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Too Many High-Touch Lending Processes? How to Offer Instant Pre-Qualification, Cut Underwriting Costs By 78%, and More

David Stoddard: Good morning, good afternoon, or good evening, depending on where you are in the world, and welcome to today's webcast, Too Many High-Touch Lending Processes? How to Offer Instant Pre-Qualification, Cut Underwriting Costs By 78%, and More, brought to you by Bank Systems & Tech, IBM, and broadcast by United Business Media, LLC. I'm David Stoddard, today's moderator. And we want to make sure this event is as interactive as possible, so I'd like to make a few announcements before we begin.

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Okay, now on to the presentation, Too Many High-Touch Lending Processes? How to Offer Instant Pre-Qualification, Cut Underwriting Costs By 78%, and More.

Joining me today are Craig Focardi, Senior Research Director, Consumer Lending at the Tower Group, a subsidiary of Corporate Executive Board. He works in Tower Group's consumer lending advisory service where he advises clients on the strategic application of technology for mortgage and consumer lending industry, financial institutions and technology providers. Craig covers a wide range of business process, strategic and technical topics related to mortgage loan origination, loan servicing, securitization, outsourcing and risk management.

We also have Joe Boissy, Director of Business Agility and Websphere Industry Marketing at the IBM Software Group. He is responsible for the overall go-to-market strategy for all verticals and cross-industry solutions for the entire Websphere product suite. He comes to IBM through the ILOG acquisition where he was the Vice President of Marketing. Joe brings over 20 years experience, with a strong background in the financial services industry. He has developed many solutions that are currently implemented and deployed.

So it's my pleasure to hand off the presentation now to Joe and Craig.

Joe Boissy: Thank you. Thank you, David. This is Joe. Glad to be here. And good morning, good afternoon, good evening, everyone.

This is part of a series that we've started in fact back in 2010, but we're starting a new series in 2011. Please make sure, if you haven't subscribed yet, that -- to make sure that you can look at the other part of this series that we have.

As David mentioned, we have today with us Craig Focardi from Tower Group, and we're delighted to have Craig. We've worked with Craig many years, back in the heydays of the mortgage lending, and also we worked of course when the economy was not so good. And of course the questions that would come to mind today is that, what's happening today? How are people dealing with lending processes, many touches, of course, and how to deal with the situation today with ever-increasing regulations?

And so the way we're going to work it out today, Craig is going to spend some time with us sharing his insights, his views on what's going on, both from the business and the technology side. Then I'll take over with a couple of examples from customers, with specific customers. And then we'll go with the Q&A.

So without further ado, please, Craig, the floor is yours.

Craig Focardi: Okay, great. Thank you very much, Joe. And good day, everybody.

The topic Too Many High-Touch Lending Processes? is very timely because credit risk management and now regulatory compliance controls, although necessary, have bogged down lending processes. They've also increased loan origination processing costs for lenders, and they've reduced service to the end-customer.

Further, future and ongoing regulatory compliance enhancements, including the Truth in Lending Act that affects all the areas of consumer lending, and also consolidation of consumer protection regulation under the Dodd-Frank Act within the Consumer Finance Protection Bureau will put even more controls and pressures on lender costs and customer satisfaction.

And so with that as a background, today I'd like to address three aspects of this topic. So I'll segment my comments into three areas. That is, what are the industry business drivers that -- such as flat lending growth, that are challenging lenders both operationally and technologically? With that, then I'll focus on lender strategic responses. What are their issues and their pain points? And what should and what can lenders do in response? And then finally, I'll touch on what this means for technology evaluation and usage as a lead-in to Joe's comments.

I think my overarching conclusions and recommendations are that -- first, that manual data and document hand-offs and processes can introduce errors and slow down processes. Second, in a low lending volume environment, lenders need to compete on speed, service and efficiency to capture customers and preserve profits. And then finally,

lenders need to automate through rules management and process management to counteract the increase in labor costs per loan that they've experienced as a result of the new risk management and compliance controls.

So that's the setup and the quick overview. Let's take a look at some of the key business drivers in this area.

First, by business drivers here, I'm focusing on those specific to consumer lending. There are, of course, broader business drivers such as the economy, job growth, interest rates and etcetera affecting all industries. Second, when I say consumer lending, I'm referring to all areas of consumer lending -- auto lending, home equity, mortgage, personal lines and loans, and student lending.

Then finally, let's take a look at the issues that affect all of those areas -- increased loan data and documentation requirements. Certainly, the first mortgage sector is the most affected in this area, but also in home equity.

And credit quality issues have affected every sector, and so there are increased data and document requirements from federal regulators, state regulators and issuers of asset-backed securities and mortgage-backed securities. And this data is required to improve credit quality and quality control. And so it's going to be a new permanent part of the landscape. And it ought not to be something that slows down the lender's interaction with the end-customer, but it needs to be accommodated.

