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eMortgages:

Research Findings on the State of Industry Adoption

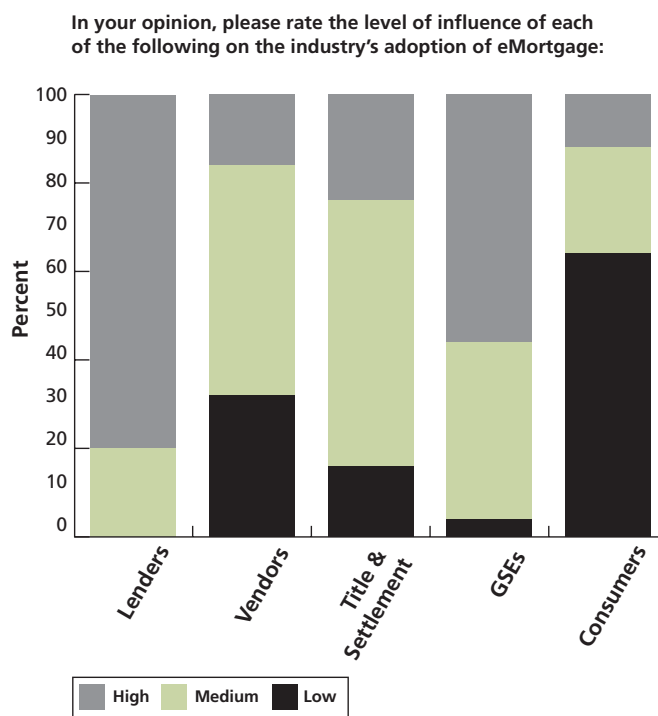
eMortgages: Research Findings on the State of Industry Adoption

In 2006, Fannie Mae sponsored a comprehensive, industry-wide research initiative to assess the current and future state of electronic mortgages (eMortgages), predict adoption patterns over time, and catalog perceptions of value and barriers to adoption. This report summarizes the research findings with special focus on the lender analysis and perceived friction points to adoption. More details about the research – the methodology, participant profile, and other aspects of the research – are provided near the end of this report.

eMortgage adoption is growing slowly but steadily. eMortgages are a reality today for several lenders, and there is a solid pipeline of lenders in the planning and piloting stages of eMortgage implementation.

In our research, the majority of lenders, technology vendors, closing agents, and title company executives believe that eMortgages eventually will be broadly adopted. The majority of the participants perceived lenders to be the most influential drivers to broad adoption of eMortgages (Figure 1). Many vendors, title companies, and closing agents are ready to support the lenders in the planning, development, and implementation of their eMortgage strategies.

Figure 1. Lender and Vendor Survey Response to Questions About Influences on Industry Adoption



Industry analysts agree that eMortgage adoption is slower than adoption of other new technologies or processes, such as automated underwriting and ATM usage. The slower rate of adoption can be attributed to the greater number of participants, all of whom need to agree on the technology and business process standards that are required.

There is a high degree of interest in eMortgages among lenders. According to the lender survey, 44 percent of lenders expect their companies to implement eMortgages. Seventy-two percent indicated that they will implement eSignature technology, which analysts consider a leading indicator of market movement toward eMortgage adoption.

The research indicates that broad adoption could be in the not-too-distant future. Though difficult to predict, a critical mass of lenders could have eMortgage origination capabilities within three years. There are several assumptions that contribute to that finding – including a significant lender success story in 2007–08, and targeted educational efforts to address several issues that surfaced in the research.

To date, the industry has seen the creation of just over 1,000 eNotes. The E-SIGN legislation was signed into law in 2000. Many industry participants had expected eMortgage adoption to be further along by now. So why has it taken so long? Our research revealed seven perceived friction points that might be stymieing eMortgage adoption:

1. **eRecording**
2. **Security and privacy**
3. **eSignature laws and regulations**
4. **Market readiness**
5. **Consumer acceptance**
6. **Completeness of industry standards**
7. **Higher priority for other initiatives**

With so many potential benefits, why the slow rate of adoption? We used an interactive Web seminar to explore the friction points in more depth with research participants. (See Methodology, Clarification of Results for details.)

