Greg Holmes is national director of sales and marketing at Salisbury, Md.-based Credit Plus, a provider of credit and mortgage information services since 1928.

BY GREG HOLMES

The paradox of autumn leaves

Fall is an ideal time to give your validation program a boost

In the last five years, the mortgage industry has suffered a historically serious case of the flu. Now that some time has passed and we are feeling a bit better, let us not forget the need to greet every autumn by taking our flu shot.

Since the U.S. government passed the Troubled Assets Relief Program, or TARP, in October 2008, much has been done to help stabilize a mortgage market ravaged by the U.S. subprime crisis. Congress passed the Dodd-Frank Wall Street Reform and Consumer Protection Act, and the Consumer Financial Protection Bureau is now a permanent part of the mortgage industry landscape.

Despite all this government effort, industry observers have noted that the bulk of the responsibility for the health of individual mortgages is still placed squarely in the hands of lenders. This means it is the responsibility of industry professionals to maintain a high standard of quality in every mortgage they originate. Given this responsibility, there is a very real need to inoculate ourselves against errors and omissions in the process. As with any vaccine, the industry's origination processes are going to require a regular booster shot to make sure every mortgage created is rigorously reviewed and ultimately becomes a safe asset for the lending institutions we serve.

As with every good vaccination, there is a sting involved.

In the case of the mortgage industry, the pain connected with assuring quality comes with additional stress on an already overburdened staff. Administering a more robust and reliable loan process requires plenty of work. This pain becomes even sharper in markets like the one our industry enjoys today, with healthy mortgage volumes stretching staff resources to breaking point. Plenty of midnight oil is being burned. This makes it tempting to relax standards, especially on the part of small- to medium-sized mortgage lenders who must use limited staff pools to stay competitive with the industry's large nationwide lenders.

EMPLOYMENT VERIFICATION

Fortunately, overworked mortgage verifiers will find no shortage of ways to maintain a rigorous home mortgage approval process without sending costs through the roof. Some of the most attractive offerings address the increasingly time-consuming process of verifying employment.

As with many of the steps in a post-meltdown mortgage, compliance is easy but quality is challenging. And today's lenders can't afford to let standards slip. In today's privacy-oriented business world, a casual call to a borrower's employer isn't always enough to get a reliably straight answer on employment status. Staff members charged with this task run into a variety of challenges.

Employer stonewalling: In an increasing number of cases, employers simply decline to offer employment information when requested. A company may be concerned for an employee's privacy. In larger companies, the cost of providing verification is significant enough that they may simply decline in the face of a scarcity of staff resources.

Old information: Since an employer is under no obligation to provide information to a lender, they may not be concerned about how up-to-date their records are. The front desk receptionist who answers the phone is often unaware of an employee's status with the firm, even long after the human resources department has terminated their employment.

The old-fashioned runaround: How many times has a staff member called a human resources department, only to find that the person in charge of employee verification is out to

Copyright 2013 by HousingWire • 2701 Dallas Pkwy, Ste 200 • Plano, TX 75093 • 469.893.1480 • HousingWire.com • Reprinted by permission

ARMS REVIVAL FRAMED BY HARDER REGS P.80

lunch or on vacation? Most companies place a low organizational priority on providing this information, as anyone charged with obtaining it will quickly come to understand through firsthand experience.

Once again, the free market comes to the rescue. In this case, collections of payroll records contributed directly from employers prove valuable resources. These types of programs allow employment status to be verified in a matter of seconds, with the reliable accuracy reinforced by updates every payroll cycle.

EXCLUDED

But what about the large percentage of U.S. employees not currently included in such databases? Increasingly, credit service providers are backing up such data with additional services that fully verify employment without the need for a member of a lender's staff to pick up a phone and start digging personally. More and more lenders are seeing the need to outsource this time-consuming and frustrating function. They are realizing that mortgage brokers simply don't have the time for employment verification while they also help clients through an increasingly complex approval process and work to hunt down a constant stream of new homebuyers and refinancing customers.

