Luxoft
A DXC Technology Company

Digital default management

Modernizing mortgage default for the future

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Introduction

Mortgage Servicers are at various stages of their default digital transformation journeys. To be successful, they can leverage solid fundamentals and lessons learned from other parts of the organization.

After years of making do with legacy systems, the mortgage default servicing industry is primed to make a major digital transformation leap. As the origination space has seen rapid investment and advancement, banks are now putting more focus on their default operations. Recent events, such as the COVID-19 pandemic have proven challenging for the industry to manage due to the unprecedented numbers of customers seeking assistance. Most servicers utilized traditional call center methods or hastily developed point solutions to handle the massive increase in transaction volume. Servicers have historically focused on internal efficiency, timeliness and accuracy while adhering to robust regulatory and investor rules, we're now seeing more focus on the customer experience.

The industry is starting to adopt technologies that will transform their operations by leveraging more automation, customer personalization and efficiency. While leading servicers are well on their way to digital transformation, others are struggling to prioritize and execute a coherent strategy. A Forbes and Freddie Mac survey of mortgage executives found that digitizing the servicing operation ranks last among all areas; falling behind marketing, origination applications, compliance and others. Only around half of all Mortgage Servicers have transformation pilots underway or are fully digital[1].

In this paper, we will explore the key fundamentals and major areas of opportunity required for a successful digital journey. The benefits of digital transformation are clear and include:

- Improving the overall customer experience through consistency and personalization
- Reducing customer assistance timelines
- Reducing human error throughout the process

"Mortgage Servicers that embrace innovative approaches and mindsets will outrun the competition in the digital future."

Ashish Shreni,
Cognizant's Consumer Finance Consulting Practice

1 "Digital Mortgages: How Leaders Are Harnessing Tech To Streamline Processes, Cut Costs And Improve Customer Experience", Forbes Insight with Freddie Mac, 2019MIT Technology Review

Fundamentals of the transformation journey

Servicers embarking on the transformation journey should be equipped with a solid set of fundamentals to guide them to success.

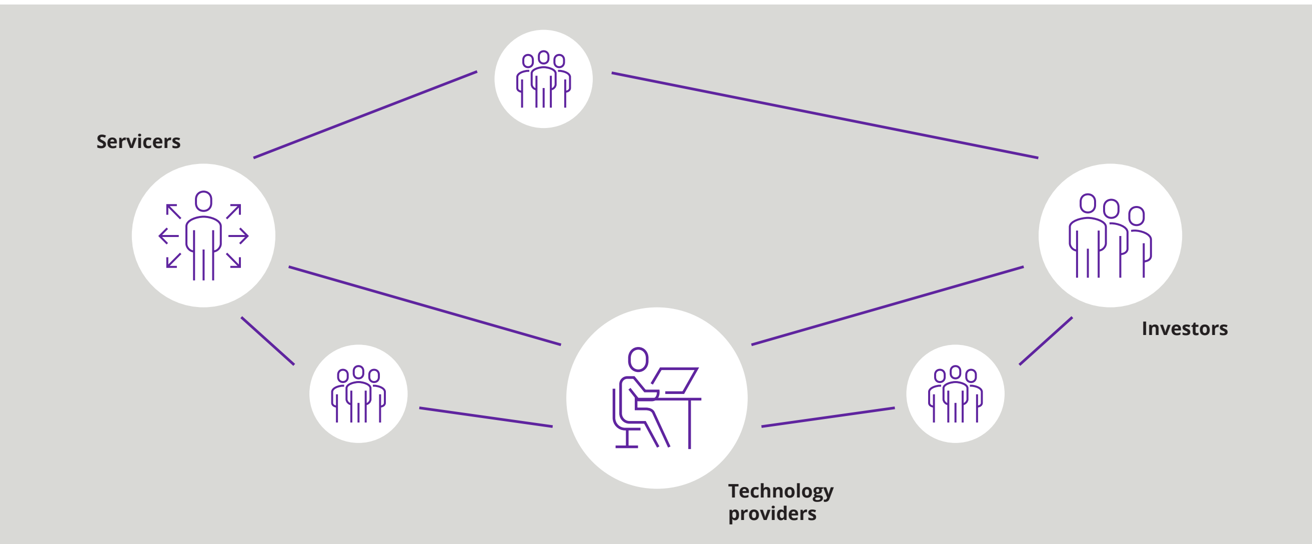
Defining a vision for the industry

The default management digital journey requires more than just the implementation of new technologies, it also involves fundamental changes to each participant of the process. Servicers, investors and technology providers all play a role in evolving processes, resources, and technologies in the space. Targeting a clear future state, understood by all is the first step in the journey.

