document exchanges efficient and trouble free? Can items like appraisals and verifications be ordered automatically or with minimal human intervention? Can incoming data from documents like automated valuation models (AVMs) and credit reports be interpreted without having to put eyes on them?

The answers to these and related questions should not be assumed, especially with changes in forms and formats on the horizon for the coming year. Data streams are amazingly reliable, but when variations come in, they must be detected and dealt with in order to avoid defects that affect closings and post-funding reviews.

Resource requirements

The days of having to have large IT staffs is long gone, thanks to

the future of mortgage banking

tremendous advances in LOS architectures and cloud-based delivery. But implementations and conversions from one system to another are not trivial processes. It is important to have a real-world understanding of how long it takes to get a new system up and running, and the LOS provider will have metrics to lay out an implementation schedule, as well as existing customers to speak with. Lenders will want to know about the support capabilities of the LOS company, as well as the expected maintenance and who will provide it.

Customization is important when buying a new car—but it's absolutely critical when looking at a loan origination system. Lenders have different ways of doing things, and though the best LOS come with best practices presets, it is vital to be able to set things up the way you want them, according to your rules.

Vendor strategy

Speaking of rules, lenders want the flexibility to follow their preferred strategies on everything from the origination channels they serve to collaborations with business partners. Being able to refine workflows to make that happen means having rules-based systems that are not only flexible, but also easy to modify. Rules engines are like automobile engines—some are easy to work on and others are mystifying. You are likely to want rules systems that don't require an IT person to set, just as you don't want to be hampered by templates that are restrictive.

Different business channels have different requirements, so depending on whether your company does retail, wholesale, correspondent, consumer direct or any combination, your LOS will have to support the channels. You might be surprised to learn that some systems are stronger in one area than another, but it's quite true. It is wise to have your due diligence team include a representative from each business channel in the evaluation process.

Our industry has become more collaborative than ever over the last decade, with strategic partnerships and mutually beneficial alliances have becoming the standard operating procedure. These increasingly close ties among vendors, partners and collaborators mean that data sharing and bi-directional information flows can cause additional complexity on the tech side. How well does the candidate LOS play with others? Perhaps more importantly, what do the collaborative players have to say about the provider's ease of use when sharing information? And what measures are taken to ensure security for all parties on sensitive borrower information?

Price

The industry has learned that price isn't the only thing any longer, but it's still obviously important. The four main cost categories to be concerned about include implementation, recurring fees, customization costs and maintenance burden.

Cloud-based solutions have the benefit of being less expensive to implement, but there is still time, effort and hard cost involved. Installed systems are better for some companies, particularly if they already have significant IT staffs, but most lenders are finding that Software-as-a-Service (SaaS) is the more attractive choice. Recurring fees are to be expected, as technology this complex needs some care and feeding to keep it at peak performance, but providers vary widely on this. Some rely on the vendor, some emphasis staff members, and others blend the two in specific roles. It's an important area to research and understand completely, with written schedules provided for all recurring fees.

Customization also comes with a cost, and it is important to consider the role of architecture here. Some systems are designed to be more readily customized than others. And while some are easy for the lender to customize, certain features will always require the vendor's involvement. Age is also a factor to some degree; older systems may cost more to customize, even if they seem to be lower in cost up front.

Finally, never underestimate the power of existing client input. Legend has it that a casual observer at an auto show in 1900 asked the fellow next to him, "Is that Packard car a good one?" The man, who happened to be J.W. Packard himself, replied with "Ask the man who owns one," a suggestion that became one of advertising's most iconic lines. It's also great advice. LOS providers will make available customer retention rates, satisfaction surveys and other metrics that will aid in the lender's decision. But it always a great idea to speak with multiple users directly—and in several disciplines, including sales, operations, QC, IT and management.

There is much to consider when looking at options in loan origination systems, but there are also tremendous benefits to be gained by making an informed choice. The LOS is the foundation for any originator's business, and there is much to be learned regarding what is evident both above and beneath the surface—if the time and energy is invested.

Lionel Urban serves as CEO, founding partner, and chairman of the board for PCLender LLC, responsible for the overall strategic direction and the vision behind the technology development of the company. Since 1987, Lionel has acquired vast mortgage banking experience in management, origination, operations, secondary marketing and compliance roles within banks, credit unions, and independent mortgage bankers.