

# MISMO

A "Time and Motion" Study

EXECUTIVE SUMMARY

CONDUCTED ON BEHALF OF THE  
*MORTGAGE BANKERS ASSOCIATION*

BY

*CC PACE*

AND

*THE STRATMOR GROUP*

OCTOBER, 2004



## INTRODUCTION

In 2004 the Mortgage Bankers Association (MBA) commissioned a study by CC Pace and The STRATMOR Group to demonstrate to the lending community the value of adopting the MISMO standards, encouraging their immediate movement towards adoption. This initiative has resulted in an economic study of the mortgage transaction to measure and assign value to the application of MISMO standards to these activities from both a human resource and a capital expenditure perspective. These measurements tell a compelling story to the mortgage lender and other industry players that the application of MISMO data standards today will begin to reap real benefits in time, money and quality. As adoption rates continue to grow the benefits will begin to multiply.

The economic study was accomplished through a combination of practices including interviews, site visits and surveys. Data gathered in the course of this study clearly supports the case that broad adoption of the standards can dramatically lower origination costs for the lender and borrower alike. The study shows that direct costs can be lowered by as much as \$249 per loan, approximately 75% of which directly benefits the lender. In addition, the surveys show that execution costs can be improved by as much as 15.38 basis points, a 25-50% pickup in retail lending margins or \$450 for the average loan.

The study also demonstrated that while data standards are too often incorrectly perceived as a purely technological interest, some of the greatest values were seen in their ability to reduce manual activities, increase data accuracy, lower the costs of third-party services and improve a lender's competitive positioning in the marketplace. Seamless internal and external interfaces act as enablers to process improvement and improved service levels. Data standards also help lenders measure performance distinct from the impact of poor data quality and improve accountability and transparency in financial reporting. As the study clearly demonstrates, adoption of the MISMO standards should in fact be an important business priority for all lenders seeking greater operational efficiencies and the agility needed to compete effectively in a dynamic market.

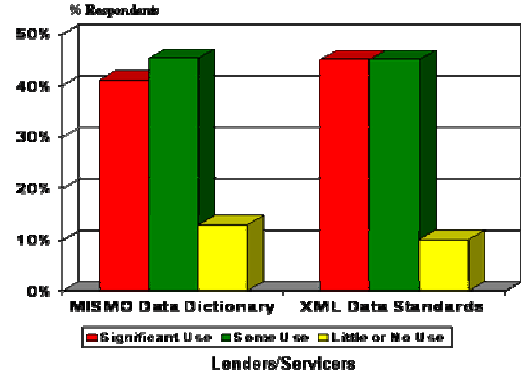
## SUMMARY OF STUDY FINDINGS

The survey was sent to all MISMO listserv participants, Campus MBA and MBA NewsLink email recipients and was posted on the MBA and MISMO web sites. After eliminating duplicates, responses received totaled 45 for lenders/servicers and 80 for vendors/suppliers.

Lender respondents claimed average time savings of over 16% and cost savings of over 15% when using MISMO standards in their last systems integration project. Over 80% of survey respondents are planning on using MISMO in some way in the immediate future.

|               | MISMO Data Dictionary |                | XML MISMO Data Standards |                |
|---------------|-----------------------|----------------|--------------------------|----------------|
|               | Time Savings %        | Cost Savings % | Time Savings %           | Cost Savings % |
| # Respondents | 12                    | 10             | 10                       | 10             |
| Simple Avg.   | 17.80%                | 15.46%         | 15.48%                   | 15.07%         |
| Wtd. Avg.     | 10.54%                | 12.97%         | 9.65%                    | 9.14%          |

Lenders/Serviceers



Lenders estimate that in a virtually electronic industry (the achievement of which will require an industry standard such as MISMO) direct **origination costs will be reduced by \$249** across the touchpoints/functions surveyed. About 75% of these savings will benefit lenders.

