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A Booming Business

Stewart Lender Services provides just about any service that's in demand in the mortgage industry. These days that frequently means outsources loss mitigation, asset management and REO disposition work.

BY STEVE BERGSMAN

Back in 1983, Stewart Title Guaranty Company began operations in Galveston, Texas, and just like physical movement in the humid, coastal environment along the Gulf of Mexico, growth had been long, slow and meandering.

It wasn't until 1956 that Stewart Title finally made the big leap forward, expanding beyond the state border into neighboring New Mexico. Fourteen years later, with its expansion into other businesses, the company changed its name to Stewart Information Services Corporation and in 1073 its new corporate office was erected in booming Houston. Eleven years later, the company began trading on the New York Stock Exchange.

Stewart Lender Services (SLS), the Houston-based subsidiary of Stewart Information Services, began its corporate life mimicking the parent, a long, leisurely unwinding after it was established in 1996. Then in 2007, the world changed. In quick succession, the country and, indeed, the world, faced a blow-up in the mortgage markets, the credit crisis, Wall Street meltdown, a foreclosure epidemic and a prolonged recession.

SLS, which provides centralized origination, loss-mitigation and real estate-owned (REO) asset management, had to ramp up in a hurry.

The loss-mitigation and default management pieces were cranked out at the beginning of 2008. In December 2009, the company unveiled Stewart Asset Recover, a full-service REO asset management and disposition provider. In October 2010, the company opened a new national processing center in Dallas, its third location for loss-mitigation call-center operations and refinance title and escrow processing in addition to Phoenix and Houston.

SLS also has operations in Irvine, California, and Tampa, Florida—both locations provide REO asset services, including asset management, eviction management, auction services, and REO title and escrow. In the Tampa location, with the tripling of staff, the company in 2010 signed a lease for a much larger facility.

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In 2008, the company employed at most 70 people, says Jason Nadeau, SLS' president and chief executive officer. "At the end of 2010, we had over 500 staff, if you include temporary employees," he says.

And more hires are coming—loss mitigation and REO services are the areas expanding most rapidly—especially as Dallas gets up to speed.

"The move there was really a reflection of growth," Nadeau says. "We were expanding exponentially and running out of capabilities in Houston. In 2008, we opened a small office in Dallas."

Since then, SLS created in Dallas a new call center for loss mitigation and short-sale support, put in a second originations services group and doubled its operational footprint.

"We moved from a place that had 20 to 30 employees to a location that can handle 200 people," Nadeau says.

Not only had SLS' Houston facility used all its currently leased space, but as big as the city is, there was also a limited pool of experienced mortgage servicing workers. Dallas, on the other hand, was a mortgage servicing industry locus.

"The center of the mortgage servicing world shifts between Dallas and Jacksonville [Florida]," Nadeau observes. "These cities are key hubs of talent from a mortgage standpoint. All of our competitors can be found in those cities. It was important for us to move there, because we have a large customer base in Dallas. And Dallas has a very strong talent pool, especially on the REO side, and we are growing substantially in that business."

The secrets of growth

Along with the mortgage industry imploding and housing values being in free fall, millions of Americans have lost their jobs and homes since 2007. Foreclosures have overwhelmed the lending industry, which is why companies such as SLS that can help banks and other lenders deal with defaulted loans (either by processing foreclosed properties to prepare them for resale or retaining current ownership) have been in such demand. All companies in this part of the industry have been growing, and many have been doing this longer than SLS.

It's not always the companies that are first out of the gate that succeed in the end, but the ones that can operate better and more efficiently.

Loss mitigation, default servicing and REO asset management on the service end generally are considered hands-on businesses, but the only way to handle thousands, if not millions, of busted loans quickly is by employing better technology. SLS was able to ramp up and succeed swiftly for a number of reasons—most importantly because it already boasted a deep technology infrastructure.

That wasn't by accident. Nadeau and Laurie Pyle, SLS' group executive vice president and chief information officer, are technology geeks.