Lenders believe the benefits of eMortgages to be:

- shorter processing time
- competitive advantage
- reduced operational cost
- faster funding
- increased profit
- improved secondary market price
- improved data integrity

Perceived Friction Point #1: eRecording

FINDINGS

We asked: “How has county readiness to eRecord affected eMortgage adoption?”

Research participants responded:

>> **45%** – I don’t see the value of electronically signing mortgage documents without the ability to electronically record with the county. The immediate recordation of those documents is where the primary value of an eMortgage lies.

>> **31%** – A bifurcated process (having some documents eSigned, others wet-signed) adds extra work and cancels out the value derived from an electronic process.

>> **24%** – Electronic recording is required to originate eMortgages. Therefore, eMortgages are currently limited to those states and jurisdictions that allow electronic recording.

ANALYSIS

>> There is a significant perception that eRecording is required for efficient business operations and is essential for achieving value. Fully three-quarters of the respondents to this question have this viewpoint.

>> While this is a very tangible perception, experience at Fannie Mae shows that lenders have realized operational efficiencies without eRecording. A fully paperless mortgage that includes electronic recordation is a desired end state, but in practice we’ve seen lenders be successful without that capability.

>> There has been some misunderstanding about the definition of an eMortgage. Many research participants think that an eMortgage requires the electronic signing and recordation of the security instrument – the Deed of Trust or Mortgage documents. The terminology and nomenclature may be contributing to the confusion and misperceptions.

>> In our view, educational efforts would help clear up the terminology and value misperceptions.

Perceived Friction Point #2: Security and privacy

FINDINGS

We asked: “How have security and privacy issues affected eMortgage adoption?”

Research participants responded:

>> **66%** – I am concerned about the identity theft of my customers. Electronic documents, as opposed to paper, create a centralized repository of data vulnerable to a single breach.

>> **34%** – I am concerned about the ease of alteration of electronic documents, including the note and other key loan documents.

ANALYSIS

>> Analysis shows that lenders are concerned about identify theft and protecting nonpublic information. When we probed more deeply, we found that security and privacy are general topics of concern to the industry as a whole and not specific to electronic mortgages. Electronic mortgages are about a new electronic way of conducting business, so security and privacy are naturally topical areas of consideration.

>> Many current eMortgage practitioners believe that there are no unique security or privacy issues with eMortgages (with the possible exception of the document alteration concern raised above). In general, it may be that the participants in the research are expressing a general concern, and education may play a large role in addressing the perceived issues. The document alteration concern also may be addressed through education regarding existing document integrity technologies.

Perceived Friction Point #3: eSignature laws and regulations

FINDINGS

We asked: “How has the legal environment of eMortgages and eSignatures affected their adoption for you?”

Research participants responded:

>> **64%** – I don’t have a solid understanding of the eSignature laws, so this issue is a high priority for my company’s adoption of eMortgages.

>> **18%** – It is difficult to attribute an electronic signature to the party involved in the transaction.

>> **18%** – The lack of case law relative to eSigning mortgage documents is a problem for us.

>> **0%** – Electronic signatures are not currently legal in all jurisdictions.

ANALYSIS

>> Many lenders still are not fully aware of the existence and strength of the eMortgage legal infrastructure. The fact that there are new eSignature laws may be a concern for some participants because of the potential lengthy engagement with corporate counsel. Current eMortgage practitioners see the new law as beneficial, because it shows that Congress has specifically encouraged our industry to conduct business electronically.

>> Here again, the analysis shows that education can significantly reduce this friction point.

Perceived Friction Point #4: Market readiness

FINDINGS

We asked: “How has the overall readiness of the industry affected eMortgage adoption?”

Research participants responded:

>> **65%** – My key business partners (e.g., investors, closing agents, correspondent lenders, etc.) have not implemented eMortgages.