| Touchpoint/ Functional Area | Current Costs      |                    | Projected Savings     |                       |               | Savings Allocations |              |
|-----------------------------|--------------------|--------------------|-----------------------|-----------------------|---------------|---------------------|--------------|
|                             | Item/ Service Cost | Data Movement Cost | Item/ Service Savings | Data Movement Savings | Total         | Lender              | Borrower     |
| Credit Report (20)          | 16.65              | 2.32               | 3.23                  | 1.42                  | 4.82          | -                   | 4.82         |
| Appraisal (15)              | 283.67             | 7.64               | 33.33                 | 6.85                  | 42.07         | -                   | 42.07        |
| Title Search (13)           | 210.00             | 7.62               | 9.00                  | 7.64                  | 16.73         | -                   | 16.73        |
| Flood Cert (13)             | 19.31              | 1.36               | 6.86                  | 0.40                  | 7.75          | -                   | 7.75         |
| Closing Docs (13)           | 29.67              | 8.69               | 11.33                 | 5.69                  | 16.15         | 16.15               | -            |
| Mortgage Application (13)   | 226.00             | -                  | 161.88                | -                     | 161.88        | 161.88              | -            |
| <b>Total</b>                | <b>785.29</b>      | <b>27.63</b>       | <b>225.64</b>         | <b>22.00</b>          | <b>249.40</b> | <b>178.04</b>       | <b>71.36</b> |

Based on the survey, execution costs are estimated to improve by 15.38 bps in an electronic industry. Based on an average loan of \$180,000, and when execution pickup is taken into account (15.38 basis points on a \$180,000 loan is \$276.84), overall lender margins are expected to improve by more than \$450 per loan, representing a 25%-50% pickup in retail lending margins.

|                                   | Bps   | \$/Loan       |
|-----------------------------------|-------|---------------|
| <b>Income Benefits:</b>           |       |               |
| Execution pickup                  | 15.38 | 276.84        |
| <b>Total Income</b>               |       | 276.84        |
| <b>Direct Expense Reductions:</b> |       |               |
| Credit Report                     |       | -             |
| Appraisal                         |       | -             |
| Title Search                      |       | -             |
| Flood Cert                        |       | -             |
| Closing Docs                      |       | 16.15         |
| Mortgage Application              |       | 161.88        |
| <b>Total Expense Reductions</b>   |       | 178.04        |
| <b>Net Direct Income Pickup</b>   |       | <b>454.88</b> |

The survey focused several questions on the opinions of the respondents regarding the perceived value and future of MISMO:

- ✓ Over 80% of agree that the use of MISMO standards will *reduce their cost* across all business operations.
- ✓ Over 67% agree that MISMO standards provide them with internal efficiencies.
- ✓ Over 80% agree that MISMO standards will reduce their system development costs.
- ✓ Over 85% agree that MISMO standards will reduce data entry and re-entry costs.
- ✓ Over 76% agree that MISMO standards will reduce costs related to poor data accuracy/data integrity.
- ✓ Over 66% agree that MISMO standards will reduce the cost of services provided by third-party vendors and suppliers.
- ✓ Over 61% agree that MISMO standards will improve their competitiveness. Almost 30% are neutral, whereas less than 10% disagree.

Only 16% claim not to have the resources to adopt MISMO standards.

## OPERATIONAL AND ORGANIZATIONAL IMPACT

### OPERATIONAL

As we tie back specific findings to the functional areas in the mortgage process, the systematic application of MISMO demonstrates specific concentrations of cost minimization and quality improvement that can help your organization receive profit maximization.

There are multiple themes that are consistent through all functional areas:

#### Efficiency

A recent speech at the FNMA technology conference by Michael Williams (President Fannie Mae eBusiness) calculated the cost of re-keying data during the origination and fulfillment process to be an average of \$460 per loan. MISMO will enable the ability to move data between the lenders, agencies, and MBS investors, improving the overall efficiency of the capital market by substantially improving the quality of data investors will have available to make decisions on.

Seamless interfaces between internal systems and outwardly to service providers and trading partners enable companies to change processes more quickly to adapt to an ever changing business environment, taking advantage of new opportunities as they arise (such as a better price/service from service providers

#### Corporate Governance/Disclosure

Due to Sarbanes-Oxley, the need for information transparency in financial reporting has become more critical than ever before. Adopting the MISMO data standard may decrease the risk associated with individualized

interpretation and enable companies to be more accountable and transparent in their financial reporting. Data standardization combined with improved data quality will help lenders clarify performance results attributable to management (rather than unavoidable bad data). This, in turn, improves corporate governance accountability and will also improve investor confidence.

### Data Integrity

The data integrity associated with standards is critical for lenders in their compliance efforts. Data integrity issues manifest themselves in multiple ways, including high labor costs for error detection and resolution, compliance risk and reduced marketability due to the proliferation of bad data across multiple systems.

