



THE HILLARD HEINTZE
360° INSIGHT

MORTGAGE QUALITY CONTROL AUDITS:

Peeking Into the Engine Room

Rarely Tapped Strategies for Improving Case File Timeliness,
Accuracy and Completeness - At High Volume

A HILLARD HEINTZE EXECUTIVE BRIEFING PAPER



Today, the number of mortgage loans either in default or imminently in danger of defaulting has risen to levels unseen in more than thirty years, if ever.

It's not just the risk of default. For many businesses, the most pressing issue is controlling the business costs required to manage these risks.

By now, the investment that companies across the mortgage industry - from lenders, investors and brokers to mortgage insurance providers - are making in mortgage verification and quality control audits can represent a staggering commitment of time, energy and cost.

Not surprisingly, for companies seeking to ramp up their mortgage verification audits on an in-house basis or engage an external provider for these services, the two most critical imperatives are (1) the quality of the audit itself - in terms of accuracy and completeness, and (2) its timeliness - the number of days it takes from case identification to finalization.

The "blue ribbon" standard, however - and the tripwire that nearly all firms with mortgage quality control operations trigger at some level of frequency - is the unwavering ability to meet quality and timing performance metrics systematically, day-in-and-day-out, on a reliable and predictable high-volume basis.

Variability and Volatility: The Business Costs of Failing to Control These Can Be High

Just a decade ago - when corporate profit margins were less tight, regulatory oversight less severe and audit case volumes hovered at a far lower level - mortgage verification was a tactical, often largely manual back office function better recognized for requiring little senior management attention, if any, than for contributing to bottom-line business performance.





Today, it's not unusual to see mortgage verification process excellence as a strategic priority on the agenda of the Chief Risk Officer, the Chief Compliance Officer, the Chief Financial Officer and even the Board of Directors. Why? The true business costs of failing to manage this cost center are uncomfortably high, including direct and indirect costs such as:

- Elevated loan delinquency rates and, by extension, lower portfolio valuations.
- High loan reserve levels required to comply with regulatory requirements - which tie up capital and weaken balance sheets.
- Inflated management and overhead costs associated with tracking and managing the post-close quality control audit process.
- Compliance exposure - along with the attendant implications for risk management and internal controls, and potentially company reputation and shareholder value.

What Are the Most Common Tripwires To High Throughput, Minimal Variability and Low Volatility?

Personnel: Difficulty finding and retaining sufficient talent with all the requisite skills. Inconsistent training. Failure to incentivize case investigator performance with opportunities to share in the program's achievement of quality- and timing-related metrics.

Technology: Inability to customize COTS (Commercial Off-The-Shelf) software to the program's changing needs. Less than robust automation. Poor cross-platform integration and functionality - both within the program and, in the case of an external provider, to the client's pre-referral and post-report systems.

Process: Failure to systematically embed quality and timeliness objectives within core operating processes and procedures. Hidden conflicts between these "goal posts" and other non-strategic operating metrics.

Internal Controls: Gaps between oversight, feedback and enforcement. Inefficiencies inherent in either over-centralization (i.e., aggressive escalation procedures, backlog and executive burn-out) or too much decentralization (i.e., auditing the auditors).

Management and a High Performance Culture:

Failure to champion program excellence and core values and principles. Absence of focus on celebrating individual achievement. Missteps in promoting the balance between work and personal time. Uncertainty about how to instill in each employee both very high performance expectations and an acute sense of their own contribution and participation in the program and, if relevant, the client's success.

Practical Tips for Execution: Our Recommendations

How can you best manage these costs and risks? Different models - ranging from in-house solutions and outsourcing to a surprisingly wide range of hybrid alternatives - offer various advantages and drawbacks. Whether you set out to create an "engine room" for mortgage quality control audits or prefer to engage an external provider to deliver these services, each of the strategies and tactics below will be crucial.

Tip #1 - Bring a disciplined, quantitatively-structured focus to quality and timeliness.

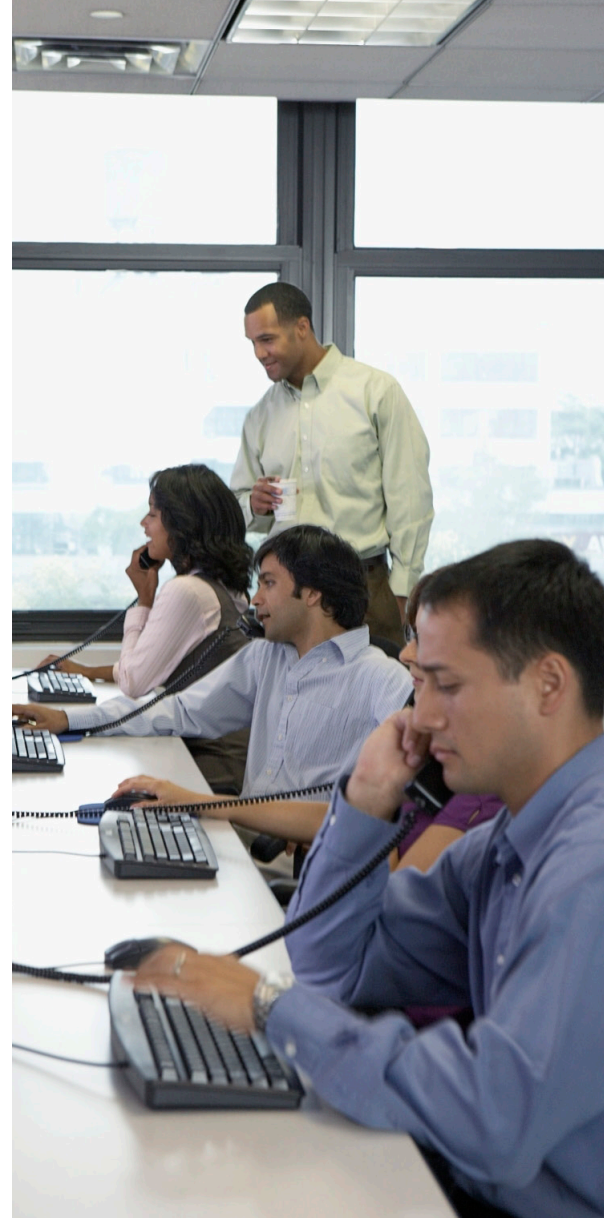
These become even more important as case volume rises. Hardwire these priorities into your core operating processes and personnel policies - from recruitment and training to performance reviews and compensation. What are the key metrics to use? Start with (1) average cycle time by period and by case file manager and (2) mid-process measures that give you early insight into quality-related issues.

Tip #2 - Be prepared - or seek out service providers that are prepared - to scale.

It's one thing to achieve case file accuracy and timeliness on a limited basis. It's quite another to bring the same intensity, process discipline and planning predictability to several hundred cases at the same time.

Tip #3 - Make sure you actually capture the economies of scale.

Think simplification, standardization and automation. Make sure that your quality control audit strategy impacts your business's bottom line. How? Through lower costs, fewer vendors, and manageable levels of risk that can emerge from predictable, efficient and auditable operations that can be systematically improved over time.



For More Information

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