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Assessing the Value of Verification of Employment

OVERVIEW

Accurate, on-time verifications of employment and re-verifications of employment ensure that lenders can assess their risk and make the correct lending decision concerning borrowers' mortgage loan applications. The goal, therefore, of a VOE is to identify high-risk loan files when the borrowers become unemployed during the origination process.

The VOE ensures that the borrower was employed at the time he filed his mortgage application and a re-verification ensures he was employed within three days of the loan closing.

With the emergence of the Consumer Finance Protection Bureau and the establishment of the quality mortgage criterion, the failure to verify employment is considered a material defect that will result in buybacks, other penalties, and damage to corporate reputations.

Experienced, proven VOE providers deliver a combination of experienced staff, pro-active, well-trained customer service, and a successful track-record covering all sectors of employment, including large corporations, state and federal governments, small businesses, third-party verifiers, and self-employed borrowers. Also, VOE's provide proprietary, flexible technology, and a Rolodex of contacts at human-resource departments that's current and covers companies located throughout the U.S.

IN-HOUSE OR OUTSOURCE

Lenders that perform VOE's in-house maintain control over the process, but may open themselves up to conflict of interest charges in the future. That's especially true if the lender's staff make mistakes, which become public and look like they were approved solely to generate revenue for the bank. Over the past several years, there are well-publicized examples of conflict of interest charges leveled against banks. For instance, lenders that had their own appraisal management companies were criticized for appraisals that were done based on valuations that made the transaction work, not on the value of the property.

Some lenders complete VOE's in-house with the aim of eliminating the expense of licensing the services of a third-party and to retain control of the service. But lenders often find that their expenses are higher than budgeted because they don't have the economies of scale, technology, or the skilled customer service representatives in sufficient numbers to ensure accuracy or timeliness.

VOE's require specialized knowledge of the mortgage business; a single mistake that results in a buyback, another penalty, or a damaged reputation is often costlier than hiring a third-party to perform the work.

Given the cost of doing the work in-house with full-time employees, compared with hiring a third-party to complete the work, it's almost always less expensive to select a service provider to do the work. For instance, a medium size bank that hires 10 people to perform verifications will pay salaries of $25,000 to $40,000, depending on the expertise of the employee and the section of the country they work in. In addition, benefits such as health insurance often double the cost of employees.

Inexperienced employees will require training and may underperform while they learn the mortgage business and their jobs. Even experienced employees will need to learn to use the lender's technology, and develop contacts and relationships with human resource departments to ensure accurate, on-time, and consistent performance. To ensure the lender saves money, the in-house employees will need to complete hundreds of VOE's every month.

Moreover, a third-party assumes the risks of bringing on staff in busy times and finding work for them during market downturns, or having to lay them off, which harms office morale and can lead to negative press coverage. In the rare case where a lender performs VOE's in-house and saves money, the return on investment is too low to justify the risk of making a mistake and suffering a buyback.

CUSTOMER FINANCIAL PROTECTION BUREAU

Under Consumer Finance Protection Bureau regulations, lenders are required to comply with the ability-to-repay rule, which requires them to make a good-faith effort to determine whether borrowers can pay back their loans.

To determine if borrowers can afford their loans, lenders have to consider income, assets, debts, credit history and other factors. Also, they must be able to document that they did so during a regulatory audit. Moreover, to help ensure that borrowers can repay their loans, the CFPB created the Qualified Mortgage and permits Fannie Mae, Freddie Mac, Federal Housing Authority and other Government Service Enterprises to force a lender to buy back a loan that did not comply with QM rules. For instance, these loans must have a debt-to-income ratio of 43% or less.

The CFPB does not mandate the use of VOE's, at least directly, but it does expect compliance with its regulations.

That leaves lenders to decide on their own the importance of incorporating VOE's into their processes. Most see their importance, and the inherent risks of not performing them, and run verifications through a third-party or in-house. To be sure, in the absence of a timely, comprehensive, accurate VOE, lenders run the risk, perhaps unknowingly, that they've closed a loan with an unemployed borrower. That's a material defect under QM regulations that can subject lenders to buybacks, other penalties, and damage to their reputations.

To be sure, it's a risk that they face each day. On average, almost 1.03% of borrowers were unemployed within three days of closing their mortgage in the past year, ending in the third quarter of 2014, according to the Advanced Data-Jobless Borrower Index (AD-JBI). The index reached a high of 4% in the second quarter of 2011, and hit a three-year low of 0.53% in the fourth quarter of 2013. These statistics are based on aggregate percentages derived from individual verifications of employment during the origination process.

In light of these statistics, many lenders order a VOE at the time the loan application is filed, and pull a Re-Verification of Employment within three days of closing the loan. They do so because under CFPB regulations, a loan no longer qualifies for reps and warrants if the borrower pays for a few months as was the case in the past; instead, loans are subject to new, more rigorous rules that require 36 months of on-time payments.

However, some reps and warrants will not sunset, such as loans that were approved due to misstatements, misrepresentations, omissions, or data inaccuracies. In addition, the loan had to be originated in a manner compliant with the law, under responsible lending practices, and had to meet product eligibility requirements. A loan that closed because a VOE was inaccurate or one was never ordered, enabling an unemployed borrower to be approved when he should not have been, will face regulatory scrutiny and the borrower's file will be audited. It is likely that a buyback will likely result from this situation.

CASE STUDY

VOE: The Shift Differential Maze

Borrower
Shift employee

Employer
Stop And Shop

Lender
Top-10 Lender

CHALLENGE

Borrower worked rotating shifts and was paid more for working nights, weekends, and overtime but that was not broken down sufficiently for the lender to make a decision on the loan application. Neither the human resources department nor a corporate manager at Stop and Shop were able to provide the information.

RESULT

The specialist was able to gather the detailed income breakdown for nights, weekends, and overtime that the lender required. Moreover, the manager told the specialist that the extra income from this work would continue. The borrower was approved for the loan.

ABOUT ADVANCED DATA

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