Building an Intelligent Operational Framework for Mortgage Processes

Abstract

As the regulatory landscape keeps evolving, managing compliance risks will be a key priority for lenders. New and amended regulations put undue pressure on mortgage firms' ability to respond to changes and also drive up the cost of compliance, increasing the overall OPEX. The cost to originate a mortgage loan has been increasing steadily since 2008 – growing by 48% by 2017.[1] Compliance risk emerged as the top primary risks among Matters Requiring Attention (MRA) as per the June 2017 OCC report for large banks. Although the current US administration promises of relieving regulatory burden, the reforms process has been slow.

Given the scenario, how can mortgage firms comply with stringent regulatory standards while controlling production expense and minimizing enforcements? This paper explores the challenges faced by lenders and proposes scalable solutions for automating core operational processes.

The Regulatory Landscape is in a State of Perpetual Flux

The mortgage business landscape has been in a state of reorganization over the last few years as a result of the new regulations introduced through the Dodd-Frank Wall Street Reform and the Consumer Protection Act. Lenders now find themselves in a tight spot between meeting stringent reporting requirements and controlling the spiraling OPEX.

This situation is likely to become more complicated with the recent amendments to the Home Mortgage Disclosure Act (HMDA) and the TILA/RESPA Integrated Disclosure (TRID) rule over FY 2018-19, which mandate additional reporting and tracking conditions.

Some of the key regulations that might have an impact on the way mortgage firms function are:

- **New mortgage servicing rules (Regulation X and Z):** Mortgage servicers will need to provide periodic statements for each billing cycle as well as upfront ARM notices at least 60 to 240 days prior to payment due date. In addition, they will have to instantly credit payments upon receipt from the borrower, provide payoff statements within seven business days of a request, provide special protection to delinquent borrowers with loss mitigation options, and abide by a 120 days prohibition on foreclosure initiation. These changes came into effect in October 2017.
- **HMDA amendment:** January 2018 onward, lenders will have to report 48 data fields, which include age of applicants, points and fees payable at origination, rate of interest, prepayment penalty terms, loan terms and loan tenure, value of property, debt-to-income, origination channel, applicant credit scores, among others.
- **TRID rule and amendment:** Lenders will have to share a written loan estimate and closing disclosures within stipulated timelines. It also delineates zero tolerance in fees and costs levied in initial estimate and closing disclosure. The new amendments require the inclusion of tolerance provisions for the disclosed total of payments, exemptions for certain housing assistance loans, and guidance on sharing of disclosures with third parties.

In response to these changes, mortgage companies are required to introduce additional checks, which means they need to expand their workforce and strengthen internal training and quality assurance programs.

What Mortgage Firms Must Do to Stay Profitable

It's time mortgage firms devise an operational strategy that ensures compliance while being cost neutral. This would mean embracing digital solutions, and creating and establishing agile and efficient processes and systems in line with business and regulatory objectives. We see two broad areas where changes will need to be made. These are:

Technology and process related enhancements

Use machine learning to improve efficiencies

For starters, enterprises need to revisit traditional quality check methods that require a loan file to be reviewed by multiple members within the loan processing team before getting clearance. While this ensures relatively fewer errors, the number of checks has a proportionate impact on the cycle time and cost per loan. Here, a machine learning enabled quality control and assurance review framework (see Figure 1) can be implemented to limit the need for human intervention to troubleshoot complex or escalated issues.

The biggest advantage such an approach will bring is the ability to process multiple requests with high precision and faster turnaround time. The system will also have the flexibility and adaptability to learn from new data sets and provide outcomes aligned to compliance requirements. Such an application will have a toll gate-based compliance testing—wherein the file goes through compliance checks for pre-defined toll gates within the loan processing lifecycle.

This standalone compliance application will communicate to the lender's loan origination software (LOS) or servicing platforms through APIs to fetch the required compliance data from different, relevant databases. The built-in machine learning