Third, new regulatory disclosure requirements. I mentioned a few of those. Some of those require new data. Most of them will require a change in process, and sometimes new or different documents. And so, workflow and rules management around what documents to present and when becomes increasingly important in this environment.

And then finally, lenders are shifting from broker or indirect channels to increased retail channel activities, whether it's branch level, call center, or Internet direct. And that's also a means to control credit and regulatory risks too. And so, rules need to be automated and processes -- new processes need to be implemented in areas of the retail channel that are, for some institutions, the primary source of new lending environment.

Regulation, in particular, is a huge business driver. So let's take a look at this more closely. Now, compliance is, in my view, is a necessary evil. Many aspects of it are non-discretionary in terms of fulfillment. I think the spending on automation is where things get -- are discretionary. But overall compliance, although some of it may be well-intentioned, parts of it may be ill-conceived, but many parts of it I think are very necessary to increase industry credibility and consumer trust in the industry again.

And one other key theme that I've seen develop over the last couple of years, and this is both, I think, from a regulatory perspective and as well as one from the ABS or mortgage-backed security investor market, is this philosophy about the quality of the loan in terms of the credit risk, the regulatory compliance issues, the documentation, etcetera.

And that philosophy is one from "Don't ask, don't tell" about what's in the loan file and 10% review of individual loan files that are sold into the secondary market, to "Zero tolerance and zero defects." That is, every loan today is going to be scrutinized in great detail both by the lender while they're creating it and as well as by the end-investor and even end-regulators after the loan is completed.

And so for these reasons, this permanent shift in risk management is going to drive lenders to either incur lower profits on their loans or need to find new ways to automate these processes in order to maintain good customer service, process loans fairly quickly, as well as manage risks.

Let's take a look at another business driver, and I touched on this earlier, and this has to do with growth rates in the consumer lending area, to see if they're going to help or hinder lender revenues and lender strategies. Now this exhibit shows historical and Tower Group estimates for new consumer loans originated by loan type through 2013. The key point is that in most consumer lending segments, except automobile lending, growth is essentially going to be flat, slightly down, slightly up, or really about the same this year and the next two years. And so, a rising tide will not lift all lenders' boats as far as achieving their goals in the coming years.

In the auto sector, which you can see there in the blue line, sales rebounded in 2010 off of historical lows, and this trend is continuing strongly in 2011. And so that's some good news there.

Also in the student lending sector, in the red line, you can see the number of new loans being originated by year. And the key driver of student lending is two-fold. The first one really is demographics, the percentages around the number of students, the numbers by age that tend to enroll in college, is fairly steady. It's somewhat responsive to recessions, but it's pretty predictable.

The second thing -- aspect of student lending, is that the cost of education continues to go up, and so the loan amounts for borrowing go up as well. And so loan growth will outpace enrollment growth due to this increased cost of education. In some cases, students will get more than one loan, and Tower Group forecasts that loans per student will increase from 1.2 last year to 1.6 by 2018.

Now on the bottom there, you can see automobile lending and home equity lending. And I think we all know the story there. There's a continued negative impact of declining and weak home prices and high default rates and high credit risks and the lack of job growth. And so, despite historically low interest rates, volume is likely to remain low for the next couple of years. The bottom line is that lenders in all areas of consumer lending will need to alter their product strategy, their processes, their systems if they want to grow.

Now let's take a look at what lenders need to do in their internal operations and with the technology and with their strategies in order to combat these business drivers. These are

four major pain points that lenders have, especially in the mortgage and home equity lending sectors.

There are a lot of credit risk issues, as we know, so the need to improve credit quality and data and document quality is clear, but they resulted in increased documentation requirements, consumer disclosures and repeated loan reviews throughout the process. And so you have this constant process of checkers checking checkers. If you can capture the data quickly and efficiently from the consumer at the point of sale and process it efficiently, you'll do it at lower cost and close more loans.

This manual work that's current -- that a lot of lenders are doing currently though, is increasing processing costs per loan. If you take a look at the exhibit on the right, it shows how loan origination costs have increased in the mortgage sector. There are two axes here.

The blue bars, measured on the left y-axis, show there's a constant rise in direct processing costs per mortgage loan since 2002. There was a slight drop in 2009, but still those levels remain near their historical peak. And as a result, consumers are increasingly frustrated and voting with their feet. They're looking for loans with a different lender. As a result, fewer loan applications are converting to closed loans.

The gold line, on the right y-axis, shows the conversion rate, the number of apps that convert to closed loans, and how that has dropped significantly over the last few years.

Now, let's take a brief look at critical decision points impacted in the loan account opening process, and I think Joe will touch on these briefly when he gets into his portion of the presentation. The exhibit at the right shows basic flowchart activities and decisions by customers, sales people and the customer service group. There are too many manual and repetitive decisions in the loan account opening process, such as borrower qualification, loan underwriting, and document verification.