Fifteen years ago, Nadeau managed the technology department of Stewart Mortgage Information before leaving to start a mortgage technologies venture in Houston called RealEC Technologies Inc. Two of RealEC's original investors were Stewart Title and Fidelity national Financial Inc., Jacksonville, Florida. In 2007, Nadeau returned to the Stewart fold and one year later took over Stewart Lender Services.

Pyle worked with Nadeau at RealEC Technologies, made a lateral employment move to the technology group at Santa Ana, California-based First American Financial Corporation, and was recruited to come to Stewart to build SLS' technology and robust loss mitigation operations. Today, Pyle divides her time between overseeing and directing SLS' technology strategy and managing its loss-mitigation and short-sale operations.

Substituting technology for experience

By 2008, it seemed all of the experienced loss-mitigation people on the planet had already been soaked up, Nadeau recalls. "There were so few of them anyhow [to begin with], because the mortgage implosion never happened before. Those who were around were already in place elsewhere before we got into the business."

SLS' solution was to break down the loss-mitigation processes into work units and rely on technology to conclude individual tasks in an assembly-line fashion.

"We reviewed the functions of very experienced loss-mitigation people and saw that 90 percent of what they performed did not require loss-mitigation experience," Nadeau says.

"Most of it was administrative and procedural in nature. As long as our technology ensured our employees did the job correctly and we had a second set of eyes on everything, we realized we didn't have to staff as many experienced individuals/"

Many skills are basic, Pyle reiterates. "For instance, inserting paper into envelopes or reviewing documents are pretty basic functions. If you are going through a set of documents to see if a borrower passed a subset of rules, one project might be to receive three pay stubs from the last three months, look at the dates and determine if they are actually from the last 90 days. It's not necessary for our employee doing that task to have a loss-mitigation background if the technology supports the function properly."

On the other hand, when it comes to underwriting or phone support, then it helps to have more experienced personnel, Pyle adds.

SLS was somewhat lucky—if that's the right word—here as well, as much of this staffing was recruited from other Stewart companies, particularly the post-closing settlement services division, which wound down as mortgage origination volume sharply declined.

Additionally, Stewart was able to find experienced loan processors and originators who were familiar with origination terms and practices and were able to apply those skills to loss-mitigation call support.

"If you think about it, 2008 was the year of decline for everybody, including Stewart," says Nadeau. "But senior management at Stewart had a vision of where business was moving, what services would be needed, and they made a commitment to build out those services and plan for the future. We were able to recruit good talent from companies—including other Stewart divisions—that were downsizing."

"We have used technology in every area as much as possible," Pyle says. "My background and [Nadeau's] is in technology, so for us it was natural to look at operations and say, 'In particular areas, technology could surely help us perform more efficiently.' Technology allows us to be very nimble."

SLS got its Dallas office up to speed quickly, Pyle says, "because we are 100 percent paperless. We can set up shop anywhere as long as we have an Internet connection."

Also, by breaking down processes into individual jobs, SLS was able to offer customized services to clientele. If a particular lender didn't want to outsource to SLS all of its loss mitigation activity that was OK because SLS was willing to do the individual tasks.

"By breaking it down into different components, which hadn't been done before, we were able to offer individual pieces to customers," says Nadeau.

In some ways, SLS is set up like a Chinese menu—you can order this and this, but not this.

"If I had a factory and everything always had to go from A to Z, I would lose customers along the way," says Pyle. "You have to be able to tailor the solution to the specific client you are working with. A lender might want to keep certain components of the loss-mitigation process in-house, but realize they have less expertise in other areas and are willing to outsource. We can be more flexible with our clients."

The ideal lineup

To get SLS more narrowly focused as a company that helps lenders with problem loans, the subsidiary had to both shrink and expand.

Older business lines were sold off, including an outsource document preparation subsidiary (Online Documents Inc.) that was acquired by Ellie Mae Inc., Pleasanton California, in 2008, and a flood-determination services group (Stewart Flood Determination Services) that was bought by Wolters Kluwer Financial Services, Minneapolis, also in 2008. In addition, an automated valuation model (AVM) business, Stewart Valuations, was wound down.

