

The Three-Day Convention in the Real Estate Settlement Services Vendor Management Industry: *Where it came from and why it mattered for the times*

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ABSTRACT

This paper examines a half century-old convention in the real estate settlement services vendor management industry: The three-day turnaround time for title searches and appraisals. The three-day turnaround time, or, the “three-day convention,” as it is variously referred to in this paper, represents the traditional service level and performance measurement for third-party suppliers of title and appraisal services. Certainly, vendor management companies (VMCs, intermittently described as VMs and vendor managers; a VM specializing in appraisal management is referred to as an AMC) facilitated fast turnaround times by dictating to vendors they worked with that orders placed today must be returned the day after tomorrow. And they closely tracked the status of these orders and called their vendors as soon as an agreed-to time frame elapsed. And yet as this paper argues VMCs were responding to the timeframe demands of the consumer finance industry they served. For it was the consumer finance industry and the competitive environment of the period that heralded what was then a new imperative at least in this part of the mortgage industry: Speed of delivery as strategic necessity. This paper seeks to explain why.

1. Introduction

Innovation and productivity drive competitiveness in every industry in which goods or services are produced, marketed, and sold. In the real estate settlement services industry, innovation and productivity are recognized in the familiar phrase *Better-Faster-Cheaper*, which the industry uses to describe the ideal, the ambition, for the collective efforts of the people and systems that comprise the industry. *Better-Faster-Cheaper*, and variations like *Quality-Service-Price* and *Good-Fast-Cheap*, may not have originated in the vendor management sector it is probably fair to suggest that few sectors of the settlement services industry have embraced the phrase with more vigor than the vendor management community.

For many *Better-Faster-Cheaper* is shorthand to describe their company’s value proposition. Moore describes a value proposition as anything that increases productivity, reduces overall

operating cost, or provides strategic advantage to the customer [8]. Porter describes it as a “set of benefits, different from those that competitors’ offer [13]. To VMCs, B-F-C encapsulates the myriad customer benefits in just using us. “Use us,” we imagine the sales executive saying to a prospect, “because our people, processes, products, and systems are all built around delivering a better, faster, and cheaper (or a lower overall-cost) buying experience than our competition.” And to a large extent that would be true; VMCs have a long history of delivering innovation and productivity to the settlement services industry.¹ As I see it B-F-C is a metaphor to describe *what VMCs do*.

In this paper, I dissect just the “Faster” component of the metaphor. Specifically, I explain the origin of the three-day turnaround time in the context of the competitive landscape of consumer finance companies (alternatively referred to as CFCs, finance companies, consumer discount companies or CDCs) circa 1963 to 1989. This timeframe is significant as it spans not only the first generation vendor management industry, but also the first generation secondary-mortgage loan industry in the United States. My central thesis is that the three-day convention made sense from a business perspective in light of the competitive mortgage environment of the times.

Some title abstractors and appraisers are likely to dispute the thesis; a few vigorously. For years service providers have complained that production and delivery of consistently high quality products and services requires more time. A three-day window is not long enough to do a credible job. Besides they’d argue, borrowers don’t need loan approval that fast. Proponents would reply that the mortgage industry calls the shots. The three-day convention has endured for over 30 years now *due to* customer demand. And without they’d argue, a showing of a string of catastrophic failures due to client- prompted turn times. To drive home the point, proponents would remind that most every form of commerce involves time pressure. Nonetheless, to critics at least the 3-day convention is just not a very good way to operate a business. To the extent that the sides cannot be swayed by the pleadings of the other, this paper may prove unsatisfying to both.²

So why is this paper important, really? It is important because there are industry analysts, like the author, who believe that every business model of every stripe ought to be reviewed periodically to see if it still makes sense. The real estate settlement services and vendor management industry should be no exception. The industry is almost a half-century removed from the original decision

¹ This includes transaction management systems (TMS) technology, electronic delivery of title and appraisal reports first over credit bureau terminals, early homegrown IT (like LSI’s “Speedcom [7]” in the mid-80s), and later via electronic onscreen images. In addition, VMs did pioneering work in the development of a standard platform for delivering appraisals (ACI, Lighthouse, etal.). And, they were the first to introduce automated rules-based appraisal and title report reviews. And, as is described herein VMCs introduced the concept of the professionally managed third-party fee panel in the settlement services sector.

² A biographical note: I am not insensitive to the objections of those put off by the three-day convention. I arrived in the VMC industry in 1984, as the assistant regional director (PA and WV) for Lender’s Service, Inc. (LSI) following a 2-year stint at Signal Finance, a regional consumer finance company that utilized both LSI and Record Data. Much of my time was spent in quality control and risk management, and for many years was a liaison between my employer and the appraisal profession (mostly). I’ve spoken to thousands of appraisers, regulators, and clients about the VMC industry business model and value proposition. I’ve written about the need for balance among the B-F-C components. And I’ve also heard from the user-side that fast and cheap is good. This paper won’t change – and doesn’t seek to change – anyone’s position. It simply lays out the business case for why early VMC clients demanded fast service.

to go with a 3-day timeframe for titles and appraisals. No one would dispute that there have been massive changes in economic, information technology, supply chain management science and any number of other factors since then. Changes in any combination or even a single of these factors might well produce different conclusions about how modern settlement services are produced, coordinated, and delivered. Wouldn't a review of where the 3-day convention came from and why it made sense for the times seem like an appropriate start? That is why this paper is important.