Many lenders still lack the ability to receive data and documents from consumers electronically or digitize this information into an electronic workflow, and synchronizing that with analytic decisioning processes. And these disconnected workflows result in processing errors, increased compliance risk and slow service. And so these are precisely the issues that lenders need to address and fix.

Now let's take a look and see what this has done -- these challenges have done, to customer satisfaction and why it's so important that automation fix these issues. This exhibit shows the impact on customer satisfaction throughout areas of banking -- cards, mortgage origination and servicing, retail banking, and automobile finance. Here, I've summarized the results of J.D. Power customer satisfaction surveys by banking line of business, going all the way back to 2005 for some measures.

The blue arrows on the right indicate the recent trends in customer satisfaction, with the lower numerical score meaning declining satisfaction. Fortunately, in the automobile

sector, credit has been easier to come by lately and demand has come back. The loan processing is a bit simpler than the real estate sector. And so that aspect hasn't slowed down as much as some of the areas. And pricing is good, interest rates are low. So, customer satisfaction appears to be up.

But mortgage lending satisfaction is still declining in both origination and servicing, and it will be interesting to see the 2011 survey results. I suspect that those numbers will still continue to trend down.

And so, clearly, customer satisfaction is a significant problem, and I've addressed qualitatively why I think that's a problem, but here are some quantitative statistics to support that. Here, I've mapped other J.D. Power survey results for mortgage loan origination to show how processing timelines have skyrocketed since 2008. You can see along the y-axis there the days from mortgage application to loan closing. And for '09 and 2010, the data is segmented by app-to-approval and approval-to-close, and you can see the number of days within each of those bar segments. For 2008, I just have the total data there.

And so you can see that the total days to close has increased from 30 days three years ago to 52 days last year. You can see that this is especially true for the loan application to approval process. I've also indicated the customer satisfaction ratings across the top, and it sure seems that the two metrics are closely correlated.

So, those are the strategic issues, the pain points that lenders need to address.

Now let's take a look and turn to the tech issues and the solutions that institutions ought to be looking at, and here again I'll focus my comments in the pre-qualification and processing and underwriting areas that relate to business rules management, process management, and imaging and content management.

And these are some recommended strategic responses for lenders that have a direct impact on what technologies they ought to adopt. First, increasing new risk assessment needs with new data and analytics, and increasingly, lenders want to apply these analytics closer to the point of sale and closer to the pre-qualification process. Similarly, lenders need to combat new regulations with rules management and document management automation. And this requires business process management tools to sync data and document processes with each other.

Third, and I've touched on this throughout the talk, they need to improve their customer interaction, service standards and speed, and apply technologies that do that. And then finally, they need to re-examine their core processes with their loan origination systems as well as the integrations between those core systems and their subsystems that drive key decisions and customer interactions.

So those are the key strategic responses with technology implications here.

I just want to touch on briefly Tower Group's top 10 technology initiatives for consumer lending in 2011. And our methodology here is to show how industry business drivers affect strategic responses which lead to the technology initiatives that lenders ought to adopt. And this is a broader-based approach than what I've shown today, with some additional drivers and responses, but I want to show the methodology and how it leads to a number of technology initiatives that impact consumer lending.

But here I want to focus on the three tech initiatives that I've highlighted in bold. And these are the ones that Joe will address in his talk -- integrated credit collateral and fraud risk management. This is both a back-office process as well as some components that directly affect customer interaction. Secondly, data management for business intelligence, which consumers are eligible for which loans and at what price? And then finally, analytics for loan decisioning in order to ensure that customers meet a lender's credit quality requirements.

And so these are the key issues that are going to help lending institutions attract customers, secure them and close loans that are profitable for the lender and appropriate for the end-consumer.

So, now let's take a look at these specific technology initiatives within the context of lending processes. This exhibit focuses on the impact of the Dodd-Frank Act on lending processes and technology, both from the initial marketing through portfolio management. And here I've segmented some of the activities by process -- disclosures, analytics, reporting data, and platform. So this is a broad-based schematic for how -- for the kinds of things that lenders need to do specific to regulatory compliance change.

And compliance is having the dual effect of absorbing resources and priorities, but also rekindling interest by lenders in both core systems replacement as well as workflow and decisioning enhancements to ensure compliant processes, but also to capture consumers at the point of sale.

Next, let's drill down more into this issue into loan origination, with a specific focus on rules management and processes. And here, this exhibit looks at specific subsystems across processes. So you have lead generation and point-of-sale systems at the point of sale, and then other systems for processing and underwriting, closing and post-closing.