>> **23%** – A viable eMortgage solution that meets my needs is not available. I need an “in-the-box” solution.

>> **12%** – I haven’t seen a huge success story, so it seems too early for me to get involved. I don’t want to be an early adopter.

ANALYSIS

>> Lenders indicate that a prerequisite to their own eMortgage adoption is broader support among industry business partners – especially investors.

>> This finding is the one area that makes eMortgage adoption slightly different from the adoption of other technologies and business processes. The number of participants involved in a mortgage closing transaction and the level of interdependence among business partners creates complexity that is naturally slowing adoption.

>> In general, many lenders appear to be waiting for a significant success story – a major catalyst that would force their entrance into this space. These lenders are not the innovators or early adopters but are ones who will get involved when they perceive the market to be ready.

Perceived Friction Point #5: Consumer acceptance

FINDINGS

We asked: “How has the consumer market readiness affected eMortgage adoption?”

Research participants responded:

>> **79%** – Consumers are concerned about security and privacy issues.

>> **15%** – Consumers won’t understand or accept electronic signatures.

>> **6%** – The eMortgage process will be more complicated for consumers.

ANALYSIS

>> Analysis showed that lenders are simply concerned about the consumer reaction to this new way of closing a loan. They perceive the consumers to be reticent to electronically sign documents because of security or privacy issues.

>> In Fannie Mae’s experience, lenders who have implemented eMortgage programs report that consumers have been accepting of eMortgages and have not been reticent to complete the transaction with electronic signatures.

>> This perceived friction point may have more to do with the lender need to appropriately inform and position electronic signatures with their customers. Here again, help may come in the form of additional education.

Perceived Friction Point #6: Completeness of industry standards

FINDINGS

We asked: “How has the lack of completeness of industry standards affected eMortgage adoption?”

Research participants responded:

>> **62%** – The business processes between trading partners have not been standardized (e.g., custodians, warehouse lenders, servicers, investors, etc.).

>> **25%** – Industry standards are in flux. Some of the original standards that were put in place (e.g., SMART electronic documents) have been targeted for replacement with competing standards.

>> **13%** – There are gaps in the technology standards that have been developed that need to be filled.

ANALYSIS

>> The lack of widespread investor acceptance and the numerous investor delivery specifications for the eDelivery file make some lenders hesitant to invest until the industry standards are more widely accepted and implemented.

>> This perceived friction point appears to relate to the gap in business process standardization. While MISMO (Mortgage Industry Standards Maintenance Organization) has done a thorough job of developing technology standards, more work may be required to examine standard business processes for electronic mortgages.

>> Also noted was some concern about the state of the eMortgage technology standards. A new electronic document standard has recently been proposed, giving the perception that the technology standards are not stable and are still evolving. Some lenders don't want to implement too early because they are concerned about additional costs required when the standards stabilize.

Perceived Friction Point #7: Higher priority for other initiatives

FINDINGS

We asked: “Why have other initiatives had a higher priority?”

Research participants responded:

>> **35%** – Until I see broader adoption or a successful lender implementation, eMortgages will not rise to the top of the IT (information technology) project list.

>> **33%** – I don’t understand what I need to do to implement eMortgages.

>> **32%** – Other projects have shorter, less expensive implementation cycles and a clear ROI.

ANALYSIS

>> Analysis of this point showed a close relationship with many of the other points already covered. Lenders want to see a significant success story and broader adoption before committing resources and funding.

>> A third of the respondents said they found it difficult to understand what’s required to implement, clearly signaling a role for greater education.

>> A third also said that the expense and value were unclear, making it difficult to create a business case to justify the necessary resources and funding.

Friction Point Take-Away

Analysis of the seven perceived friction points yields four primary needs: Industry education, a significant lender success story, clearer understanding of the requirements for eMortgage implementation, and broader investor acceptance. These four areas must be addressed in order to resolve the seven friction points and accelerate eMortgage adoption.