Along with the integrity of common data definitions, MISMO also enables the transfer of data across multiple internal and external systems without the risk of modification or translation. Deployment of reusable MISMO interfaces with industry participants will allow organizations to use those interfaces, processes, and transactions throughout the organization, minimizing errors and increasing data reliability.

A study commissioned by a large industry vendor, showed that certified, correct data could save a large lender from \$20-40 million annually. Use of MISMO standards can ensure that correct data at the beginning of the process always stays the same throughout the entirety of the process.

### Interface Development

There are many factors that contribute to the substantial savings derived in development costs from MISMO adoption:

- ✓ The logical data dictionary (LDD), with over 5000 terms and valid values defined, can reduce upfront analysis by as much as 90%.
- ✓ The delivery mechanisms for sending and receiving data (the “enveloping”) are similar across all data sets
- ✓ Modification of interfaces, adding or removing data, will take no effort as the interface is already prepared to handle it.

### Vendor Management

Easy/low-cost interfacing with mortgage services vendors will materially reduce or eliminate the barriers to switching, leading to intensified competition between providers and resulting ultimately in both lower costs and higher service levels. If lenders were able to easily establish MISMO interfaces with lower cost service providers, respondents estimated that they would save, on average, \$51 per loan.

## ORGANIZATIONAL

The study shows that the positive influence of MISMO go well beyond operations. In creating the MISMO standard, the industry participants also worked towards a common interpretation of legislation such as eSign and

UETA. These are significant pieces of legislation that are still awaiting legal challenges that are ironically an important part of establishing precedence regarding the appropriate legal interpretation as viewed by the courts. While MISMO plays no direct role in establishing such precedence, adopting the MISMO standards may reduce a lender's risk associated with misinterpreting the legislation by demonstrating that the lender's interpretation is aligned with the generally accepted views of the industry in lieu of a formal legal precedence.

A number of organizational areas will be impacted directly, and positively, by the use of standards, as well.

### **A More Efficient, Reactive Organization**

Internal operating efficiencies achieved through use of MISMO standards can transform organizations, making them more nimble and able to react more quickly to changes in the marketplace. Organizations enabled by MISMO standards can leverage their existing technology and interfaces to make business decisions quickly, and that agility will enable them to become more competitive.

MISMO standards allow lenders to take advantage of new service providers with lower fees, for example, faster and at less cost by reusing interfaces developed previously for other MISMO compliant vendors. The survey found that MISMO standards will thereby reduce the cost of third-party services.

Lenders will be able to make business decisions without consideration to interface limitations and take advantage of potential revenue-maximizing opportunities created by increased competition in the marketplace. Additionally, there will be opportunities for the organization to grow into new territories (e.g., new markets, new products, and new channels) that will no longer be derailed by a company's inability to adapt to new technical frameworks. Survey respondents have highlighted reusability as a key advantage of MISMO, allowing lenders to build one interface that can be reused with multiple investors. Lenders can thus broaden their product offering and quickly establish relationships with new investors.

### **An Organization Aligned With the Industry**

Infrastructures built today that take advantage of MISMO interfaces and standards will provide the foundation for industry participants to be aligned with future initiatives that will further streamline and improve the mortgage process. Currently, MISMO is at the core of a number of different activities being pursued by the industry, including eVaulting and SMART documents and, ultimately, eMortgages. Organizations that adopt MISMO standards now are on the fast lane to take advantage of benefits derived from widespread adoption of those initiatives.

The ability then to quickly analyze and take on new opportunities brought forth by the industry will allow lenders to concentrate in other areas of the business, which too often suffer (e.g., lack of resources, lower prioritization) due to attention-grabbing initiatives on higher priority areas.

## Impact on Process Automation

MISMO standards are enablers of automation, and automation is becoming more and more desirable in an industry that spends millions of dollars as a result of data errors, inconsistencies, and overall data-related issues. Most technical initiatives taken on by corporations deliberately pursue a high level of process automation aimed at reducing cost caused by errors and inefficiencies associated with manual processes. It is not a surprise that most survey respondents truly believe that MISMO will reduce data entry and re-entry costs, a goal that MISMO shares with other industry initiatives.