If you look at the location column there, you can see that these particular systems, many of these are external to the lending operation, in many lending shops. Now you have a lot of internal dedicated systems that are utilized across origination from point of sale to closing and post-closing. And so you've got external systems and internal systems, some of these systems are core, others are subsystems that need to integrate with the core systems.

Within large diversified institutions, you also have internal systems but they may be shared across areas of consumer lending or across the broader bank. And so for that reason, it's particularly important that you have integration and process management and

rules management bringing these systems together in order to have seamless processing that will help shorten those consumer timelines that are reducing customer satisfaction and is increasing costs to both -- to the lender.

So now let's take a look at specific systems and integration at a high level before I turn things over to Joe. And here I just want to take a step back at a higher level from the previous exhibit and show the key systems and processes that lenders have across consumer lending. And that rules management systems and BPM, to tie those together with the core processing systems, and in some cases, the enterprise content management, or ECM systems, is the new paradigm for lenders that want to be able to process loans quickly and efficiently.

And even though lending volume is low today for institutions that can increase share or that do want to position themselves for when markets do come back and begin to grow, this kind of schematic will enable them in order to position themselves for much more rapid growth when it occurs.

And then, so, to just summarize what -- the topics I've addressed today, growing risk and compliance requirements are driving demand for better data and analytics, and lenders need rules management and integration and workflow in order to integrate and make that happen, both to satisfy external regulators and investors as well as internal lender risk managers, and also to satisfy customers.

The smaller lending markets mandate speed and service to convert leads, scarce leads, to applications and the customers. And the only way to effectively do this is through automation, which is going to prepare lenders for the return increased loan volume that they want, and also product diversity. Many loan products today are far simpler, and lenders would like to differentiate themselves in the future and bring back products they're not currently offering. And that too can only be facilitated effectively through automated risk management and decisioning systems.

And so with that, I'll turn things over to Joe. Joe?

Joe Boissy: Thank you. Thank you, Craig. This is a great -- it was great insights that you gave us here. Unfortunately, it doesn’t give us, you know, the picture, not that easy, you know, given where we are today and given what's happening. It tells us that, yes, maybe in the auto business, things are getting better. But in the mortgage business, things are going to be flat. And therefore, there is a lot of challenges that we have to face today in order to cope with these challenges.

So, what I'd like to do over the next 10 to 15 minutes is simply give you a couple of examples of customers that are implementing solutions and how these solutions are helping to cope with these challenges. But before doing that, I'd like to simply maybe do some level-setting here by talking about, again, this chart that you see here, is more like a repeat of what we just heard from Craig, about solid situation, manual, intensive, or loan origination processes. You have a lot of things like repetitive systems. You have on top

of that regulations are making things much tougher. And on top of it, you have lack of visibility and lack of control. So, that is more like the situation that you face more or less, many big financial institutions today.

And so I'd like to use the opportunity now to, before I give a couple of examples, just to level-set on a couple of technical terms that you heard from Craig, BPM and BRMS.

So, what is BPM? BPM stands for business process management. And sometimes it's used interchangeably with something bigger, BPMS, but the bottom line is that BPM is a set of tools, software tools in fact, that would help a customer, would help, in particular, a bank here, to manage their processes. By that, we mean everything from inception to settlement, all the tasks that has to go, all the stages from one, from step to step. But in order to orchestrate that, you need to also talk about modeling the process, look in the process, monitoring the process, and of course executing the events within the process.

Now if we took a closer look, there's something in red in this chart, that you see in the middle, that's rules. And when we say rules in general, we're not talking about the traditional way of thinking about rules, which is a rule engine, some engine executing rules.

What we're talking about here is something we call BRMS, and BRMS stands for business rules management system. And by management, we mean we're not talking about traditional rules that are embedded within the applications sort of encoded in an obscure programmatic code. We're talking about business rules written by business users for the business itself.

For example here, we're talking about rules for auditing, rules for pricing, rules for eligibility written by the loan officers, by the risk managers, etcetera. And I will insist on that because, again, in the old days, the technology did not allow us to do that. But today most of our customers, 90% of the rules are written by the business users.

And so, we're talking about a repository that has these rules, but on top of that, you have also the execution of the rules, of course the rule engine, but also you have all the authoring of the rules, the maintenance of the rules, the monitoring, the reporting of the rules. That whole thing is called the BRMS.

So with that, now I would like to cover the couple of examples that I have here. I'm going to start with GE Money Bank, one of our customers. And their situation is not different from many other situations that I'm sure you're familiar with. So, GE of course is one of the, you know, General Electric's largest growth engines. They have lending products, revolving lines of credits, equipment leasing, and they have cash flow programs, asset financing. And they play a role both in consumer and commercial finance. And they are international. They work in 35 countries.