The idea is to concentrate on service-based businesses as opposed to "widget-based" businesses, Nadeau says. "We decided that all the services we will be providing would be high-touch and high-customer service."

Today, SLS' lineup breaks out into five different units. There's the original title, closing and settlement services; loss-mitigation solutions, including Home Affordable Modification Program/Home Affordable Foreclosure Alternatives (HAMP/HAFA) services, home-retention services, short-sale management and deed-in-lieu solutions; default services; REO asset management, including property inspection and preservation, eviction/redemption/cash-for-deed, valuation reconciliation, management and customized reporting; and REO title and settlement.

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The goal of the new division was to tap into markets that traditionally didn't have a lot of REO activity in the past, including smaller mortgage lenders, regional banks and credit unions.

Those smaller-sector financial institutions didn't have the core competencies to manage the volume of loans going into foreclosure over the last year and a half, says Harris, president of Stewart Asset Recovery. "We felt our competitors wouldn't be able to provide services to smaller entities and it would be a nice market to tap into."

The difference between SLS and its competitors, Harris adds, "is that our clients are giving us 20 to 50 assets a month, whereas [competitors] are doing 100 to 200 assets. Our client base is more diversified and we provide a more hands-on, single-point-of-contact business model."

One subset of Stewart's Asset Recovery Solution is Stewart REO Asset Solutions, which is run by Senior Vice President Landon Smith. His unite makes sure REO properties can be sold free and clear. In other words, if Harris' job is to market the REO assets, Smith makes sure all the legal work is done, foreclosures are properly completed and there are no further encumbrances. Smith says the "robo-signing" issues that came to the forefront last fall have not had a big impact on the work his unit is doing. "Robo-singers have had little effect upon the title position or the ability to insure title. However, the robo-signing issue and the subsequent temporary moratoriums on foreclosures has slowed the influx of new REO referrals," he says.

"Fundamentally my work is the same as regular title work, except in one regard," Smith explains. "In regular transactions, 80 percent of those properties have simple title issues to be resolved. You record the deed and pay off the last person. Twenty percent get messy with death, divorce, etc. In the REO world, 80 percent are messy and the other 20 percent are problematic."

He adds, "It's the same core business we have been doing for 100 years, but with an eye toward having your staff much more experienced in foreclosure laws. Many of these assets should have been taken care of, but during the foreclosure process incorrect actions were and [now] additional work needs to be done."

Stewart Title has been perfection and insuring residential title for more than a century; however, the percentage of transactions that are REO have significantly increased over the past few years, Smith says. "Secondly, with the dramatic increase in foreclosures over the past few years, the quality of work performed during the foreclosure action has diminished, thereby generating more issues to resolve prior to closing of the REO sale," he says.

With the first complete year as a business entity now under his belt, Harris was asked how it all went. "We are growing steadily," he answered. "We are satisfied with the numbers, doubling our REO inventory over the second half of 2010."

Growth has been impeded by various moratoriums and confusion with the different government programs dealing with foreclosures. "Although 2010 was not the explosive growth in REO we originally projected," Harris says, "we expect growth over the next five years to be extensive."

Other new ventures

Early in 2011, SLS intends to add more services centered around portfolio due diligence, and two similar programs—loan repurchase defense and mortgage insurance buy-backs. All of this is part of staying ahead of the mortgage-services industry curve.

"We got into the default space through a strategic decision slanted toward loss mitigation. The industry is about as busy as it's going to get in that space," notes Scott Gillen, SLS' senior vice president of strategic initiatives.

"We are in the REO title and asset management space on a smaller scale, but I can see us continuing to grow that side of the business. There will be a lot of expansion there over the next 36 to 60 months."

Historically, SLS has been a loan origination support company, and Gillen expects SLS to dust off the old skills and be a player again in loan quality and loan review. Those will all be important services if and when the residential mortgage-backed securities (MBS) business ret urns, and as Gillen notes, "robust loan reviews" will be needed.