The remainder of the paper is divided into four sections. Section 2 provides an overview of the vendor management industry, and the consumer finance industry, and decomposes the three-day convention for titles and appraisals. Section 3 presents some of the demand- and supply-side factors that influenced the initial 3-day turnaround time determination. Section 4 explains how VMC-led innovations streamlined production, coordination, and delivery of third-party services and helped consumer finance companies compete for second-lien loans. I conclude with some closing observations and recommendations for future research in Section 5.

2. Vendor management, consumer finance, and the three-day convention decomposed

2.1 The Vendor Management Industry

Vendor management companies are independent third-party or lender-affiliated providers of real estate settlement services. They function as an outsource solution to mortgage lenders and provide all of the back-office settlement services needed to process, underwrite, close, fund, and record residential real estate mortgages. Products provided by these firms fall into the three categories: Title agency, appraisal management, and closing management. Some VMs also offer credit reporting, flood reporting, and automated valuation models (AVMs). Others limit their offerings to only appraisal/valuation management (AMCs), title abstracting, or closing management.

Services these firms provide to mortgage lender/clients include but are not limited to [18]:

- Recruiting and qualifying independent appraisers, abstractors and closing
- Negotiating and maintaining service level expectations with individual suppliers
- Handling loan-level administrative duties for lenders, such as assignment, tracking and progress updates
- Performing both pre- and post-delivery quality control assessments
- Reviewing completed reports to assess conformity to applicable guidelines
- Providing secure delivery options for completed reports
- Providing detailed management and workflow reports to track assignments

Boiled down, vendor management involves two distinct functions: contract management and workflow management. In the role of the contract manager the VMC engages the services of independent third-party providers of settlement services on behalf of a mortgage-lender client. VMCs conduct due diligence, audit work samples, negotiate fees, turnaround times, and service

level expectations. To illustrate the size of some of these companies, a large VMC, for example may have over 20 thousand suppliers of title, appraisal, and closing/escrow services.

Its other role, that of the workflow manager, the VMC monitors the order pipeline, communicates with the service provider regarding open orders, updates the client the firm's transaction management system. A large VMC may have well over a thousand orders (sometimes multiple thousands) in the pipeline at any given time.

2.2 The Consumer Finance Industry

According to a report commissioned by the National Bureau of Economic Research, Inc. [9] in the middle of the last century, the consumer finance industry dates to around 1915. For most of its history, consumer credit came in three varieties: retail installment (sales finance) contracts, small consumer discount loans, and wholesale financing of retail inventory. These loans were mostly unsecured and ranged from a few hundred to a few thousand dollars. The primary collateral for these personal loans was limited to the future income stream of the borrower, which in many cases could be garnished or assigned by the lender in case of a default. Some personal loans included collateral like cars, furnishings, and personal belongings [1]³.

The best "in a nutshell" description of consumer finance that I could find appears on Wikipedia.com.^{4,5} What makes this description so notable is that it touches on three (3) of the essential points within the thesis of this paper: 1) The restrictive credit environment that consumer finance companies operated in; 2) the buying habits and preferences of their customer base; and 3) the fact that finance companies availed themselves to more than just people with imperfect credit.

The Consumer Finance industry (meaning branch-based subprime lenders) mainly came to fruition in the middle of the twentieth century. At that time, these companies were all stand-alone companies not owned by banks and an alternative to banks. However, at that time, the companies were not focused on subprime lending. Instead, they attempted to lend to everyone who would accept their high rates of interest. There were many reasons why certain people would:

- Banks made it difficult to obtain personal credit. Banks did not have the wide variety of programs or aggressive marketing that they do today.
- Many people simply didn't like to deal with bank employees and branches, preferring the more relaxed environment of a consumer finance company.

³ Personal property collateral usually had little real value beyond providing collections personnel leverage. For the most part UCCs listing such collateral often remained in the loan file instead of being filed with the county.

⁴ The original source of the material is unclear. A Google search of the first bullet point in its totality returned three hits: The Wikipedia text above; a commercial website containing links for ads; and a website at the following URL: <http://www.aboutfinancing.ca/consumer-finance-companies.html>. Both this site and the Wikipedia site include these same bullet points. I don't know which is original material and which is a reprint.