So they needed to streamline their processes, of course, to operate more efficiently and sustain the growth, at the same time, sustain also the new regulations that we're talking

about. So what you typically start with a situation is that you have lots of documented processes and operations, you have a lot of process inconsistency, duplications, non-compliance, non-standardization, etcetera.

So what they did is very simple. They started using one of our products which we call -- it's called Websphere Business Modeler, to do what we call the modeling of their existing situation. So instead of going and starting, "Okay, let's build a new super-process," let's understand what the process is. And those of you who worked in BPM before know the very first stage you have to do in this kind is just model, understand where you stand today.

And so you see here, what they did is they looked at their processes and they looked across their channels and see -- so, what happened? And you can see immediately the things that they have done after that in the implementation, where now they looked at the situation they had as is and they decided to, "Okay, these are the areas that are most critical for us. These are the areas that we have to make the progress, we have to make the improvement on."

For example, let's take the first one. There are different processes used, identify existing customers using different channels. So, each time you go to a different channel, if you're going through the web, through the kiosk, or going to a branch, you have a different data file, you have a different story, and you are not using the same repository.

So what they did is they worked on having a single, centralized view of the customer and the product and the account regardless of the channel that you're using. And that makes of course a big difference, and of course the service that you're getting.

I'm not going to go into the whole list here, but see the third one, for example, the fourth, they didn't have a global product catalog available. So the products were scattered around, of course, left and right. And as a result, it was difficult to find the right products for the right customer at the right time. And so they again worked on finding a lender process, a global, companywide product catalog that would be available across channels again, allowing them to pick and choose and decide what is the best match for the customers for that particular catalog.

And so the results again were really flabbergasting from -- gained 8,000 hours of loan productivity. But more importantly, I think, the important thing I would say is the reduced number of customer callbacks. And that's really critical. Because in the past they used to have a situation where you submit your application in no man's land, you don’t know where it is, until you realize at the end, it was approved or declined or delayed, and you know where. Now, you go to the website, and within your special credentials, you can go log in and see exactly where you stand, what is the status, and what's happening. And that's key in fact to better customer satisfaction.

Now I'm going to switch to another customer example, and I'm going to talk about here a regional bank. And let's focus this time on how the rules can help in this situation.

We're talking here about a regional, large regional U.S. bank, and their situation is not very different from many other big banks. By that, I mean the minute you have a bank that has been there for years and acquired many different financial institutions, you end up with a number of multiple systems. So this particular bank, what they had is in fact a lot, a lot of, in fact, a number of LOS's. And in fact, they had three big ones, three big loan origination systems.

So as a result, you can imagine the situation they're running into. They have different services depending on which LOS you go to. And they -- it was not sustainable. They had inconsistency in their credit processing, and it wasn't really integrated properly in their architecture.

So what they decided to do, and that's the interesting aspect of the thing, they decided to go, "Okay, we're not going to go into the big bank approach. We're not going to go and remove everything and replace with a super-uber new loan origination system." Because, as you know, this solution will be just lasting for a few months, if not less than that, then afterwards, the minute they acquire -- or they get acquired by another company, the whole story has to start from scratch.

So what they did is they looked at each of the LOS (inaudible) and they decided to put individuals, again, subject-matter experts who are experts in their domains, to extract the business logic within these LOS's. So they had, for example, people responsible to extract their business logic for eligibility, across the three LOS's. Other people working on risk assessment, other people working on stipulation, other people working on pricing and rating and things like that.

So when they got that information, they centralized it in their BRMS. And the beauty of our BRMS is that you can -- you are able to connect it with your LOS. So now, regardless of which LOS you're using, and it's very important to say they did not -- they did not get rid of their LOS's, they kept them, and that's the beauty. When you have a system that had been working for many, many years, interacting and having all the connectivity that you need, you can't just replace it overnight. What you need to do is extract what is the heart, what is the business logic, the area that are most critical for your business. And this is the area that you're going to connect and you're going to modernize, if you like. But everything there is, the connectivity, the planning, the stuff, the pipeline management of the LOS were kept intact. And that's the beauty of the system here. So, when they did that, they were able now to start working on it.

And if you follow me on the next chart, you will see that the way they operated. They started, as I mentioned, by revamping the decisioning once again, eligibility, scoring, pricing, etc. But they started only on conforming on Jumbo, which is their biggest part of their portfolio. But then gradually, and this is the important thing, within three months they were able to get that up and running. We're not talking here about months and years and years of working. And that's very important to understand in a BRMS system

because we have methodology that allows you immediately to reap the benefits in the system and start implementing and be in production.

And after that, they started going on to the next level. So they did home equity, they did more additional work on the deal repair, then went to another line of products, for student loans, etc. and you can see over the few quarters they had here, they had a full running system. But the beauty again of the system is that, within 45 days, they were up and running and getting their system running. And that's the beauty of, again, our BRMS.