This all goes hand-in-hand with loan repurchase defense, which is in essence a forensic loan review. "The skill set tied to that also ties very well with due diligence," Gillen explains. "Right now there is little [business] to go after for due diligence, as there are not a lot of loans trading hands. As a result, the initial focus is to grow our presence in the forensic loan space."

Forensic loan review is an olderskill set perfected by the company, and one that was attractive to Amie McCarthy, currently senior evaluator for whole loan mortgage evaluations in the New York office of Interactive Data Pricing and Reference Data, a unit of Bedford, Massachusetts–based Interactive Data Corporation. Before her tenure at Interactive Data, she worked at Freddie Mac, McLean, Virginia; Nomura Securities International Inc., New York; and Credit Suisse (USA) Inc., New York—and at each stop employed SLS.

"At Nomura, I hired SLS to handle the trailing documents for whole-loan purchases and mortgage-backed securities trade perfection," says McCarthy. "We employed the firm to find trailing documentation so collateral files were complete. This requires document chasing—going back to recorders, title companies and closing attorneys. Stewart had to do the forensic work on those mortgage closings, and they are efficient at what they do."

SLS also provided the value-added service of imaging the mortgage underwriting files. This enabled Nomura, contract underwriters, the trustee and loan servicers to access mortgage underwriting files in the case of putbacks, defaults or other events.

S he adds, "SLS is an industry leader in perfecting collateral files and making certain that once you acquire a group of mortgages, all of the documentation that in the end makes it tradable can be tracked down."

A bigger bang

In October, the parent company, Stewart Information Services, reported third-quarter financials that for the most part were flat compared with the year before. For the third quarter of 2010, total revenue reached $430.1 million as compared with $460 million for the third quarter of 2009. For the first nine months of 2010, total revenue hit $1.223 billion versus $1.204 billion for the same period the year before.

As for earnings, the company was in the red for both the quarter and the first nine months. Because Stewart Information Services is still heavily weighted toward title insurance, the lack of mortgage originations still hurts the bottom line—plus the company was dealing with a hurricane of title insurance claims.

For Stewart Lender Services, the results through the first three quarters were mixed.

The parent company reported: "Our lender services operations in the REI segment reported an increase in revenues of 27.8 percent for the third quarter of 2010 compared to the third quarter of 2009, but down 26.2 percent sequentially from the second quarter of 2010. Demand for loan-modification services, a product introduced in the second quarter of 2009, retreated somewhat in the third quarter relative to the second quarter of 2010 as demand for this product is dependent on the number and scale of government programs and lender projects, and can fluctuate significantly from quarter to quarter." The Real Estate Information (REI) segment includes the operations within Stewart that are non-title in nature.

Stewart Information Services executives and Nadeau have higher hopes for SLS.

"Over the last three quarters, SLS contributed 5 percent to 10 percent of corporate revenue," Nadeau explains. "However, SLS has a much higher profit margin than traditional title insurance, which always had just moderate margins and even more so today with so many title claims. Title companies have been traditionally running at 8 percent margins, but REI is closer to 30 percent profit margin."

Nadeau wants to significantly improve SLS' percentage of corporate profits.

"Our goal for the lenders services segment is to account for 20 percent of profit in the coming years," he says. "There is a very strong effort to grow our global footprint as a countercyclical business so as a publicly traded company we are not as tied to the title insurance segment of the business."

How long will it take SLS to move from 10 percent to 20 percent of corporate profits?

"We are giving ourselves the goal of doing it within the next four years," Nadeau says. "The last three years have been explosive in our growth. We could reach the goal much quicker if we see the same exponential expansion."

Or, SLS could get there even faster through acquisitions. All recent expansion has been de novo. In the years ahead, that strategy could easily change.

"We are not looking at anything specific from [the perspective of] additional services, but we are considering acquisitions in all of the spaces we are in today," Nadeau says. "There are a number of companies out there doing good work. Many of these firms are sole proprietorships, and capital is not flowing to small businesses. They could benefit from an affiliation like ours to help them grow. We have not yet made any acquisitions, but we are looking for opportunities." MB