While most organizations today have a relatively large number of automated processes, those processes are not as flexible as they could be. Changes in specifications on custom interfaces, for example, require a significant effort to analyze, build, and deploy. When MISMO standards are used, as survey respondents point out, processes become more efficient and easier to maintain and deploy. Also, when MISMO standards are used there is less chance of specifications changing unilaterally (i.e., changes generated by one side of the process that the other side may not necessarily agree to). Changes to MISMO specifications are proposed and analyzed by a number of different workgroups before they are ever implemented. Participants in those workgroups, made up of industry players (e.g., lenders, vendors), have a say in what gets adopted, when, and how. Risks associated with changes get discussed and minimized. Current and future automated processes that take advantage of (and rely upon) specific standards are identified, and the impact on those processes is assessed and discussed.

If automated processes that do not use standards are compared with similar processes that take advantage of current MISMO standards, there is no question that those processes with MISMO as a key component have a higher degree of maintainability, openness, and reliability. To this point, survey respondents agree that MISMO definitely lowers development costs, which are a key component of any process automation.

## CONCLUSION

While no one argues the obvious value that data standardization would have in the mortgage industry, adoption is not occurring at the rate necessary for achieving optimum benefits.

Agreeing as an industry to data definitions and standards will allow organizations to spend their time and energy focusing on unique and core competencies that can truly differentiate a lender from its competitors.

The responsibility of proliferating the standards throughout the mortgage industry belongs to all of its participants: lenders, vendors, service providers, investors and associations. The full study discusses several initiatives incentives and recommendations to be taken on by the MISMO organization or other third party, in order to foster widespread adoption of MISMO standards in the mortgage industry.

Most if not all industries in which standards are implemented quickly begin realizing the benefits of standardization. Having a common language, whether it is a commonly agreed-to data dictionary or a set of specifications

for electronic transmissions – or both -, brings industry partners together, eliminates confusion, improves data reliability, and ultimately has a positive economic impact on the industry as a whole, as well as on the individual participants.

In most industries, there is a group of early adopters that clearly understand the benefits of standardization in their particular niche. For these early adopters, that understanding comes mostly from the altruistic belief that standards are “good”, even though at the time of implementing those standards there may not be enough empirical data to justify the investment necessary to create and adopt those standards. For these early adopters, the rewards will come later, and they believe the rewards will indeed be there.

Most of the time, though, businesses need to understand the economic drivers for adopting such standards – especially since adopting those standards will for most people cost money. The more difficult it is to formulate the economic benefits of adopting and promoting standards, the harder it is for an industry to convince its participants that they should do it.

This study presents clear evidence, as reported via surveys by a wide variety of players in the industry, that using MISMO standards (data dictionary and XML data standards) results in significant savings throughout an organization. Those savings, when possible, have been quantified and presented here in the executive summary, and in greater detail in the full study results.

The survey has shown that there are significant efficiencies and cost reductions in real estate finance as a whole as a result of the standards. These gains are already being recognized by lenders in the form of reduced costs and compressed times from loan application to closing, by borrowers as low upfront costs in mortgage acquisition, and by investors as improved data and investment analysis quality. MISMO is an enabler of Straight Through, or using the newest lingo, “Lights Out” Processing. Transferring data instead of paper would save considerable process time and greatly reduce errors, and the industry will not get there without standards.

Organizations need to understand the true strategic advantage that adopting MISMO standards will help them realize. In times when technical innovations are helping industry participants become more dynamic while facing an increasingly competitive marketplace, those companies that are “built to last” are the ones that will survive. MISMO standards provide the foundation to create the necessary dynamism in those organizations. Those who react quickly and adapt to change, some positioning themselves as innovators, will gain benefits that are unattainable to those that cannot (or will not) adapt to new paradigms.

The most difficult part of creating standards in the mortgage industry has been getting consensus between the corporate counsels, the business, the engineers and the economists. This has now been accomplished and the foundation set, clearing the way for industry players to realize the real benefit of setting standards, reaping the rewards of execution.

In order to continue moving forward with the creation and adoption of standards, mortgage industry participants need to work together. It has been demonstrated over the years that only those standards that have been created in a collaborative way by the industry to which they pertain will

succeed. It is therefore up to you, whether you are a lender, a vendor, a GSE, or another industry player, to take action and do your part.

MISMO as an organization is committed to not only continuing creating and maintaining industry standards, but to fostering widespread adoption of those standards. With MISMO's help, organizations should embrace and implement the standards as a simple yet powerful economic decision.