The complete employee verification process commonly involves serious sleuthing. Reaching the right person — especially in a smaller company — often requires multiple phone calls and plenty of patience. The difficulty is doubled when the same information must be verified once again in the 10 days prior to a loan's closing. Human resource professionals who are willing to comply with a first request may be less than thrilled to repeat the exact same exercise a second time around.

Outsourcing employment verification is also an attractive option for the managers of mortgage lending firms, who appreciate the rigorous process control that comes with outsourcing validation. An outside vendor is far more likely to have a well-documented validation process in place, along with the ability to quickly and easily generate proof that the process was followed to the letter. This goes a long way toward convincing company management that a failed loan isn't the processor's fault. Fannie Mae, Freddie Mac and government regulators also look favorably on a firm with a well-managed, quality-assured and well-documented employment validation function.

Verifying and re-checking employment status is only part of the burden that causes mortgage lenders to turn to outsourced validation services. Tax return income verification is also increasingly being performed by outside providers, thanks to their extra expertise in navigating the complexities of the IRS system when tight turnarounds are necessary.

Uncovering undisclosed debt is an especially challenging part of the mortgage loan approval process, which is why it increasingly appears on lenders' lists of outsourced services. Undisclosed debt ranks with overstated income as a leading cause of mortgage fraud. Some products focus on keeping track of a lender's credit activity in the quiet period between the original pulling of a credit report along with the closing date of the loan.

For some borrowers, incurring additional undisclosed debt during the "quiet period" is an attempt to cover up debt that might otherwise work to disqualify them. For others, it is merely an honest impulse to buy a car, add a credit card or buy some furniture for that new house during the often-lengthy process of loan origination.

Both of these types of new debt is sufficient to scuttle a mortgage that has taken many hours of hard work and organizational expense to get arranged. As a bonus, these types of products keep a continuous watch on a borrower's credit status automatically. This then eliminates the need for costly and time-consuming rechecking by an employee on the lender's staff.

OUTSOURCING

There is an underlying reason why protection services like employment verification or undisclosed debt are increasingly being outsourced — and it is vitally linked to the subprime mortgage crisis and to the new, more stringent attitude toward regulation that was its result.

The reason, in a word, is rigor. Today's mortgage originators must do more than merely try and be diligent in validating the mortgage loans they create.

Tasking an employee with the responsibility for following up won't be sufficient without a clear procedure and a well-developed mechanism for making sure the process has been faithfully followed and carefully adhered to. Today's investors and tomorrow's regulators may be unlikely to accept an employee's assurance that the process was followed to the best of their ability. If your process should ever be audited, the auditors will want proof.

The mortgage industry's top corporate managers are under increasing pressure from Wall Street and Washington. The inhabitants of Mahogany Row are turning to outsourced services that provide both a sophisticated system for improving the quality of mortgage information and the staff resources to carry it out reliably. They love the ability to respond to the demands of a constantly fluctuating market, without stressing in-house staff to the breaking point or adding staff that cuts into their windfall profits.

Through hard experience, executives are learning that the overhead costs connected with outsourcing parts of the validation process are much more palatable than the alternative: The cost of repurchasing an invalidated loan.

Nobody looks forward to having a vaccination. It costs money, and it hurts.

But the sting of inoculating your company against the scourge of validation error is far easier to tolerate than the enduring pain that a bulging portfolio of bad loans can bring.

Indeed, improving your validation process can improve your own corporate vital signs. That is a notion to which executives across the country can perhaps all subscribe. It can also prove to be your company's individual contribution to preventing another epidemic of default that, at this point in time, the mortgage industry can ill afford. ■

KEY CONCEPTS

As with many of the steps in a post-meltdown mortgage process, compliance is easy but quality is challenging.

In today's privacy-oriented business world, a casual call to a borrower's employer isn't always enough to get a reliably straight answer on employment status.

The underlying reason why protection services like employment verification or undisclosed debt are increasingly being outsourced is linked to the subprime crisis.

Copyright 2013 by HousingWire • 2701 Dallas Pkwy, Ste 200 • Plano, TX 75093 • 469.893.1480 • HousingWire.com • Reprinted by permission