⁵ Online open-source dictionaries aren't often referred to as authoritative resources. However, research on consumer finance is not plentiful. According to Durkin and Elliehausen (1994), this is due to the relative prominence of commercial banks and savings and loans and corresponding availability of public data, even though consumer finance companies held the second largest share of consumer installment credit following commercial banks [6].

- Consumer finance companies focused on lowering the required monthly payment for their customer's debts. Many customers [who?] would gladly refinance \$10,000.00 worth of auto loan debt at 7 percent interest in a home equity loan at 18 percent interest because the auto loan would have to be paid off in 5 years while the home equity loan would have a 20 year repayment plan, making the required monthly payments for the customer lower (even though overall, the customer would end up paying dramatically more).

Besides charging a higher interest rate to compensate for their risk, consumer finance companies are usually able to operate successfully because their employees are given more flexibility in structuring loans and in collections than banks. Consumer finance companies may also require far less contingent liabilities than banks [20].

2.3 The three-day convention decomposed

The dictionary defines a *convention* as an agreement between persons; general agreement on usages and practices; customary practice, rule, method, etc.[19] In the title and appraisal vendor management business the three-day convention represents what has become the standard turnaround time – from order to delivery – for title searches and full appraisals⁶. Table 2.1 represents the calculation of the three-day turnaround time.

Table 2.1. The Three-Day Turnaround Convention

Day 1 – Area representative receives an order from the client and places an order with the appraiser or abstractor. In the case of a full (URAR) appraisal⁷ the appraiser contacts the homeowner to set the appointment (for the following day, optimally). Appraiser and/or abstractor starts to work.

Day 2 – Appraiser completes physical inspection, drives by and photographs comparable sales; abstractor researches courthouse records, chain of title, taxes, liens, etc.

Day 3 – Abstractor and/or appraiser delivers the preliminary report⁸ with a hard copy to follow.

⁶ Other products like Property and Judgment reports (P&J), current owner property reports, among others, typically had 24-hour turnaround times. Most of the VMCs took the 24-hour turnaround to mean that if a P&J is ordered sometime today it is due by the end business the following day. Others took it quite literally to mean 24 hours.

⁷ Drive-by and review appraisals typically had 2-3 day turnaround times.

⁸ A preliminary report, (or “prelim,” was a phoned-in abbreviated report highlighting information the lender needed to make a loan decision. A form was used to gather information like the order number, property address, lot and block, brief legal description, taxes and liens, chain of title (title search), neighborhood (urban, suburban, rural), number of stories, gross living area, value of land and improvements, real estate taxes, comparable addresses, gross/net adjustments, largest line item adjustment(s), adjusted values, and the estimated market value of the subject property (appraisal), etc. As technology progressed prelims were delivered by facsimile machine or credit bureau terminal. A hard copy followed in the mail or was delivered to the branch by the appraiser or abstractor.

To further complicate matters, some clients counted the weekend and others counted just Saturday as working days. When this happened it was usually a client that was open on weekends or Saturdays. So as simple as the calculation appears on paper, it proved to be a sticky subject in practice for both suppliers and (some) clients; for different reasons. Suppliers wondered why they were always under the gun, whereas clients wondered why their suppliers didn't have to work weekends like they did.⁹

2.4 Customer delays and supplier delays explained

As with most guidelines, the 3-day convention included a few allowances for delays depending upon circumstances on the ground and the other parties to the transaction. The first of these delays was known as a customer delay. A customer delay occurred when the borrower couldn't be reached by phone, was out of town, unable to leave work, or was otherwise unavailable to meet the appraiser. When this happened, the time clock temporarily stopped, as long as the AMC/VMC was promptly alerted. On the title side, an order could be customer delayed and the time clock temporarily stopped due to a problem with an address, list of liens versus common named borrowers (Smith), unexpected courthouse closing, etc.

Another form of delay occurred if the appraiser encountered a unique property and required more time to perform the appraisal. Such a property may have made comparables hard to come by, research and analysis more in-depth, or both.

A third form of delay was known as supplier delay. Unlike customer delays, however, there was no temporary stop of the time clock; it kept on ticking. Most VMCs though, built tolerances of between 5% and 10% into their delivery measurements to account for some level of supplier delays. These same tolerances were incorporated in client service level agreements.¹⁰

Thus the criteria used by the VMC industry (with some variations - like counting Saturday as a workday for example) to measure how often a supplier has met the 3-day convention becomes evident. In measuring supplier turnaround time performance: *At least 90% (or 95% say) of appraisals and title searches not delayed by the customer must be returned within 3 days.*

3. Demand- and supply-side factors influencing the need for speed

Throughout the 1950s, 60s and 70s, the mortgage lending industry was dominated by the savings (or building) and loans. Borrowers with a good credit history, sufficient down payment, and a steady income source had little few problems borrowing money to buy a home from any number of S&Ls located in and around their community. Not only did S&Ls extend purchase-money

⁹ Of course, we all did; they just didn't realize it. Nor did the honchos at the VMCs seem to care much about the overtime abstractors, appraisers, and yes, middle-managers invested to get product out the door.