For servicers, this means taking an inventory of their entire operation and the goals for each area. Servicers who catalog their processes, technologies and pain points will be able to identify areas that need attention. Servicers are often amazed to see a plethora of technology systems in place to solve niche business needs, often with overlapping capabilities. Understanding the current state will help drive out where the largest opportunities exist within the operation. Establishing a governance apparatus with clear priorities and deliverables helps to formalize the digitization journey. Constant communication on progress is important to drive the entire organization to a new digital state.

Investors play a major role in the mortgage servicing process and must also have a firm strategy to transform their technologies and operations. Traditionally, investors have published guidance on borrower and account treatment, with servicers expected to interpret the complex requirements. Investors are already starting to create new technologies to simplify the interpretation of these guidelines while reducing overall process timelines. Examples include Fannie Mae's SMDU and Freddie Mac's Resolve workout decision engines, available via API's. Investors are also starting to reevaluate how critical customer information is gathered, allowing for more digital gathering of information, instead of the traditional reliance on the customer. This is reflected in **Fannie Mae's recent update to their Servicing Guide** to explicitly allow for electronic verification of income and assets via third parties.

Lastly, technology providers are a critical driving force in the digital journey. Technology companies must understand the default industry and provide tools that are flexible, scalable, and fit into the overall footprint of the organization. SaaS-based tools should take lessons learned in the CRM and ITSM arenas to create an ecosystem of partners to give clients choices of third-party vendors and services. In the servicing space, this ecosystem will include document vendors, valuation services, attorney networks and other participants.



Adopt an agile mindset

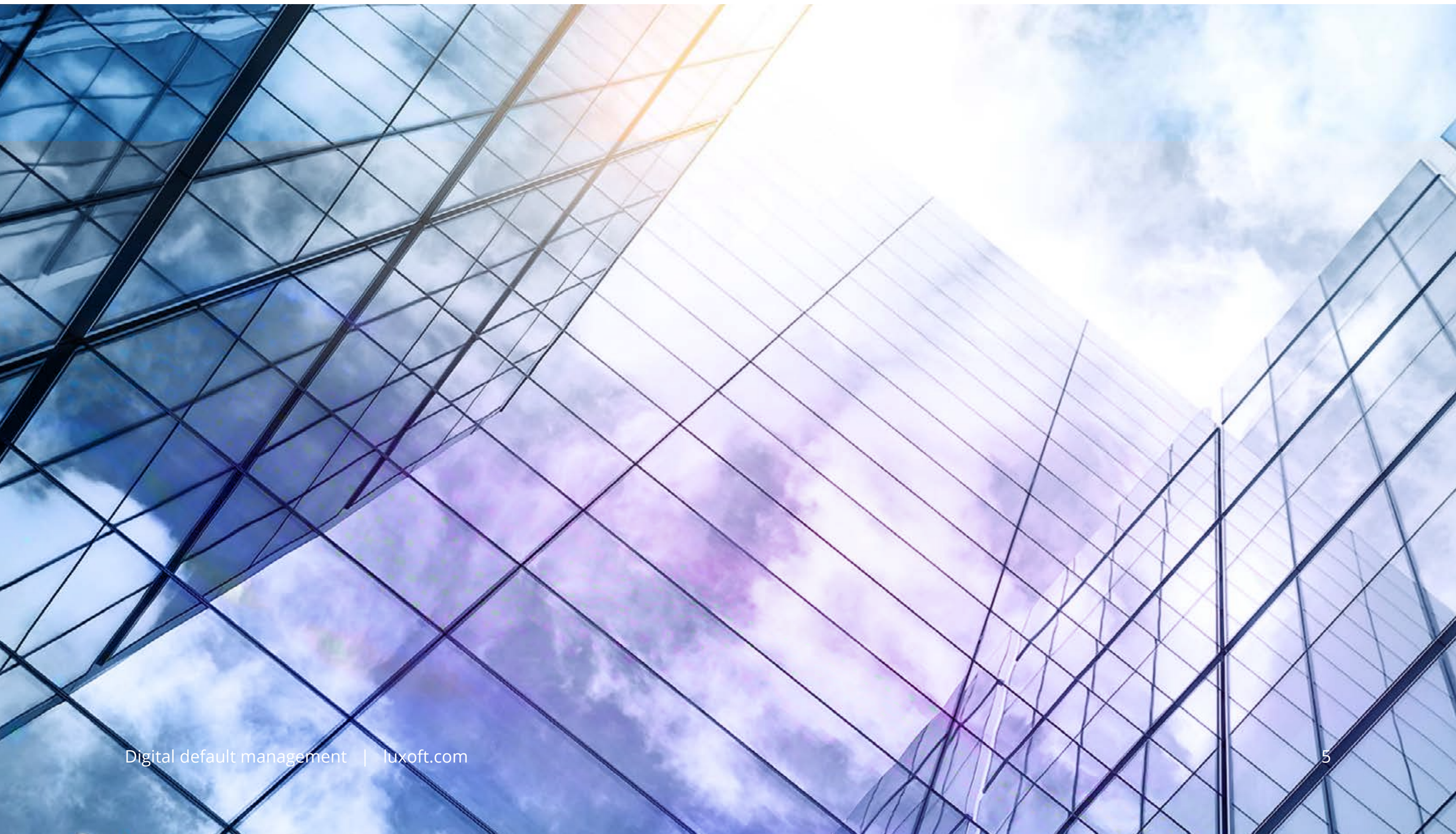
Servicers should adopt a mindset that emphasizes flexibility, openness and iterative change. Since the 2008 financial crisis we have noticed that servicers who build agility into their operations are able to react much quicker to natural disasters, investor rule updates, and ever–changing market conditions.

