



MortgageCadence[®]

Enterprise Lending Solutions

Compliance Insight



CURRENT STATE OF THE MORTGAGE MARKETPLACE - 2010

The past year has seen significant changes within the Mortgage Industry, many of which have forced lenders to make drastic process modifications to their origination platforms in an effort to meet essential compliance requirements. The burden on lenders (fiscally and operationally) has taken a toll as they seek to meet the overwhelming demands of regulatory agencies and investors. In order to regain control without increasing costs and lowering overall margins, lenders must reassess their business operations, identify areas that expose them to the greatest risk (such as the new RESPA requirements) and ensure that their platform has the necessary controls in place to originate compliant products.

CHALLENGES:

In today's highly regulated mortgage marketplace, lenders 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.

For example, FHA has instituted a "zero tolerance" enforcement policy, not only removing origination and underwriting authority from lenders, but imposing significant civil fines for violations of FHA origination and underwriting requirements. With the recent revelations of the financial health of the Mutual Mortgage Insurance Fund, lenders can count on timely audits by HUD to insure compliance within areas of concern, such as validation of source of funds, borrower's ability to repay, documentation of compensating factors for loans with low qualifying ratios and general data integrity. Violations such as these have already severely impaired the financial well being of lenders, and in some cases have completely shut down operations because FHA has the ability to impose fines of up to \$7,500 per violation or \$1,375,000.00 for all violations within a one year period.

Furthermore, it is no secret that GSE's and Capital Market Investors have recently made a significant commitment to auditing non-performing loans in an effort to enforce the Representations and Warranties made by sellers/originators under their Loan Purchase Agreements. Once a material breach is uncovered, the GSEs or the Investor make a repurchase demand requiring the seller/servicer to buy the loan back at par regardless of the current market value or performance status. The traditional Representations and Warranties within these Loan Purchase Agreements are drafted with very broad language that will permit a repurchase demand for any deviation from the approved guidelines and for any compliance violation. In this new world of mortgage lending, loan originators must commit significant resources to ensure every loan is reviewed for compliance with all origination guidelines, as well as all federal and state compliance requirements.

Due to this proactive loss mitigation strategy, post-closing quality control reviews that test only a small sample of production can no longer be relied upon by lenders to identify loan level, portfolio and repurchase risk. In a competitive pricing market with paper thin margins and ongoing constraints on the type and amounts of fees collected, the financial burden associated with committing significant Quality Control resources to ensure the credit, collateral and compliance quality of all assets is overwhelming and not practical for many lenders.



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SOLUTION:

“Compliance Modeling” is a paradigm shift from traditional origination practices. This approach ensures a lender’s compliance with all guideline requirements through process validations and verifications within the workflow that permits lenders to control and monitor the quality and content of all originations. Through Compliance Modeling, lenders drive their operational workflow with a customizable end-to-end origination, processing, underwriting and closing platform that permits implementation of individual institutional risk requirements, such as product guidelines, while requiring the upload of supporting documents, for digital archiving. Lenders are able to ensure that every individual requirement is met prior to the loan moving to the next step in the process while creating an auditable trail to document supporting information; in effect, creating a digital underwriting file. This removes the manual processes, such as checklists and worksheets that traditionally exposed the lender to risk while minimizing the risk of lost documents (i.e. bank statements) that support underwriting decisions.

The ability for “real-time” automated reporting and issue escalation creates a workflow that is transparent, providing Senior Management and Executives with the necessary information to control and efficiently manage operational risk while creating a clear trail for auditing purposes. For example, under the new RESPA requirements, to control the circumstances that would trigger a re-disclosure of the GFE, a lender may standardize change tolerances and prompt the user to provide supporting information to substantiate the decision to re-disclose. This automated control has the effect of standardizing a subjective decision-making process while digitally memorializing the unique details and circumstances that may be relied upon to offset questions or defend against claims made by Regulators, Investors or Auditors.

"The Mortgage Cadence compliance team is extremely knowledgeable and proactive in providing us compliance support services including dynamic compliance modeling through their platforms," stated Bob Phelps, Business Systems Manager of Standard Pacific Mortgage. "Mortgage Cadence provides us with leading edge automation tools to address these new rules and regulations so that we can ensure compliance and mitigate risk within our organization."

Lastly, the new rules require that the documents be consistent and, if there are changes, they be supported by specific documented changes in the circumstances of the loan. Mortgage Cadence Orchestrator provides side-by-side comparison screens for users to check for variances between the GFE and HUD-1. All changes of circumstance can be tracked and are available for review.

The compliance modeling approach is yet another way Mortgage Cadence proactively assists its clients in meeting these extraordinary regulatory demands. Mortgage Cadence clients, both forward and reverse lenders, benefit from this shift in compliance automation by significantly mitigating risk that may lead to buybacks, fines and the potential loss of licenses. It is the difference between the cost and expense of identifying errors after the fact vs. preventing compliance errors before they take place through automation within Mortgage Cadence Orchestrator. This enables lenders to dynamically enforce business policies while adhering to new regulatory mandates.