¹⁰ At the risk of being redundant it is important to recall that as strictly as VMCs held their vendors to the agreed-to deadlines, clients held VMCs to these very same deadlines. It was one of the primary means lenders used to measure a VMCs performance compared to other VMC competitors.

funds, they extended these same homeowners home improvement loans. Refinancing, though available, didn't shift into high gear until the latter part of the 20th century.

In the 1980s, after the S&L crisis befell that industry banks solidified their position as the mortgage lender of choice. By the mid-1980s many savings institutions had been stung by numerous bad bets on real estate, prompting FIRREA (the Financial Institutions Reform, Recovery, and Enforcement Act of 1989) and the demise of S&L dominance in the mortgage market.

The 1990s ushered in the rapid ascent of subprime lending in the commercial banking industry, killing off much of the market sector previously served by the consumer finance companies. At that point, regional and even national CDCs began to consolidate into banks or larger CDCs for survival. Perhaps the largest and best know of these consolidations occurred in 2000, when Citigroup purchased The Associates. Even before that, banks were well on the way to becoming the kings of the subprime market. But in earlier times, small, privately owned, single-state and regional consumer finance companies ruled the market for small balance loans.

Finance companies are widely viewed as providers of high-cost loans to people with bad credit. And while this characterization has merit it doesn't recognize that many bank-worthy customers often availed themselves of CDCs services, as mentioned, for the speed and personal service they provided. Service was the primary means for finance companies to compete, although most attention is paid to the interest rates they charge customers, which contributed to the prevalence of usury laws to try to protect consumers from being charged exorbitant interest rates.

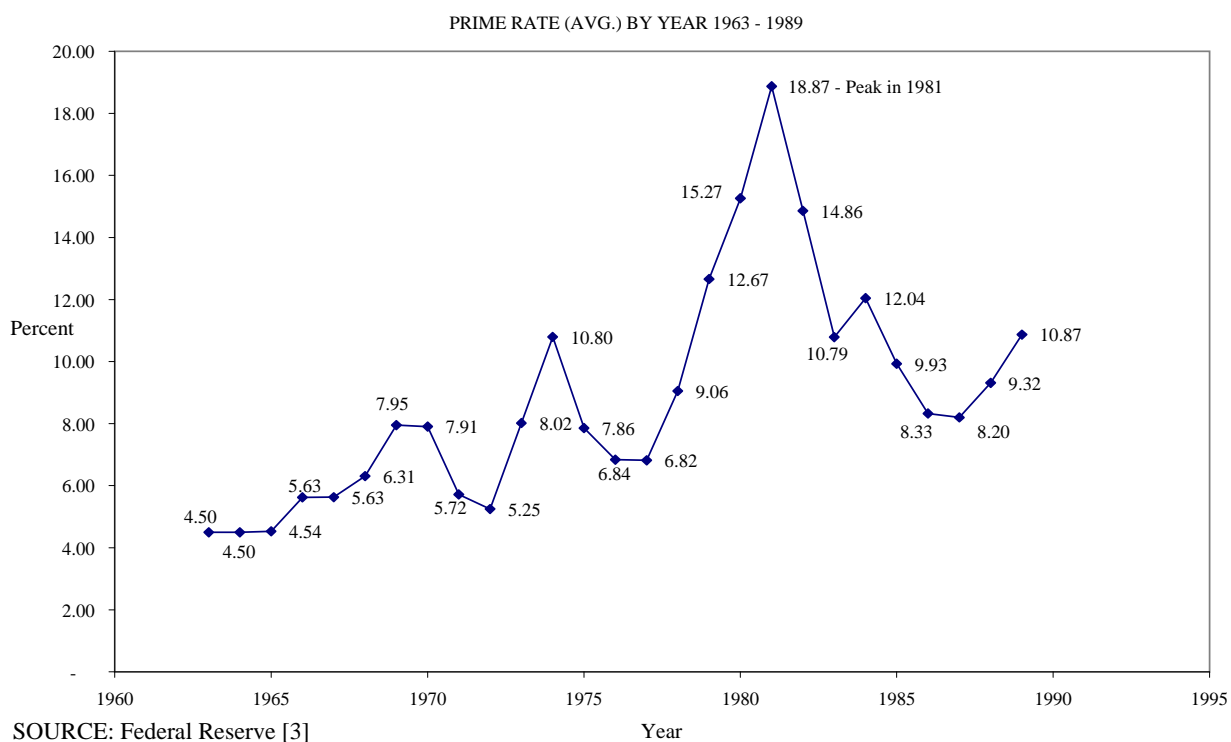
3.1 Usury laws restricted the supply of credit to borrowers with credit problems

