



MortgageCadence[®]

Enterprise Lending Solutions

Industry Insight: Investor Driven Conduit Programs



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Investor Driven Loan Conduit - Ensuring Loan Quality in Today's Market

In today's highly regulated mortgage marketplace, lenders and investors are acutely aware of the risks associated with the origination of loans that do not meet strict compliance standards; specifically, the exposure to repurchase risk from investors and/or insurers, federal and state regulatory inquiries and audits, as well as the ever-present potential of civil litigation. This is especially true for third party originations. Traditionally, lender and investors have had little control over the quality of third party originations exposing each to even greater risk.

Challenges:

The focus on loan quality has the industry abuzz on which industry participants are best suited to shoulder the necessary level of risk to ensure products are originated in a responsible manner without limiting access to credit. The ability to track the performance of a loan will create a world where a lender's success is driven by their ability to consistently produce and deliver quality products to the Secondary Market.

The traditional practice of sampling loans is fundamentally flawed. Trading Desks, Credit Rating Agencies and Insurers must rely upon this sampled loan data to make very important decisions. The industry must have all of the necessary data points from each individual asset that comprises the requisite securitization collateral to price, rate and ensure adequately. Investors must challenge the traditional role of due diligence and bring control back to the beginning of the lending process with a focus on the lenders ability to ensure that every loan meets each objective element to which the loan is underwritten.

It is time for Investors to take advantage of "Service Providers" and their dynamic technology solutions and take back control, as opposed to figuring out a way to make their business processes work within the current third-party origination process. Investors need to embrace "Service Providers" that can individually configure workflow tools combined with a rules-based underwriting engine to effectively provide a built-in quality-control solution for lenders and investors that will identify credit, collateral, compliance threshold, tolerance and guideline violations as well as any potential fraud-pattern recognition **prior to origination and funding of the loans.**

Solution: "Investor Driven Loan Conduit delivered by Service Provider"

This concept permits TPO's to originate, underwrite, and submit the fully underwritten package to a Service Provider for verification/validation/issue remediation. Once the vendor verifies that the loan meets the Investor's guidelines, the Investor gives a "clear to close" and "funds" the loan.

The key need in this type of platform is the Service Provider must have a "rules based software platform" with the necessary "underwriters" to manually re-underwrite the loan to verify that the TPO meets all Investor Guidelines.

Mortgage Cadence is perfectly positioned to balance the lending needs of the borrower with the demand for loan quality from investors. They have the mortgage banking experience, loan processing center staffed with experience underwriters, dynamic technology solutions, and expertise to successfully deliver on this Investor Driven Loan Conduit program.

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For Investor Driven Conduit programs to succeed there must be a clear “reporting mechanism” for the Investor to monitor real time pipeline reports, and “a results report” necessary for “clear to close” and “clear to fund”.

Leveraging the proper Service Provider solution can significantly reduce institutional and loan-level risk by ensuring compliance with loan credit, collateral guidelines and regulatory compliance requirements while reducing overhead through the operational efficiencies a smart platform can create.

The Mortgage Cadence Fulfillment Center with dedicated highly qualified underwriters is capable of fully underwriting over 200 loan files a day, with the ability to send and receive document packages, electronically or via commercial carrier. They also have real time access to collateral data, including appraisals, for remote desk reviews during the underwriting process.

The Mortgage Cadence solution contains rules-based underwriting tools with configured workflows that “lock down” data to ensure the necessary credit, collateral and compliance requirements are met as the loan progresses through the origination process.

The Mortgage Cadence rules-based underwriting system is a preconfigured underwriting engine that has built-in calculations and threshold validations to enforce the specific investor or product-specific guideline requirements. This system automates the traditionally manual processes associated with loan underwriting. It transforms worksheets into objective electronic calculations, memorialized in an electronic format that will be archived with the originator in anticipation of electronic audit delivery and passed on to the ultimate Investor as part of the entire closed-loan file.

