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# LOSS MITIGATION COMES OF AGE

How to fit loss mitigation ♦  
into your processes

Recover before default ♦

Advice consistency needed ♦



In an attempt to help debtors cope with the effects of the sub-prime mortgage crisis, lenders must embrace loan modification strategies which could help in the long run

By Jame Cofran and John Frey

**T**he sub-prime mortgage crisis and resulting financial meltdown have created a tidal wave of consumer delinquencies and, in particular, an unprecedented volume of defaulted home mortgages.

While most collections organisations have invested in automating and streamlining many aspects of their operations, loss-mitigation activities have remained highly manual and labour intensive due primarily to historically low volumes and intrinsic complexity.

However, this volume surge, paired with intense governmental and public interest and falling home values, has brought automating loss-mitigation operations to the fore.

## How did we get here?

By now, those of us who have been entrenched in this crisis should no longer need to ask that question. We are all too aware that, not so long ago,

virtually anyone who wanted to own a home could do so.

Some lenders were notoriously creative, offering loans with little or no down payment and, even though interest rates were at historic lows, many people opted for adjustable rate mortgages (ARM) as they started thinking of their houses as quick-turn investments rather than as their home.

Eventually, as prices began to plummet, owners panicked and put their homes on the market to get out while they still could, but potential buyers were not buying.

At about the same time that those, once-attractive, ARMs were coming due, homeowners found it increasingly difficult to pay for – let us be honest – more house than they could originally afford.

The mortgage crisis quickly became merely the tip of the iceberg. After depleting their savings, homeowners

began to borrow against home equity lines of credit and credit cards to pay their mortgage. When those sources dried up, they walked away from their upside-down mortgages in droves, forcing banks to assume ownership of hundreds of thousands of properties.

A vicious circle was created as repossessed properties, sold at discounted prices to stem further losses, accelerated the downward spiral of surrounding housing prices, causing even more defaulted mortgages.

## What happened next?

The initial reaction by many banks, lenders and loan servicers was to hire additional staff to handle the increase in repossessions, short sales, deed-in-lieu agreements, bankruptcy processing and, most recently, loan modifications.

While this has helped somewhat in the short term, it is not efficient or effective in the long run, and this crisis is a long way from over.

The bad news is that tackling these issues appropriately requires leveraging several types of technology to address the various, somewhat complex and still-evolving, requirements. >>

>> The good news is that most of the required technology already exists; it just needs to be re-configured to address these new opportunities.

#### How should we respond?

Loss mitigation involves a complex workflow caused, in part, by numerous regulations. Missing a key date or completing actions in the wrong order can cause you to have to re-process or, worse yet, forego a government reimbursement.

The best solution is to either extend your current collections system workflow processing to include loss-mitigation activities, or implement a stand-alone loss-mitigation workflow system, several of which are available in the market. This will not only reduce the number and experience level of staff required, it will also ensure that all necessary steps are accurately performed in the appropriate timeframe and that an electronic record is created.

A successful loan modification – the fastest growing, and most misunderstood, loss mitigation activity – presents its own unique challenges. As a creative way to help homeowners bring their monthly mortgage payments to more manageable levels, the \$50bn plan in the US got off to a slow start, mostly because these are tremendously complex transactions, wrought with policies and regulations that many banks and loan servicers do not understand.

This has caused delays in providing mortgage holders with the assistance they so desperately need. In fact, according to the US Treasury, only 920,000 loan modification offers have been processed to date – just 29% of those that are eligible.

Financial institutions are trying to improve their responsiveness, but find it difficult to hire experienced or trainable staff to manage the millions of applications. This is another area that can be fully automated by configuring existing collections systems.

By leveraging existing call scripting and advanced-decisioning capabilities, these systems enable less-experienced staff to complete loan modifications in accordance with all applicable regulations and policies.

Successful loan modifications also depend on up-to-date, accurate home values. In a rapidly changing market, this is difficult for lenders to obtain and, at a minimum, requires costly and time-consuming individual visits by skilled property appraisers.

An evolving response to this need is online, real-time data on home sale

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prices. Integrating this information electronically into the loan modification process will provide enhanced data to enable better decision-making as well as increase speed and decrease costs.

Lenders now report that the most significant hurdle in successfully resolving defaulted mortgages and other types of loans is actually making contact with the borrowers.

In many cases they are working with a different kind of consumer – one who may never have been in collections before. These people are worried about losing their home and their livelihood. They may not respond to requests for payment through traditional means – the phone call and correspondence – because they are embarrassed to be in the position they are in.

And, with the intense scrutiny on mortgages, credit-card fees and overdraft-protection charges, banks and collections agencies have become ‘the bad guys’. Now, more than ever, it is critical to become nimble, flexible, customer-focused and open to changing the way things have always been done.

#### Options

One way to do this is through self-service online debt management applications. Stimulated by the customers’ increased desire to keep a closer eye on their finances, online banking continues to grow, and an online option to review and resolve outstanding debt could be seen as attractive.

Another way is to leverage predictive models, to identify those customers most likely to become delinquent in the near future, and to engage them early

to establish the contact and rapport necessary to sustain communications throughout the process.

There are experts that can help you define your comprehensive debt strategy, be it online collections or using an outsourced model, to shift gears as collections needs change. These tailored solutions range from

hosted application maintenance to full business process outsourcing.

Outsourcing your collections or loan-modification business helps manage the volume without recruiting so you do not find yourself in a downsizing position when volumes subside. All stages of collections are addressed, including recovery, default management, loan modification, third-party management and recovery accounting, resulting in a fluid, end-to-end operation that maximises efficiency and results.

#### Conclusion

The bottom line is this – the effects of the financial crisis are not going away any time soon. There are signs that the situation is getting better, but we predict that the glut of repossessed homes, backlogs and write-offs will be on your books for longer than you may envisage.

It is time to look at options for increasing the efficiency and effectiveness of your business, which, in turn, will lead to lower losses and ongoing operating costs. **CCR**



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