Many legacy systems utilized by the servicing industry are decades old and rigid, making rapid transformation a challenge. In addition, servicers have had to build their own internal solutions to solve distinct parts of the process. Examples include homegrown income calculators, document checklists and underwriting engines. These tools have proven to be challenging to support, extremely inflexible and expensive to maintain. Trying to plug new solutions into the current process is often a laborious exercise, relying on internal business and technical gurus to understand what has previously been built.

Focus on the customer

For customers who find themselves struggling, their interactions with the bank can be frustrating, confusing, and time-consuming. They must endure endless phone calls, paper applications and mailed correspondence. Providing documentation to the servicer is labor intensive and relies on outdated technologies. For a customer going through the loss mitigation process, attempting to understand the status of their application can be a challenge, not to mention that calling into the bank is often a source of frustration.

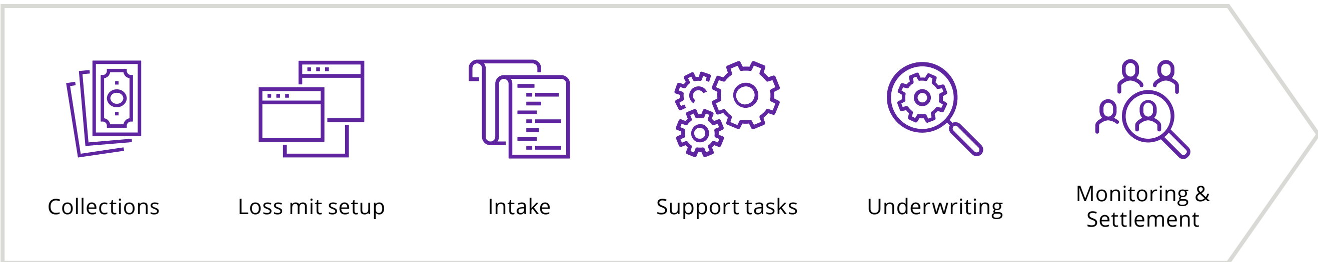
Many servicers have begun focusing on the customer experience (CX) as a critical success factor in the default process. For customers who are experiencing hardships, such as job loss, the traditional default process can be overwhelming. Servicers who focus on making the default experience as painless and straight forward as possible will benefit with shorter timelines and higher customer satisfaction. This customer-centric approach should flow to all available contact channels, from call–center agent interactions, customer portals, chatbots and IVR interactions.



Default management **transformation opportunities**

The mortgage default space is ripe with digital transformation opportunities

An analysis of the mortgage default management process unveils an abundance of transformation opportunities. Most servicing operations have traditionally had a distinct set of technologies utilized in each area such as collections, loss mitigation and settlement. At the core, there is often a legacy system of record that must be updated, referenced, and managed throughout the process. Hanging off the system of record are innumerous homegrown and third-party technologies, each addressing a distinct part of the process. As a result, the technology footprint is expensive, inflexible and inefficient.



Default management overview, major transformative areas highlighted

Customer communication

Communicating with customers throughout the default process continues to be overly reliant on phone calls and mailed documents. Delinquency notices, payment reminders, and various loss mitigation notices are all opportunities to streamline customer communication. Customers are becoming more difficult to reach via phone, while mailed communications reduce overall timelines. Customers now prefer their banking interactions to be digital, an expectation formed by retail banking mobile apps and portals. This interaction is highlighted by a global survey of banking customers, which indicated ~ 60% of all customers interact with their banks at least two times a month via online banking or mobile apps[2].