So, now I'm going to just summarize the whole thing by giving you some examples of what does that mean for us when we talk about business agility for banking?

So when we say we improve the customer acquisition and retention, Craig mentioned that the situation we're facing today is that there's more and more regulation. What does that mean? It means that -- and at the same time, the growth is not there. I mean we're not having double-digit growth, far from that. So, what does that mean? It means that the situation today is that you have to be better, faster, more automated, and basically reducing your cost.

The best way to reduce your cost is basically to automate. But you need to automate properly. And the BRMS, combined with the BPM, allows you in fact to automate the pieces that are repetitive without jeopardizing, without putting in jeopardy or without compromising your customer satisfaction. Because you're doing -- you're automating the right things, and when you're coming to a situation when you need to have exception handling, the system will handle for you, will give you the exception handling that you need.

Another example, important aspect that I'd like to mention here, is the fact that when we are talking about like combining all these product catalog and errors, how many times you have a situation where you subscribe or you apply for a loan or -- and you don't see what's going on, you have no visibility of the system? Again, this system allows you to have, because of the rules, giving the possibility of tracking, tracing exactly what's happening on -- and why, which rule has been applied, which rule has been fired, and giving the explanation to your customers, and you don't have to do that.

On top of it, many of our customers are able to converge, in fact, the credit decisioning with the customer care, which means you don't have a situation anymore where you, after looking at your customer profile, you suggest a great product for them only to realize after they started filling up the application they don't qualify for it. So you can do the qualification and the risk assessment at the same time because you have the customer profile, and the bottom line, is you're suggesting, recommending the right products, the best fit for your -- products for your customers. And that gives of course another great satisfaction with customers.

Now, many customers ask me, "Okay, well, this is great, but what does it mean? I mean, business users are making the business rules, and what happens to IT?" Well, let me

repeat that. The IT is definitely critical and important in this equation. The IT is implementing, is putting together and in fact building the platform for the business rules management system. But when it comes to maintaining, creating, authoring the rules, 90% of the rules are written in a business language for pricing, for eligibility, for risk assessment, so therefore it's the risk manager who's going to make the changes to these rules.

Now there's a lot of tools that we have in order to monitor and have a permissioning system to know who's doing what and when and what permissioning. But we're talking about business users doing this thing. And because of that, it gives you a great edge in terms of how fast can you put together a new product, how fast can you make a new regulation into play, how fast can you be compliant with a new act that's coming, that is going to be applied, that will become a law. So that's the kind of thing that you can do. But at the same time, the IT here is building the platform, is building the infrastructure.

So it's a win-win situation for the business users, because they don't need to go to IT every single time they're making a change. And for also, for the IT, because they have now control on their structure and they know how to build a robust system without necessarily being bugged -- bothered by the business users every single time there's a need for a small change.

Now, the question that comes to mind is, okay, this is great, how do I start? So I have two options here that I would like to share with you. First one is what we call a process improvement discovery workshop. As I mentioned, although we sell and we market a set of products, we do understand that there's no such thing as one-size-fits-all. And that has happened because we've done so many of these applications, over a thousand of implementations and variety of lending situations and lending processes and lending institutions, give us really the guts to say that we can't have a super-solution, you press on a button, everything is going to happen.

As you know, every single bank, every single institution have their own, you know, their own background, their own history, their own pain points. And what we do in these 2.5 days of workshop, we sit down with your IT people and with your business, and we have a road map to build together. We show you our products, we give you experience of what we've built in the past, and at the end, the outcome of this two-day workshop is really a road map that you can take to your executives and execute upon on how to get to the point. And again, we're not talking about the uber-project that takes forever. We're talking about a very strong and proven methodology that gives you fruits within the 45 days. We have programs within 45 days, we have rules that are implemented and executed and used in production basically.

The second thing I would like to mention here on this chart is something that we are really excited about, and it comes from an acquisition that we did recently, Lombardi, that now we've converted into a full-blown IBM product. It's called IBM Blueworks Live. And what is that is typically a way to helping you implement and start using on the fly, on the cloud in fact, building, modeling your process. The beauty of this thing is that not

only -- you don't have to install anything because it's on the cloud, so you just use your browser for that. But also you can collaborate with your colleagues, your partners across the world, and on top of that, there's a bunch of predefined process on lending and other things really to processing and lending, that you can use a starter. So this is a great way of again kicking off and starting modeling your process and see where you are today and what would you like to improve.

The next thing I'd like to mention, this is very important -- for those of you who are familiar with, but those of you who are not familiar, I definitely encourage you to come to our Impact 2011. It's our user conference. Last year we had over 6,000 attendees. This year we're expecting close to 7,000 attendees. It's a great opportunity for you to mingle with your colleagues in the industry, with IBM technologists and IBM -- both from the business side and the technology side. We have a great lineup of a technology program with a lot of sessions, over 500 sessions. But also we have a very dedicated business program with a dedicated staff for banking with Forbes, who's helping us sponsoring this event as well on the business side. So, please sign up for this one. And if you happen to be more than multiple people coming to -- from the same company, you can get a special company pass for that matter.