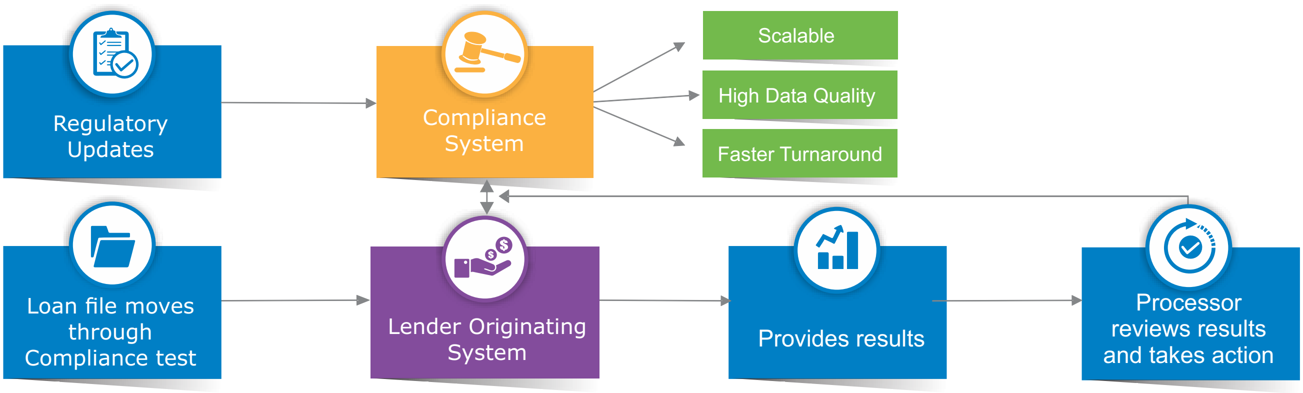

Figure 1

algorithm can be used to customize this application per the lender's or investor's requirements. Such intelligent systems will have the flexibility to add new scenarios, such as regulatory changes, and learn to process the compliance checks accordingly. This will also have a robust testing environment framework to ensure changes are implemented correctly and quickly before being put into a live environment.

Automate processes

Government sponsored enterprise such as Fannie Mae have used technologies to reimagine loan origination, processing, and closing. These can also play a pivotal role in terms of making compliance proactive and reducing risk exposure (Table 1).

People and organizational culture changes

Improve employee compliance quotient

As the number of regulations increase, so do the complexities

	As Is Status	To be Status
Workflows Automation	Present workflows do not support a structured approach to look at compliance requirements during the loan origination process. The checks are people driven rather than being process driven. There could be potential road blocks if the inflow volume is higher than the intake capacity.	Workflows to be designed with compliance checks scheduled for important milestones of loan application. By leveraging APIs, these checks (ATR and QM, HMDA, HOEPA, TRID, investor guidelines, and so on) can be automated to take appropriate actions based on results. This solution provides flexibility to scale up. Any exceptions in the compliance results can be corrected by the staff.
Platforms and Applications Integration	LOS and compliance systems operate separately and only partially integrated. Processors have to still enter critical details such as points and fees, NMLS details, ratios, and so on to get results.	API ensures complete integration of LOS and servicer application with compliance systems. This will lead to seamless data flow, maintain data integrity, and efficiently process compliance tests.
Dealing with Borrower Requirements	Document collection, conditions clearance, and borrower communications are manual with email/ fax/ papers. Regular follow-ups required.	Integration of sender or Servicer back end systems to a web-based frontend interface or mobile applications using APIs will provide real-time update to borrowers on compliance requirements and prompt them to take actions.

Table 1: Technology-led Reimagination of Mortgage Operations

associated with compliance. Organizations need a well thought out learning strategy to improve and effectively manage their workforce compliance quotient. The learning modules should not only decode the regulatory requirements but also delve upon the impact on daily operations across the loan fulfillment lifecycle and the proposed steps to ensure compliance.

Mortgage firms with a higher learnability quotient in compliance can thrive and build a robust framework to comply with regulatory requirements. This will require:

- A case study repository which can help team members gain hands-on experience in dealing with different complex compliance transactions. Creating a test environment which hosts a repository of compliance scenarios provide an in-depth view of various nuances to manage different scenarios.
- A periodic refresher training and certification process around existing and new compliance requirements to help team members stay abreast with changes in the regulatory landscape.
- Collaboration across multiple communities within the mortgage ecosystem for sharing best practices, insights, and more. This will help identify gaps in existing processes and applications and take corrective actions as required.

Toward an Intelligent Future

Scrutiny coupled with increasingly stringent compliance requirements will continue to govern lending processes and how the mortgage industry manages them. Manual methods for ensuring each process – from origination to closing – adheres to prescribed guidelines are difficult to scale up.

These companies will need to continue growing is a framework embedded with intelligent automation for managing repetitive, rule-based tasks. It will ultimately help reduce cycle time, ensure effective quality control, and more importantly, enhance borrower experience.

References

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