Servicers have already begun to expand their communication channels to include chatbots, text messages and social media engagement. Chatbots may provide the biggest opportunity to improve customer communications. During the first few months of the COVID-19 pandemic, IBM’s Watson Assist chatbot offering saw a 40% increase in usage as companies had to adjust to rapidly altered call-center environments and budget cuts[3]. Many of these companies will continue

2 “Accelerating digital transformation in banking”, Val Srinivas & Angus Ross, Deloitte

3 “The pandemic is emptying call **www.technologyreview.com/2020/05/14/1001716/ai-chatbots-take-call-center-jobs-during-coronavirus-pandemic centers**. AI chatbots are swooping in”, Karen Hao, MIT Technology Review

to expand their usage into the future, especially as chatbots improve upon natural language processing and artificial intelligence (AI). Servicers will be able to offload less complex assistance requests through the chatbots and can expand to more complex interactions.

Text messages are another underutilized technology for communicating with customers in servicing default. Text messages are an ideal way to communicate payment reminders, loss mitigation status, and other required actions to quickly resolve a customer's hardship scenario. Recent studies have found that text messages have a 98% open rate and response rates are 209% higher than phone, email, or Facebook communications[4]. Utilizing business rules engines and workflow tools, these communications can be tailored to handle specific investor, process and customer scenarios.

Where official documents must be generated, such as loan modification agreements, platforms should be able to generate, view and deliver documents electronically to customers. Customers can then then use an electronic signature for these documents, reducing the entire loss mitigation process timeline and cost.

Collections

Collections operations for most loan servicers haven't changed much in the last several decades; call centers filled with agents fielding inbound and outbound calls, triggered by customers missing loan payments. This continues to be a very expensive operating model and relies on inflexible infrastructure and resources that must be specially trained on many diverse systems.

Collections contact channels are evolving, as some servicers have begun utilizing intelligent chatbots, mobile friendly self-service portals, and smarter telephone solutions to interact with customers who have temporary hardships that can be resolved with minimal human interaction. In these scenarios, the technologies can offer unique resolution plans to the customer based on delinquency, investor, and other business criteria. Front-end systems will continue to rely on real-time APIs from various back-end sources, consolidated to provide the most interactive, user friendly front-end.

As more data is made readily available to the servicing operation, servicers will start to be more proactive in managing customers who may have fallen on hard times. AI relying on data, such as employment status, credit report data or property data, can be utilized to proactively contact customers who have lost a job, missed a payment on another loan, or have been impacted by a natural disaster.

Loss mitigation setup

Customers who are unable to quickly resolve their delinquency during the collections phase are moved into loss mitigation, a different siloed group within the organization. Customers are asked to download, complete, sign, then upload assistance applications. This data is then rekeyed into the servicers systems, introducing the possibility of manual errors. Customers are often asked to walk through the same information on the phone with the servicer to ensure accuracy.

Again, intelligent self-serve portals should be utilized to gather all of this information at the start of the process, allowing for a customized experience based on each customer's unique scenario. Information about the customer's current hardship, income, and other factors should be captured with a clear understanding of what additional documentation may be needed up front.

4 "35+ Must-Know SMS Marketing Statistics in 2020", Teodora Dobrilova, TechJury

Document and data evaluation

As the servicer begins evaluating a customer for assistance, a plethora of documents are required to validate income, employment, hardship and other factors. Most servicers still rely on the customer to send scanned images of paystubs, bank statements, tax information, and other documents to prove their situation. Customers struggle to gather all these documents, resulting in back and forth thrashing with the servicer to validate completeness. Customers become frustrated when additional documentation is requested later in the process based on factors found during processing. By improving what is needed up front, the process can be streamlined while enhancing the overall customer experience.

Many of the documentation challenges will be alleviated through the utilization of the data aggregator providers prevalent in the marketplace. These aggregators gather critical data such as paystubs, tax, or bank transactional data directly from the financial institutions or other third parties. Receiving the data from the source will improve accuracy, reduce the thrashing of the document gathering and verification processes, all while improving the customer experience.

Support tasks

Throughout the loss mitigation process, there are a number of support tasks that are still manually processed by internal resources, such as ordering property valuations and credit reports. Depending on the scenario, these tasks are manually managed from start to finish, often visiting external websites to order the products. Without an orchestration layer in place, many of these tasks do not work in an efficient manner, often waiting for nightly reporting cycles to identify which accounts to work on.

A robust workflow system to prioritize, orchestrate, and automate support tasks is critical to speed up the loss mitigation process. Modern workflow systems with flexible architectures and robust APIs to third-party vendors can be set up to automatically order all the vital products at the appropriate time in the process. Using AI and business rules, many exceptions can be evaluated and resolved automatically, without human intervention. More complex exceptions can be escalated and resolved in real-time by skilled resources.