I'd like to finish, before we get to Q&A, by giving you here, on this chart, you get a number of solution overviews, white papers that you can download, some success stories of other customers who have been very happy using the products, and some interactive learning, demos and online demonstrations that you can get and virtual briefings.

So with that, back to you, operator, for Q&A. Thank you.

David Stoddard: Okay, Joe. Thank you very much. It's a great presentation. Thank you, Craig, as well. All very timely stuff today.

So we're about to start our Q& process. And before we get there, I wanted to put our feedback form out. Before we begin the Q&A, if you could please fill out the feedback form. It has opened up on your computer. If you complete this form and press the Submit Answer button, we'll get. And that will help us very much in future webcasts to improve the webcast for the future.

Okay. So we're going to move on to our Q&A. Again, if you'd like to ask a question, just type your question to the Ask a Question text area below the media player window, and then click the Submit button, and the question will get to us.

So let's see, our first question today, Craig, looks like one for you. Can you re-summarize key elements that drove higher processing costs in the last two years? Is it fixed cost and lower volume, more manual intervention given stricter underwriting and risk assessment? What's your view, Craig?

Craig Focardi: Yeah, that's a great question. It's certainly a more nuanced analysis, and the short answer is it's a little bit of both. With respect to fixed costs and lower volume, I

think the question is saying, you know, it takes a while for me to let staff go, to reduce my office space, and so if volume is dropping, my costs are naturally going to go up because I've got some costs that are fixed over a period of months or a year.

I'd say that in the last decade, the lenders have gotten much better at hiring contract employees, and so that fixed cost issue is still there from a labor perspective. But I think there's been an increased amount of flexibility there and no great surprises on lending volume. But that is certainly part of the equation, particularly with respect to the fixed office cost that you get.

But I think the more manual intervention for underwriting, for asking for additional documentation, those requirements came in without parallel automation or simultaneous automation there. And so I would say it's a little bit more the more complex and riskier environment that's driven the higher costs than the labor costs, because those can be adjusted fairly quickly.

David Stoddard: Great. Next question, have you seen customers improving quality control on loans with business rules? Joe?

Joe Boissy: Yes. I think this -- quality control, I didn't mention it in detail, but in fact, when Craig mentioned earlier we're moving from a "don't ask, don't tell" kind of situation to a "zero tolerance, zero defects." So the question is, how do you do that, but at the same time without compromising your quality. Because you can have zero defects. But at the same time, how can you do that without spending an awful lot of time, increasing dramatically the time to close? And of course we've seen the charts saying that the time to close has been jumping up dramatically.

So, the business rules, the business rules allow you to be able to decide at any point in time who's doing what and what's been happening. So, that means that any application, any lending application or any -- that you put in the system, you have a way of monitoring and auditing every single step of the way.

So you can do two things. What customers do is two things in general. First of all, you have a justification, auditability of all your choices, so you can have top quality. So, every single time you have a decision made on a loan, on an application, you can explain, justify and showcase why this decision has been made, what has been missing or what are the decisions that have been made to doing that.

The other thing you can do is again monitor, monitor the system through the rules, so you can say for example, if my top quality is to say, I would like to get all my Type A lending applications being closed within 35 days or so, you can have triggers in your system that allow you to automatically send warnings or alarms to people who are responsible in the chain whenever there's something pending or something is plugged or something is in the log system that is preventing this from happening.

So you have all ways of controlling the system that's allowing you in your automated underwriting system as well as in your -- any stage in your system to be able to decide who's doing what, what's been happening, so you have a full auditability and full control. And because of that, you are definitely improving the quality of your loan.

David Stoddard: Great. So it sounds like they can drive down some of the costs and also meet the regulatory pressures that they're under as well.

Joe Boissy: Exactly.

David Stoddard: Yeah. Okay, next question, do you have a feel for, if special rules would be needed for loans originating outside of the US, for example, from people or companies in China, Brazil, India, South Korea and so on, do customers from emerging markets need special setups? Craig?

Craig Focardi: Yeah, another excellent question. I mean, the answer is yes and no. It's yes in that every country's consumer lending markets and real-estate-secured laws are going to be different. But they're all quite similar. And this is where the value of an enterprise-class business rules management system comes in to play. If you have a strategy to enter different country markets, you don't want to have to build a new system for each country market. You'd like to have reusable components in a similar system. And you'd like to be able to expand with a known product set. But you want a system that can quickly accommodate slightly different loan products, slightly different rules around regulatory compliance or how loans are amortized. So in that respect, no.