The term *usury* refers to the practice of lending money at an excessively high rate, or unlawful, rate of interest. According to research by Boyes, enacting usury laws was all the rage in the late 1970s and early 1980s [4]. By 1978, Boyes calculated, fully forty-eight states and the District of Columbia had statutory limits on the maximum interest rates that could be assessed. Consumer finance companies had to be aware of usury ceilings and the public outrage toward those who overcharge their customers. As well meaning as these limits seemed at the time, several studies found that usury limits had the unintended effect of restricting credit. The groups most harmed by these laws, according to Boyes, were low-income individuals, borrowers with credit problems, and first-time homebuyers. This occurred, he argued, because financial institutions were unable to cover their risk premiums by increasing interest rates. As a result, they reduced risk premiums by refusing to make loans to higher risk individuals.¹¹ By the early 1980s, on the strength of these studies, states began to repeal usury laws (usually with sunset clauses to reinstitute or revisit repealed acts in 3-5 years "just in case") [4].

¹¹ Commercial banks and S&Ls charged a common rate which covered the average risk premium associated with loans in each risk category, Boyes explained. The cost involved (legal and transaction) to charge individual borrowers' interest rates commensurate with risk individually surpassed the benefit of doing so. In contrast, these lenders realized actual benefit by reducing the quantity of higher risk loans; the benefit being lower average risk premiums.

The easing of usury laws corresponded with the significant rise in interest rates in the early 1980s. The nearby chart, Chart 3.1, depicts the prime rate during the span of years covered in this paper (1963-1989). Under the most favorable interest rate environment consumer finance company customers expected to pay relatively high interest rates. However, from 1979 – 1982 and again in 1984, were particularly rough on credit challenged borrowers; the prime rate peaked in 1981 at just under 19 percent.

Chart 3.1: Prime rate (yearly average) 1963-1989



3.2 Balancing risks and rewards in the consumer finance sector

Loan losses, Benston [2] explained, are a function of a) loan level risk; b) expenses incurred to reduce loan losses; and c) favorability of laws regarding interest rates, closing costs, insurance add-ons, collection tactics, and bankruptcy protections. CDC operators were keenly aware of the risks that accompanied lending to borrowers with credit problems. Benston's research, later challenged by Shay¹² [16] due to lack of data quantity and quality at the time, suggested that in 1970, "losses net of recoveries as a percentage of outstanding loans averaged \$1.80 for consumer

¹² Benston himself recognized and discussed in detail the same data deficiencies in his report [2]. Shay didn't challenge Benston's effort at rendering a statistically significant result, just that the underlying data wasn't very good. Nor would it be expected to be: most CFCs at the time were privately held, and states were inconsistent and lax in their reporting requirements. Data reporting didn't improve significantly until the late 1990s and the consolidation of these privately held organizations into larger publically held banks.

finance companies, \$0.63 for commercial banks...” At the same time, he concluded, “branch office operating expenses... at finance companies is estimated to be \$38 compared to \$24 at commercial banks.” These additional costs were recouped through higher points, rates, and fees. Thus they incurred higher losses and expenses on the one hand, but earned more on the other side. They further reduced expenses and risk by outsourcing vendor and order management to third-party vendor managers.

3.3 States begin to pass secondary mortgage laws

In 1963, Ohio and a small handful of states enacted secondary mortgage laws. At the time most states had Homestead Acts that specifically prohibited second mortgages. However, the growing realization that home equity could be leveraged as a funding source for consumer goods led states to reconsider such prohibitions. The transition was a slow one. Pennsylvania, for instance, didn't pass its secondary mortgage loan act until 1980, two years *after* the passage of the National Second-Mortgage Act of 1978. Texas held out until as recently as 1999 before permitting second deeds of trust. The consumer finance industry as a second-mortgage funding source had arrived.

The newfound authority to make second mortgages wasn't without hurdles. Consumer finance office managers quickly encountered at least three (3) systematic factors to necessitate the need for speed in securing settlement services: buying habits of consumers, limited product offerings and terms by title companies, and branch personnel who were compensated on loan production instead of loan performance. Readers are likely to recognize all three of these factors throughout this paper.

3.4 Demand-Side Factors: Consumer buying habits, competition, and fees

Getting the borrower off the street. Branch managers and their bosses were well aware of the need to get the borrower off the street. A typical refrain in the consumer finance industry, it quite literally meant that the CDC needed to wrap the customer up quickly or else lose them. Some branch managers promised borrowers a loan decision by the close-of-business the next day. Some approved the loan on the spot and only then took the application and ordered products. Some scrambled to pull a credit bureau report while the customer waited at the counter for an approval. Titles and appraisals ordered on a rush (or super-rush) basis became the norm. Speed to close (and then wait out the rescission period to issue checks) was normal way of life. Get the borrower off the street!