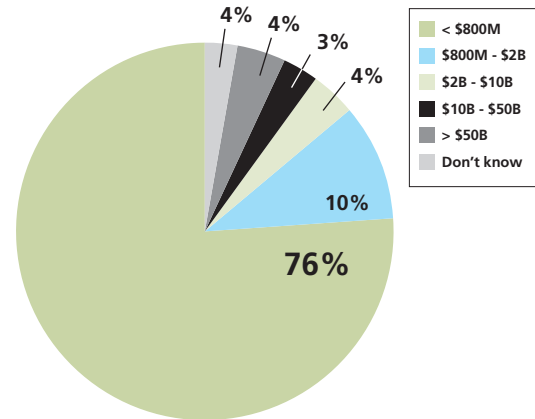
More Survey Results

Title and Closing Industry

The majority of title companies and closing agents think that lenders will drive Mortgage adoption because they finance the transaction and they have the relationship with the borrower. Title companies and settlement agents are making substantial investments in eClosing technologies to prepare for increasing lender demand.

Two of the top five title underwriters have eClosing solutions. These two underwriters control 40 percent of the title industry market share. Others are planning to offer or have sought out solution providers for their use. Most view eMortgages as a strategically important offering and are developing strategies to roll out eClosing solutions to their direct operations' title agents. Most closing agents see immediate value in eMortgages because they will be able to close more loans in a day due to shorter cycle times.

Figure 2. Lender Survey Respondents by Annual Origination Volumes



Summary

Fannie Mae found the results of the research clarifying in terms of further work required to foster this new way of doing business. In addition, it affords us a roadmap that allows the industry to determine whether the market is developing at a pace consistent with the predicted adoption.

Methodology

The eMortgage external research was conducted using three online surveys, three focus groups, and two sets of interviews. The participants in the research were grouped into three distinct populations: lenders (survey, interview); vendors (survey); and title industry – including title companies and closing agents (survey, interview, and focus groups). The research was designed and the findings were analyzed jointly by Fannie Mae and independent industry analysts. It is important to note that the majority of participants had not participated in electronic closings and had only surface knowledge of electronic mortgages.

Lender Survey (169 respondents; 13 questions): The majority of survey respondents were banks (state or national), credit unions, and mortgage bankers. Seventy-five percent of all respondents reported annual origination volumes of \$800 million or less (see Figure 2).

Lender Interviews (23 interviews; 13 questions): To obtain a richer set of information from the survey findings, we conducted 23 lender interviews, each 60 to 90 minutes long. The interview respondent group was representative of lenders with a broad range of origination volumes, and included many of the top originators in the nation. The majority of interviewees were not currently delivering eMortgages to Fannie Mae.

Vendor Survey (23 respondents; 8 questions): Vendors supported technologies involved in all stages of the life of a loan.

Focus Groups, Interviews, and Surveys of Title Companies and Closing Agents Conducted in Partnership with the American Land Title Association (ALTA): 3 focus groups; 1 closing agent survey with 160 respondents and 14 questions; 8 title company interviews with 12 questions.

Independent Industry Experts' Analysis of Results: Craig Focardi of The Tower Group and Carmelo Bramante of CDB Consultancy were key analysts in the Fannie Mae-sponsored research. Both were instrumental in the design of the research and interpretation of results.

Clarification of Results: Fannie Mae hosted a Web seminar for 48 of the lender and vendor research participants to provide richer detail around the "Seven Perceived eMortgage Adoption Friction Points."

Definitions

For the purposes of the research, we used the following definitions:

eMortgage: A mortgage loan that includes electronic signatures on one or more electronic closing documents.

Paperless Mortgage: A mortgage loan that is electronically processed, closed, signed, and sold/delivered, if applicable, by paperless means on an end-to-end basis. An eMortgage is a component of a paperless mortgage.

Our intent in providing these definitions was not to change the industry standard definitions, but to simplify the explanation of an eMortgage for the purposes of obtaining precise and comprehensive research responses.