Underwriting

The underwriting space is one of the most ripe areas for a digital evolution due to the sheer number of homegrown tools and manual processes in place today. Most servicers rely on the underwriters to manually transpose data into income calculation tools that attempt to account for all unique scenarios. These tools tend to be inflexible, expensive to maintain and are challenging for end users.

Next in the process, underwriters manually run a decisioning tool to determine the available workouts the customer qualifies for. These decisioning tools have baked in the servicer's interpretations of investor rules, traditionally a challenge to align to the investors interpretations. Investors like Fannie Mae have helped alleviate this problem with their black box decisioning engine, Servicing Management Default Underwriter (SMDU). Other investors are at various stages of rolling out similar solutions that can be called by servicers, or integrated into industry platforms.

As the technology continues to evolve, underwriting will become much more automated. The introduction of more AI, smartbots, and mature robotic process automation (RPA) will begin to displace existing manual underwriting tasks. For example, AI and RPA can be heavily utilized to perform quality assurance on loan modification final terms and official documents.

Replacing the current "stare and compare" nature of most quality assurance processes will improve accuracy in a much shorter timeframe. Initial observations suggest that the addition of more automation can reduce the loss mitigation timelines by upwards of 50%.

Trial monitoring, final and settlement

Once underwriting is complete, customers are asked to sign agreements, often sent via mail. Servicers have already begun to adopt e-signature capabilities, prevalent in loan originations for many years. All critical data from the underwriting decision can be populated into these agreements and third–party e-signature vendors can manage the entire process, keeping the servicer apprised of the status along the way.

Servicers will be able to interact with the customer via their preferred method, personalized to fit the needs of the specific business process. Once on a modification trial, payment reminders can be sent via text or email to ensure customers are staying on track.

RPA can play a major role during the settlement system maintenance process, a process which is extremely laborious and manual today. By utilizing smartbots, this process can be significantly improved, allowing for the final terms to be input, finalized, and quality reviewed at a much quicker pace.

Conclusion

The next 3–5 years will see tremendous transformation in the default management space as servicers, investors, and third parties continue to embrace new and existing technologies. The utilization of additional channels, third-party data and services, and automation will significantly improve the difficult process for distressed customers. Interactions with distressed customers will be more streamlined while spanning more channels, leading to an overall improved customer experience. Servicers who adopt a solid set of fundamentals and technologies across the entire default management process will lead the industry into a new, more digital, future state.

Luxoft has been a technology leader in the lending industry for over 15 years with leading platforms such as Luxoft EarlyResolution™ and Hogan Loans. We've been on the forefront of empowering our clients with robust solutions to manage the default management process, relying on a robust architecture and ecosystem of partners, Luxoft will continue to lead the default industry through the rapid changes that are occurring. Luxoft has a robust roadmap to rapidly develop or partner with industry leaders to deploy the latest technologies such as AI, RPA, and new digital channels to help transform the industry.

How Luxoft can help

One of the world's leading IT services firms, Luxoft is a recognized leader in complex, enterprise-scale transformations, with thousands of Banking and Capital Market, and Agile experts. Luxoft's EarlyResolution™ has led the industry for nearly 20 years in the default management space. EarlyResolution™ is a SaaS-based platform that is highly scalable and flexible with a robust partner ecosystem. EarlyResolution™ has helped customers:

- **Reduce process cycle times by up to 40%**
- **Reduce inbound calls by up to 30%**
- **Increase underwriting capacity by up to 25%**
- **Decision more than 750,000 loans per year**

Find out how Luxoft can support your immediate and long–term modernization goals.

Schedule a workshop and develop a roadmap for change by emailing earlyresolution@dxc.com.

About **the author**

Hunter Stair
Product Lead, EarlyResolution™, Luxoft

As product lead for the global Luxoft lending product suite, Hunter blends market and business trends with technology innovation to help both servicers and investors better manage their borrowers. A cornerstone of the product suite, EarlyResolution™ has revolutionized the way the industry reacts to constant change, improves the borrower experience, and reduces overall default management timelines. He has over 20 years' hybrid experience in consulting, product management, sales and technical development.

About Luxoft

Luxoft is the design, data and development arm of DXC Technology, providing bespoke, end-to-end technology solutions for mission-critical systems, products and services. We help create data-fueled organizations, solving complex operational, technological and strategic challenges. Our passion is building resilient businesses, while generating new business channels and revenue streams, exceptional user experiences and modernized operations at scale.

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