Consumer choice. Customers for their part tended to shop around, going from lender to lender in pursuit of the next debt consolidation loan. And why not? CDCs occupied space in most every strip mall so distribution points were rarely a hurdle. Most finance offices offered flexible hours for customer convenience. And they closed loans in borrowers' homes, workplaces, and sometimes rest stops alongside interstate highways when they had to. As noted, customers appreciated the convenient and relaxed atmosphere offered by the consumer finance branch office. CDCs did what they could to accommodate their clients.

Loyalty only went so far. Beyond the good will garnered by branch personnel there wasn't much to differentiate one finance company brand from the rest. Borrowers often figured that their chance to flip from one to the next bill consolidation loan might be a little better by applying with a new lender rather than go back to the current mortgagee. Current mortgagees often required borrowers to make at least 6 or so payments before rewriting a loan. Besides, the borrower could always return to the first lender the next time around. Customer loyalty was fleeting.

Competitive gamesmanship. The tendency among CDC customers to bounce around from one to another lending company, and sometimes to make application with multiple lenders simultaneously, often pitted loan officers against one another in a race to see who could convert an application to a loan approval fastest. As mentioned, one way to speed the approval was to base the approval on a credit bureau report with the customer in the office (and perhaps in-file appraisal/title evidence for current or recent-past customers). Competition was fierce as was the need for speed of product delivery.

A preponderance of charges. Upfront fees that finance companies charged also lent urgency to getting the secondary mortgage applicant off the street.¹³ And there were lots of fees that could be, and often were, charged. Depending on the state, CDCs were permitted to charge combinations of the following fees [12]:

- Title examination, title abstract, title insurance, credit report, survey, appraisal, notary, attorney, postage/messenger/express carrier, tax service, etc.
- Discount points (say 1-5 percent of the amount financed)
- Optional credit life, credit accident and health and credit unemployment insurance. Insurance coverage fees, and the numerous other fees, routinely ranged from several hundred to several thousand dollars.
- Application fee (PA law allowed a charge of up to 3% of the original principal amount of the loan. The fee was fully earned at the time the loan is made and could be added to the principal amount of the loan).

It is not surprising that among the first lessons learned by trainees and loan managers was to get from application to funding at lightning speed. Otherwise, buyer's remorse or a better deal elsewhere could cause a borrower to walk. Swift turnaround of products was essential.

The need to "get the borrower off the street"—fast—and the borrowers' desire to consolidate bills using second-mortgage financing made the "Faster" concept more of a strategic necessity. In other words, converting an application into a loan – and by necessity the products and services needed to underwrite, close and fund it – was the price of entry into the second-mortgage space; failure to do so was not much of an option.

¹³ The preponderance of upfront charges – on top of the high interest rates – generated scores of lawsuits. For example, a lawsuit filed regarding a 1996 loan in which the borrower was granted a \$15,500 mortgage loan and was assessed \$3,050 in points, fees, and settlement charges [10].

3.5 Supply- Side Factors: The traditional title agency business model resisted fast (and cheap) current-owner searches

This sub-section describes a hurdle not typically encountered in the banking and savings association arenas. To the consumer finance industry however it was a deal-breaker: The length of time it took to turn around title searches and the limited product selection offered by the title companies of the day. In a wide-ranging interview, Bruce Felder, Founder and CEO of Record Data Incorporated [15], explained that in the early days of his enterprise¹⁴ friends in the consumer finance industries would lament long delays in obtaining current owner searches and low-profit searches. “Title companies,” Felder said, “were expensive, charged an arm and a leg for searches, and treated consumer finance companies like second-rate citizens of the banking industry.”

Felder cited both economic and philosophical reasons for steering clear of this segment of the industry. The economics, Felder reminded, favored full title searches over the current-owner searches that were popular among consumer finance companies. “Given the choice between doing title work on an \$80,000 mortgage loan from a savings and loan customer and a \$5,000 loan from a consumer finance customer,” Felder said, “it made sense for title agents to put the less profitable work on the bottom of the pile; often for weeks on end. By the time the title company got around to processing the property report or title search, the customer was long gone [15].”

Another VMC veteran, Joe Casa, Founder and publisher of trade newsletters including The Title Report, The Legal Description, and Valuation Review, observed that title agencies didn’t view the consumer finance industry on the same level as banks and S&Ls. “In the early days, consumer finance companies were considered by title insurers to be loan sharks that happened to become regulated. They wore the black hats [14].”

Another industry leader observed that the VMC industry grew out of a need in the consumer finance industry. This person described the friction between the title agencies of the early days of the consumer finance industry this way:

The need from the perspective of the consumer finance company was that it could not get responsive service from title insurance companies. First, many title companies viewed consumer discount companies as second-class citizens; consumer finance was seen as a dirty business. Title insurers also were risk averse. They viewed CDCs as risky business although title claim loss ratios by CDC borrowers were very low. There was a perception of risk. Another issue was that title insurance came in one flavor: full sixty-year searches and turnaround times of 3-4 weeks. And CDCs dealt in small loan amounts. A small loan equals a small title premium to the underwriter. So they gave them poor service.

