



Servicing HELOCs in a Challenging Environment

Mortgage defaults and foreclosures are on the rise nationwide, while property values continue to slide in key geographical areas. As a result, the uncertainty in the mortgage market continues, and there is little consensus about when the market will finally hit bottom. Many fear that home-equity line of credit (HELOC) defaults will be the next shoe to drop, with significantly increased default volumes ahead.

In such a tumultuous environment, it is more important than ever for lenders to service home-equity lines on a mortgage servicing platform, rather than the consumer lending platforms that have traditionally been used. When all else is stripped away, these products are real estate-secured loans, a designation that carries very complex demands when it comes to delinquency, default and foreclosure. Additionally, reducing a servicer's exposure to risk requires mortgage-specific data and analysis.

Consumer lending platforms are simply not designed for the rigors of mortgage loan servicing. They lack the functionality that allows access to mortgage-specific data, enables sophisticated analysis and tracks mortgage-specific information such as lien position, property values, escrows and more. With a heightened level of default potential across the board, lenders and servicers need the robust capabilities of mortgage servicing platforms to effectively manage the risks inherent in their HELOC portfolios.

A new reality

In recent years, lenders experienced explosive growth in home-equity lending, in terms of both volume and values. However, as defaults increase and property values fall, many home-equity loans and lines are either in default or at risk. To further complicate matters, increased regulation of home-equity products is coming and can be expected to create additional challenges for servicers.

At a time when it is more important than ever to employ aggressive risk-management strategies, procedures and resources, servicers simply can't afford to utilize less-than-optimal technology. In fact, given the state of today's market, lenders holding second-lien home-equity loans may have as much risk exposure as first-position mortgage holders.

Here's why.

When facing financial trouble, borrowers with both a first mortgage and a home-equity line of credit will do whatever they can to continue paying the note on the first mortgage, even to the point of using the line of credit to keep their mortgage current. This means that the level of indebtedness on the home-equity line is increasing along with the risk of default, though servicers may not realize it for some time.

Fortunately, servicers can deploy a comprehensive, end-to-end servicing solution that handles all real estate-secured loan products. By migrating their HELOC portfolios to a mortgage

servicing platform with embedded HELOC functionality, risk can be better managed and ultimately reduced.

The right tools for the right job

Tracking the lien position of a HELOC is critically important for lenders and servicers. When HELOCs are in a first-lien position, there is certainly increased risk associated with escrow accounts and the payment of taxes and insurance in addition to the default risk. Servicers with HELOCs in their portfolios must be able to carefully track these and other collateral issues.

Unfortunately, most consumer lending platforms lack this most basic functionality, though it is necessary for the effective servicing of HELOCs and other real estate-backed loans. Unlike

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mortgage servicing platforms, consumer platforms were not designed to track escrow payments or default risk, keeping servicers in the dark about information that is critical to their risk position.

Even if the HELOC is in second-lien position, servicers still need to monitor the first mortgage to ensure that the note is being paid and that tax and insurance payments are current as well. Traditionally, HELOC servicers have relied upon the first-mortgage holder to make sure insurance and tax disbursements are being made on time. However, given the volatility of the current market and the second-lien holder's increased exposure to risk, the heightened awareness afforded by a mortgage servicing platform makes much more sense.

Mortgage servicing platforms also give servicers the added ability to track HELOCs against fluctuating property values. Servicers can directly order broker price opinions (BPOs) or appraisals for a determination of value on the collateral backing the HELOCs in their portfolio. With property values decreasing in many key markets, it is imperative that servicers proactively adjust available lines of credit—based not just on delinquency, but also on current property values. However, this risk-management strategy is not readily supported by today's consumer lending platforms.

Of course, if HELOCs ultimately move from delinquency into default, servicers must be able to track these loans



according to default-specific requirements. The lack of this functionality is perhaps the most critical flaw in using consumer lending systems to service HELOCs. As HELOCs move into default, there are a multitude of federal and state-specific processes—even county-specific in some cases—that must be followed.

Facilitating intelligent loan modification

Another inherent capability of mortgage servicing platforms that is not offered on consumer lending systems is functionality that enables the institution to modify loans and institute loss-mitigation efforts, such as establishing payment plans. Consumer lending systems, on the other hand, may only support the ability to freeze credit lines when borrowers become delinquent beyond a certain point.

Alternatively, prior to freezing the line, mortgage servicing platforms make it easy to adjust the available line of credit based upon property values or delinquency and begin loss-mitigation efforts. Once a line has been frozen, collecting the money that is already owed can certainly be problematic. That's where a mortgage servicing platform's ability to accommodate payment plans or forbearance agreements, as well as modified interest rates or loan terms, is particularly helpful.

Some mortgage servicing platforms also include advanced analytics to help servicers make better-informed modification decisions. Analyzing borrower information against market data can deliver insight into prepayment, modification and default propensities to determine whether it makes sense to modify the terms of the loan.

The mortgage servicing platform effectively allows servicers to produce a "re-underwriting" decision for the modification of a HELOC product. Mortgage servicing systems are typically equipped with the ability to access borrower financials, compare those against borrower debt and determine what level of surplus or shortage the consumer will have under proposed new terms. Without that knowledge, loan modifications may only prolong the timing of an inevitable foreclosure and increase its associated costs.

It just makes sense

While it may once have made some sense—back when times were good, volumes were high and risk seemed low—to service a fluid credit product such as a HELOC on a consumer lending platform. However, those days are long gone. Today, given continued deterioration of the mortgage market in general and

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HELOCs in particular, servicers need the functionality available with a mortgage servicing platform.

The vast majority of servicers already have these systems in place; it's just a matter of expanding their use to include HELOCs. Once the shift has been made, servicers will find their HELOC operations benefit tremendously.

From tracking defaults and escrows; monitoring tax and insurance payments, and property values; to informing and enabling intelligent loan modifications based on advanced analytical scoring, a mortgage servicing platform delivers benefits and essential functionality.

Whether HELOCs are in a first- or second-lien position, HELOC lenders have much greater exposure to risk today—risk that requires mortgage-specific tools to properly mitigate. In an environment of rising defaults, decreasing property values and overall economic uncertainty, there is no time like the present to move the servicing of HELOC portfolios to a mortgage servicing platform.

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