Investor Driven Conduit programs from Mortgage Cadence allow investors to take back control and ensure loan quality.

The Mortgage Cadence system is locked down to ensure that no single individual lacking proper administrative authority may alter or amend any credit, collateral or compliance data in an attempt at subterfuge. This locked-down process restricts any deviation from, or violation of, guideline requirements (intentional or unintentional) as the loan progresses through the underwriting process, delivering a loan that has met all specific guideline elements.

Workflows automate operational task progressions that not only drive the route of the loan through the origination process, but specifically permit and restrict user access to particular data fields based on the lender’s workflow. Further, these tools automate the ordering of service providers (i.e., appraisal, title), automatically task specific users with single or multiple responsibilities and, most notably, escalate credit, collateral and/or compliance issues for review when specific tolerances fall within a preset risk range.

Workflows may provide for secure uploads directly from borrowers or third parties (i.e., banks, employers), thus reducing manual processes and eliminating errors, lost documents and fraud potential. The use of secure direct uploads when used in conjunction with optical character recognition (OCR) software creates a second level of data referencing and data validation for increased accuracy while permitting upstream risk-management reporting to senior management through a transparent, real-time reporting process.

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Mortgage Cadence includes workflow tools combined with a rules-based underwriting engine to effectively provide a built-in quality-control solution for lenders and investors that will identify credit, collateral, compliance threshold, tolerance and guideline violations as well as any potential fraud-pattern recognition **prior to origination** (*Please See Appendix A – Dry Funding Conduit Workflow*).

A comprehensive quality-control program consists of more than merely identifying violations. It consists of the preparation for audit and ensuring that each loan file contains all necessary documentation to support underwriting decisions.

The ability to electronically archive vital asset and income documentation to prevent lost or misplaced paperwork is extremely important to support a defense to a claim by an auditor that the underwriter did not properly validate a vital income or asset element. For example, the Federal Housing Administration (FHA) recently implemented measures to increase monitoring of lender performance and compliance with FHA guidelines/standards and plans to publically report lender performance rankings to improve transparency and accountability. Areas of particular concern for FHA lenders (based upon recent audits by the Department of Housing and Urban Development [HUD]) must be addressed in a way that guarantee that the underwriting tasks will be fully completed and documented; such as validation of source of funds to determine a borrower's ability to repay and documentation of compensating factors for loans with low qualifying ratios.

These required processes that traditionally consisted of manual assessments have been memorialized on worksheets and supported by documentation provided by the borrower's employer, bank or asset manager. Should any of these worksheets or supporting documentation become lost or removed from a hard loan file, the lender will have a difficult time defending against a claim by the regulator. Automating these processes and electronically archiving the calculations and supporting documentation permits an originator to eternally provide proof tasks were completed, calculations were done and evidence was obtained.

The Mortgage Cadence solution focuses on a quality-control plan with the necessary automated controls to guarantee guideline compliance during underwriting. This will permit the reallocation of ineffective manual quality-control overhead toward revenue-increasing efforts to increase profitability and deliver real-time data on 100 percent of loan production that moves into the secondary market.

The beneficiaries of this direct data delivery will be those that have significant interest in overall loan quality, such as investors with skin in the game, rating agencies, credit-risk insurers, independent third-party diligence firms, and federal and state regulators.

Technology that provides an automated rules-based underwriting solution, with preconfigured workflows that restrict the progression of the loan without the fulfillment of specific conditions is reinforced by secondary data validations to effectively create an electronic underwriting file and an auditable trail detailing accountabilities and their ultimate fulfillment.

Investor Driven Conduit programs from Mortgage Cadence allow investors to take back control and ensure loan quality. This is the first step in creating an origination process that will produce loans that meet all investor and regulatory requirements. In turn, this will reduce the lender's exposure to put-back risk as well as meet all regulatory burdens it faces as a regulated entity.

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