To the extent that the CDC model relied upon fast turnaround times for titles and appraisals the prevalence of slow service by title agents (3-4 weeks), bad feelings – Loan sharks? Second-class

¹⁴ Felder founded Legal Messenger Service, predecessor of Record Data Inc., in 1959, while he was still in college. Additional insights into Felder’s, and other VMC pioneers’, see [15].

citizens? – combined with low dollar premium income and perceived risks associated with working for this segment of the industry, consumer finance companies were forced to find alternative suppliers for their title and appraisal needs. They didn't have to look far to find a familiar source: Vendor management.

4. How VMC-led innovations streamlined production, coordination, and delivery of third-party services and helped consumer finance companies compete for second-lien loans

As previously discussed loan losses are a function of the loan level risk, risk mitigation expenses, and the favorability of lending and collection laws [2]. Among productivity generation and cost control strategies CDCs deployed was the use of third-party VMCs. Already established as reliable providers of property reports and valuation products, VMCs proved to be equally adept at facilitating full title insurance policies, flood reports, and related settlement services. First-generation VMCs Record Data Incorporated (RDI) and Lender's Service, Inc. (LSI) became the go-to sources for fast (cheap and good) appraisal and title solutions.¹⁵

4.1 The VMC business model was built around the needs of the consumer finance industry

Without question VMCs were more than happy (and well positioned) to push for faster turnaround times and lower appraisal and title fee concessions from their suppliers. Their rationale, frankly, was that their finance company clients made clear a need faster service and lower cost. They also didn't want to manage and third-party fee panels; better to hire someone else to do it. Both of the original VMCs started out providing one-county current owner property reports. And most of the senior executives who built the original VMCs came to the industry from consumer finance. At LSI, for instance, the CEO, senior vice president, numerous vice-presidents, and at least one manager (me) came to the firm via Signal Finance Corporation. Their experience at Signal, and other finance companies, taught at least three valuable lessons that were incorporated into the VMC model.

The first of these lessons was that, at the corporate level at least, consumer finance executives did not want branch managers to maintain control over abstractors and appraisers. The second lesson was that CDC executives, at the home office and branch levels, wanted uniform product delivery standards that they could depend on, and measure the VMCs service level against. And the third lesson was that CDC managers (and their bosses) wanted a single contact person to beat on

¹⁵ Most of the second- and subsequent-generation VMCs were founded by former executives of the first-generation VMCs, LSI and Record Data. One salesman wryly observed that a former employer had so many vice-presidents that he almost didn't want to be one. The industry produced a vast pool of talented executives who felt they could compete on the strength of a single large client or a few smaller ones, a strong operations platform, and a sales force to build and replenish the client base. Later on companies added advanced information technology systems, client-relations teams, comprehensive service level agreements (SLAs), and better understandings and experience working with mortgage lenders in the prime markets to their tool chest. These and other competitive strategies meshed well with a rapidly consolidating mortgage lending industry pursuing scale economies, lower operating costs, nationwide coverage, and centralized loan facilities.

(verbally of course) when an order turned up either missing or late, or didn't measure up to the client's expectations. With these lessons in mind, VMCs built their business models accordingly.

The VMC business model proved to be equally responsive to the evolving mortgage and settlement services landscape as it was to the personal loan market. As Joe Casa told me in an interview, VMCs began offering title insurance around 1973 or 1974. "Up until then they just did the property report (current-owner searches included mortgages, tax liens, ownership), he said. "And they provided an Errors and Omissions (insurance) policy along with the searches for consumer finance companies [14]." This adaptability to the needs of the day permeates not only the content of this paper but speaks volumes about the impact that VMCs had on the evolution of the industries they served; and on the evolution of the more traditional settlement service business model.

The traditional settlement service business model of the 1960s and 70s proved ill-fit for the needs of the consumer finance industry. An article in *The Title Report*, entitled "What's TAVMA? For a special group of agents, it's a new line of defense in a rapidly evolving industry," pointed to the passage of the national second-mortgage act as a turning point (I have argued that VMCs created numerous turning points by innovating on traditional settlement service products and services).

When the national second-mortgage act was passed in 1978," the article stated, "few traditional title agents wanted to take on the job of supplying finance companies (largely sub-prime) with short title searches and ALTA products in the fast time frames required by that particular industry segment [17].

4.2 VMCs as go-to sources for current owner searches around the country

After World War II, banks and other mortgage lenders began to require title insurance to protect their interest in a mortgaged property against flaws or defects in the chain of title. Title agents were tasked to search the public record as far back as 60 years from the date of the search to verify that there were no clouds in the chain. When problems surfaced the title agent conducted further due diligence and documented the search file accordingly. The title agent either issued a title policy excluding the discovered defect from coverage under the title policy, or otherwise, worked with the lender to remove the defect and thus the exception from the policy. All of this took time and added another layer of costs that the borrower would have to pay at closing. And many times title insurance wasn't required, making it unnecessary to obtain a full title search. As a result, consumer finance companies often ordered current-owner searches in lieu of full title searches, which VMCs returned the same or the next day.

