Branch Office LOS Selection

THERE'S A QUIET DEBATE RAGING OVER branch-office automation. Retail mortgage origination companies that have a dozen or more branch offices face a difficult decision about what loan origination system (LOS) to use at the branch level. While I can't suggest one solution, I can outline the dilemma that chief information officers face and discuss the pros and cons of two different options.

The problem centers on what type of LOS to use in each branch when there are a dozen to hundreds of branch offices. At the low-cost end of LOS offerings are what I call off-the-shelf products. These include products like Byte, Calyx and Ellie Mae, as well as several others. They are fairly low-cost products (around $1,000 per office) and are widely used among mortgage brokers.

The other type of LOS products are those designed more for large branch operations. They are much higher in cost ($5,000 to $25,000 per office) and come from a wide range of vendors. They are often customized at the direction of the CIO and have many features just for multi-branch operations.

Many years ago, Countrywide Home Loans Inc. purchased about 60 copies of Contour Software's The Loan Handler™, which at that time was a very odd purchase. When queried about its requirement, it turned out that Countrywide needed to process loans for its broker clients—these were loans that might not be purchased by Countrywide. Its internal system could only process loans that were destined for Countrywide, since every loan logged would impact all the management reporting systems. Thus, it was cheaper to buy an off-the-shelf LOS than to reprogram the company's internal system.

So this separate LOS was used to process loans from brokers that may never be purchased by Countrywide. After a couple of years, Countrywide was able to modify its system, and the need for a separate system went away. This showed that even the largest lenders will sometimes use the inexpensive off-the-shelf products. Today, this trend has accelerated to the point where some branch office operations, as large as a few hundred locations, are standardizing on these cheaper LOSes.

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—SCOTT COOLEY—

Let's look at why a larger lender might consider an off-the-shelf product. The reasons could include the following:

- The cost is far less than for traditional products.
- These products are quick to roll out throughout all the branches.
- Often, loan processors already have experience on these products, which saves on training costs.
- Technical support can be handled by the software vendor rather than by the main office staff, which saves the headquarters significant dollars.
- The software vendor also handles the update/upgrade process.
- The branch staff often prefers a simpler LOS with which it is familiar.
- Because these products have limited customization capabilities, costs are saved by the management information systems (MIS) staff.
- Hiring loan officers can be easier when a widely accepted application is used by the branch.
- With the ups and downs of the origination cycle, branches can quickly be added and removed as the markets dictate, with minimal costs.

Of course, there are many reasons not to use these cheaper solutions as well. The CIO and management typically have many needs that aren't met by the off-the-shelf products. The reasons that many CIOs choose a higher-end LOS could include the following:

- The ability to develop sophisticated branch communication systems. These are important for secondary marketing departments and management reporting purposes.
- Security is becoming an increasingly important issue. The off-the-shelf products typically lack sophisticated security solutions.
- Taking advantage of workflow automation requires an LOS that has been designed to handle workflow.
- Large companies have a need to collect information during certain times of the loan process, and this requires significant customization of the screens and documents.
- Management needs the ability to control data entry and data integrity. The high-end LOSes provide a better ability to ensure quality control for all personnel. Mistakes on forms like the closing Reg Z can just be too costly to leave entirely in the hands of the branch office staff.

I've heard from several mortgage companies that are facing this choice and are having a difficult time deciding which way to go. I also see companies switching in both directions, so there is no clear trend that favors one approach over the other. Still, when you look at recent surveys of the mortgage industry by Wholesale Access, Columbia, Maryland, we're finding some lower-end LOS products becoming more popular among the large multi-branch origination companies. Ten years ago, such a deployment would have been unheard of.

I do see that the off-the-shelf solutions are now adding more features that help the large branch office operations. In addition, companies such as Del Mar Database, San Diego, are finding success building middleware that allows large companies to use inexpensive LOSes by filling in the missing pieces. Del Mar's product, DataTrac®, can add the communications solutions, customization, data management and reporting systems that the higher-end LOSes offer.

The high operating costs of an extensive branch network have led to the demise of some large mortgage companies in the past when interest rates rose. Companies such as The Money Store and others found their technology costs were so high that they helped bring down the entire company. There are many other cases where large firms attempted to build world-class LOSes for their branch operations only to later shelve the entire project.

On the other hand, much of Countrywide's success can be attributed to its technology solutions. As Countrywide Financial Corporation Chairman and Chief Executive Officer Angelo Mozilo has been quoted saying, "Countrywide is a technology company that does loans." While Countrywide has had a few missteps, overall it's done a terrific job with its branch-automation solutions—and this has been very evident in its ever-higher stock price.

According to the 2004 MBA Technology Study, lenders spent $15,418 per year on technology for each employee end-user. I would guess that this number could be cut in half if an off-the-shelf LOS was used. That makes me wonder: If we applied such a savings to higher salaries for better people, would the lender be better off overall? Would having better staff be enough to offset the shortcomings of the off-the-shelf products? Of course, it would be very difficult to know for sure.

What's important is that today's CIO considers both options carefully. Too often, I see egos getting involved in the decision-making. After all, what CIO wants to go to a board of directors and recommend a $1,000 solution more often associated with small mortgage brokers?

I liken it to word processing software. No company today would think of building its own word processor, and almost all standardize on the inexpensive Microsoft® Word program. It can be entirely appropriate to look at loan processing software like word processing software. An off-the-shelf product might be appropriate, especially if you couple it with additional applications that meet the needs of larger organizations.

There is no one answer that applies to every organization. Each company has to look clearly at all the options when selecting an LOS for its branches. Today there are more options then ever, and that can make the task that much more difficult.

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