I mean, special rules are needed but not special or different systems. And then, it enables an organization that's expanding internationally to do so while mitigating some of the credit risks and the compliance risks that can come along with that. So I think every market needs some special set-up regardless of product, and it's the quality of the system that enables you to expand internationally but in a prudent manner.

David Stoddard: Okay, great. Here is a question about business rules. Business rules in the hands of business users, what safeguards, tools and processes can we put in place to avoid chaos and errors? Joe?

Joe Boissy: Yes, this is a great question. I have this question typically when I say, when I start saying business users can make changes to the business rules, what does that mean? Well, it's a very good question, of course. But the answer to that is really about how do you put -- about implementing -- how do you go about implementing the business rules? If you put in the hands of business those business rules and tell them, "Okay, guys, do what you like and how you want it," of course you can definitely create chaos very quickly.

The beauty of our system is that you have a very well-thought-of permissioning system. By that, allowing certain individuals that have certain credentials to do certain changes to the business rules. Which means that, depending on where you are, by definition, you

might be allowed to do certain changes or certain authoring of the rules and maybe not all of them.

So for example, if you are a junior risk manager and all you're allowed to do is make changes maybe to a particular rating between a certain -- and then when you do this change, you have to have it approved by your superior and etcetera. That kind of thing is automatically implemented to the system. At the same time, you have a whole way of auditing, who made what and when. And of course, it doesn't mean that the minute you make the change, you press the button, it's all in production. You always have a way of testing, simulating, and making sure that the changes that you just made are being well-thought-of and executed in your test portfolio before you go on to production.

So, all these safeguards, all these things are part of a methodology that we have implemented that is now part of the system. So whenever we give business users the possibility of make changes to the rules, which happens a lot, we give them at the same time a guideline, a very well-thought-of methodology on how to doing that. And the result of course is that you are gaining a lot of gain in terms of how you interact with your customers because not only -- you don't have to go to IT each and every time you make changes to the rules, and therefore gaining a lot of time, but also you have a justification and sort of an audit trail of who made what and when for the changes of the rules.

David Stoddard: Okay, good. Well, Craig, a question for you. Are underwriting models retrofitted for each asset type?

Craig Focardi: They can be, but not always. I think one of the challenges that diversified financial institutions have is that they have separate underwriting models for each asset type. And so, one of the goals of many institutions is to use the same decisioning model, the same components of a decisioning model, and retrofit the one system to accommodate different types of consumer loan products.

In practice, the -- I think the complexity around home equity loans and lines and first mortgages has dictated that those models are separate from the simpler and less data-intensive underwriting models for an auto loan, for personal line and loan, or a card. And so, I've seen increased consolidation of the underwriting models. Some institutions will retrofit one for each asset type, but it isn't always necessary or desirable.

David Stoddard: Okay, good. Joe, a question for you about BRMS systems. What synergies and overlap are there between BRMS and loan origination systems?

Joe Boissy: Yeah. This is another question that I have a lot of these questions. Typically when we talk about LOS, many people say, but the LOS already has rules in it, which is true in many cases. The main difference between our BRMS and a traditional BRMS and what you find in a typical LOS, is that we have the flexibility of having you -- you extract the business logic, again, as I mentioned earlier, from the LOS, and you are able to

modernize your whole LOS into a full-blown BRMS, which is not the case typically in a traditional LOS.

What does that mean? It means that you don't have to take your LOS and throw it in the bin. An LOS is sometimes an old system that has been really working for years, it has very much well connection, it has managed all the pipeline of your applications, of your loan applications. What you want to do here, and that's the beauty of the thing, because our BRMS is made to be connected to all legacy systems, we have all these connectors and API that allow you to connect our BRMS to any type of system, be it modern, extremely modern, of course, or legacy systems, through APIs and through various connectors. And as a result, any LOS that you have in the market today can be connected our BRMS and you give it another -- kind of you put it on steroids, if you like.

David Stoddard: Okay, great.

Well, thank you very much, Joe and Craig, for your Q&A responses, and thank you to our audience for your great questions. If there are questions that we didn't get to here, you will receive a response from us in answer to your question.

So I'd like to wrap up our webcast today. Thanks again to Joe and Craig for the webcast. Too Many High-Touch Lending Processes? How to Offer Instant Pre-Qualification, Cut Underwriting Costs By 78%, and More. Brought to you by Bank Systems & Technology and IBM.

Craig Focardi: Thank you.

David Stoddard: For more information, please click on the link before you and other links that you've seen in the presentation. And again, within the next 24 hours, you will receive a personalized follow-up email with details and a link to today's presentation on demand. Additionally, you can view today's event on demand by visiting www.netseminar.com.

On behalf of our guests, Joe Boissy and Craig Focardi, thanks for your time, and have a great day.