Consumer finance companies made what are variously referred to by industry insiders as *character loans*. These are loans extended to people employed in stable jobs, could verify their incomes, maybe had spot on their credit records, but weren't overextended with debt obligations. They may or may not have had much equity in their property. Many times the loan wouldn't be made using the property as collateral, so there'd be no need to obtain anything more than a current owner search. The search provided evidence that the borrower owned the property, reported any outstanding liens, mortgages, tax liens, etc., all of which the branch manager used to gain a loan

approval from their supervisor.

As mentioned, title insurers of the day often didn't want to do this type of business. Full searches and title issuances were more profitable and higher margin products than were current owner searches. However, for VMCs there was a lot of volume potential in these searches. Therefore, as a customer service and as a profit center VMs built their title businesses on this piece of work.

4.3 The contribution of the first-generation VMCs

The mortgage lending industry has evolved from where it was in the early years of the VMC industry. Certainly, credit is far more available today to people with credit problems, at least it was before the 2008 financial meltdown. However, credit was not so available to such borrowers in the 1960s, 70s, and 80s. Vendor management served as a means to overcome or to lessen some of the barriers to entry into the mortgage credit market. As this paper documents they did so through innovation, information technology, flexibility, and a keen sense of what their customers needed and then executing on these needs.

An old friend from those early days once observed that at bottom "VMCs facilitated the democratization of the credit process. Twenty years ago, people didn't have easy access to credit markets. VMCs created this access," he said.

5. Conclusion

The three-day turnaround time was not grounded in science, statistics, appraisal or title theory. There were no industry conferences or planning sessions to hammer out detailed analyses to quantify the need and confirm the demand. There were no Lotus 1-2-3 spreadsheets (Excel wasn't around then) to model the timelines, handoffs, and milestones comprising the production process. Rather, the origin of the three-day appraisal and title search turnaround time was business-need driven, pure and simple. It was a response to the needs of a particular client group, in light of the competitive forces that the client group faced in that day. And it exists in the same form more or less to the present day.

Consider. The 2007 October Research Corporation National Appraisal Survey [11] found that sixty-nine percent (69%) of appraisers reported that full appraisals take 2-5 days (Q3). Also, 43% of the survey respondents said clients expect a turnaround time of 1-3 days for full appraisals; another 34% said 4-5 days (Q4). In addition, 79% said they meet client expectations for full appraisals between 76% and 100% of the time (Q5). Significantly, the ORC survey was conducted at a time when AMCs made up only 17% of the respondent's book of business (Question 1 in [11]); not nearly enough to conclude that the percentages above are skewed to the low-side by AMC turn times and on-time expectations. A survey of title abstractors is likely to render a similar response based on feedback from the title abstractor and examiner community.

What all this seems to point to is, that although AMCs, and full-service VMCs may be at the front-edge of the product delivery timeframe they aren't much different than what other client groups demand of their suppliers.

5.1 Future Research

My hope for this brief look back at the origin and business case for the three-day convention is that it may be used as a beginning point for future assessments of the three-day convention and whether it still makes sense. Some specific areas of inquiry might include:

- Is the three-day turnaround time a strategic advantage or strategic necessity? Clemons and Hitt [5] define strategic necessities as activities that must be taken to preserve parity with competitors. They aren't so unique or set such a high bar that competitors cannot replicate them. They are offered because competitors offer them. In the vendor management industry, if a competitor offers something of value (real or perceived), it won't be long before they all offer it. Which brings us back to the question: Is the three-day turnaround time a strategic advantage or a strategic necessity (both at the firm and industry level) in the second decade of the 21st century?
- Do three-day turnaround times damage the structure, safety and soundness of the mortgage finance system? VMCs have been criticized for their "restrictive" turnaround time demands that critics say force abstractors and appraisers to shirk, that is, to cut corners in order to deliver the product on time. But is this so? VMCs aren't the only clients that demand quick turnaround times. And they build in allowance for certain delays (property, comparable, access, and others on the appraisal side; name, deed, tax and municipal liens, and unrecorded satisfactions, and others on the title side). Given all these factors is the three-day turnaround time inherently bad for the system? Empirical evidence is critical to answering this question, whether it is 'Yes' or 'No.'

In the end, it is up to the mortgage lending industry to determine whether and to what extent the 3-day convention remains a necessary part of the real estate settlement services ecosystem. While banking regulators, abstractors, and appraisers can and should weigh in, and offer guidance and subject-matter expertise, the need for speed in title and appraisal acquisition vendor management is and will continue to be driven by the corporate buyers of our collective services; as is the case in virtually every vendor/client relationship.

And that is as it should be.

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