Fair, Honest *and*

BY CHARLES WISNIOWSKI

Even in a highly cynical age where "integrity" may seem to some a quaint concept, Inlanta Mortgage President and Founder John Knowlton speaks with understated Midwestern pride about his industry and more directly about his mortgage company, Inlanta Mortgage, Waukesha, Wisconsin. ■ From the time he founded Inlanta (formerly First Choice Mortgage) in September 1993, Knowlton says he has sought to walk a straight and narrow path—at times defying conventional wisdom—even as other "gouge and run" contemporaries did anything and everything to close the deal and make the quick buck. ■ Inlanta Mortgage has a simple business philosophy. As stated on its website it comes down to this: "To provide the best service to our customers and partners, with the highest level of honesty and ethics." ■ Fully aware that the open declaration of the company's Midwestern, conservative values may be viewed by others as being a bit "Pollyanna," Knowlton says Inlanta Mortgage long ago crunched the numbers, ran the models and then coldly calculated that it is simply not a good business model to stiff the customer. ■ "I've had a lot of loan officers that have been with me for 12 or 14 years. The long-term relationships that they've built with their clients and with their business partners are the total key to succeeding in this business," says Knowlton. ■ "We always say that if you don't treat a customer fairly and right, nine out of 10 times they'll say nothing to you about that. But they'll never use you again and they'll bad-mouth you to everybody else that's out there, and you won't have a business. We've seen that happen to many people in this business."

This Midwestern mortgage lender was built on a foundation of honesty, ethics and superior customer service. An early switch to FHA lending powered a growth phase for Inlanta Mortgage, while others were failing.

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Accountable

(Left to right) Joe Ramis, branch recruitment director; John Knowlton, president and founder; and Jean Badciong, chief operating officer of Inlanta Mortgage

Knowlton says many of those "gouge and run" players have been driven from the business precisely because of their slash-and-burn, short-term thinking—much to the benefit of competitors and borrowers alike.

Attention to customer service and building long-lasting relationships in an honest and ethical manner has served as the company's prime directive from the start. Yet, Knowlton says it has been Inlanta's focus on the long-term and specifically some key decisions made contrary to popular opinion that account for Inlanta Mortgage's longevity and prosperity before, during and following the mortgage market meltdown.

Three key decisions stand out—Inlanta's development and adherence to strict hiring standards; its adaptation of a "partnership" branch model from the ashes of the unpopular "net branch" concept; and the company's decision to pivot away from subprime lending in favor of conventional and Federal Housing Administration (FHA) loans ahead of the meltdown. (An essential development in the latter decision was obtaining Direct Endorsement [DE] authority from the Department of Housing and Urban Development [HUD]).

Modest beginnings

In September 1993, Knowlton was 42 years old. Having worked as a vice president for 17 years in charge of more than 40 branch offices in Wisconsin and Iowa for Minneapolis-based ITT Financial Services, based in its Milwaukee office, Knowlton said it occurred to him that if he were ever going to go into business for himself, it was either now or never.

When he opened the mortgage brokerage First Choice Mortgage with three offices in Des Moines, Madison and Waukesha, Wisconsin, it was a less-than-friendly economic environment to enter the mortgage business. The Clinton administration struggled during its freshman year to get a handle on the same recession that had driven the president's predecessor—the first President Bush—from the White House.

"I had people tell me after I started the business, 'Why are you starting now? We just came through a refinance boom, and it's really slow.' To be honest, I guess I didn't know any better. It worked out to be a great time for us," explains Knowlton.

For its first few years, First Choice operated simply as a mortgage brokerage—until about 1998, when the company opened up its own funding operation. But it was during the 2000s that the company evolved into the Inlanta Mortgage of today through modest, measured expansion and a couple of critical business decisions.

Today, Inlanta Mortgage has about 140 employees operating in 10 states—Wisconsin, Illinois, Iowa, Florida, Michigan, Minnesota, Indiana, Missouri, Kansas and North Dakota, with licenses pending in Kentucky and Arizona, according to Jean Badciong, Inlanta's chief operating officer.

"We're a referral-based company, and we work off of those relationships. The relationships we have with our branches are as important as the relationship with the customer," explains Badciong. "As we are looking to expand our national presence, we're always looking to expand branch-wise and employee-wise. The biggest focus we've always had as a company, though, is that we're not adding bodies to grow the size of staff. We're a little more selective with the originators that we hire."

It is selectivity in staffing—seeking candidates with a proven track record of ethical dealings, mortgage market knowledge and profit-generating ability—that is the linchpin for Inlanta's success to date, says Knowlton.

"Making our people the most honest, ethical mortgage professionals that we can, and creating long-term relationships with their clients and business partners—that's one of the biggest things we push here," says Knowlton.

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"This business, I used to say, is not rocket science. But I will tell you that it's getting closer and closer all the time, because there is just more and more responsibility for us and our loan officers to ensure we are giving our customer value while we are an asset to them in the loan process," he says.

Human capital

Few would ever mistake Inlanta Mortgage for the U.S. Marine Corps, but the mortgage company, not unlike the elite military branch of service, is always looking for a few good men and women to add to its ranks . . . but it won't take just anybody.

By the time prospective candidates have completed Inlanta's intensive interview and background process, they just may feel like they have completed eight weeks at Parris Island—the legendary South Carolina proving ground where raw recruits (those who haven't washed out) emerge as Marines.

According to Joe Ramis, Inlanta's branch recruitment director, the company hires only one out of 10 applicants, with the majority of those being referrals by existing employees or other industry contacts.

The vetting of a candidate can last for as long as 60 days as the would-be employee is queried about his or her business practices, ethics, competency and ability to produce through personal interviews, reference checks and careful scrutiny of the candidate's professional record—such as complaints filed with the Better Business Bureau and a review of his or her Google™ and Facebook footprints.

"The first thing we're looking for is an honest, ethical mortgage professional. We want good people that do things right," says Ramis. "But we also have to have production. You are looking for people that are running profitable offices. If it's a one- or two-man shop, running $1 million a month in volume, that's pretty good. If it's someone with five to eight loan officers, you have to be looking at $4 [million] to $5 million per month."

In a play on the adage made famous by President Ronald

Reagan, the company needs to verify but trust its would-be employees, because the wrong selection could prove costly in ways a lot more expensive than just lost profits, says Badciong.

"We can't have the trust that we have in our loan originators without knowing that they come from that foundation, and will follow policies and procedures," she says.

Of all of Inlanta's critical hiring decisions, Knowlton credits the addition of Badciong in November 2005 as "a stroke of good fortune" for the company.

Badciong has been in the mortgage business since 1990, beginning her career doing quality control at a state bank. Knowlton credits Badciong's experience with hands-on, human-touch quality control for the fact his company didn't get all caught up in the go-go, non-traditional lending business.

"In 2005, after I had Jean working on some quality-control issues here, I had her take a look at our funding side because I had some concerns about that. In about six or eight months, we decided to get out of subprime," explains Knowlton. "It was a great idea. It didn't seem like it for a while, but it was. We moved in the other direction, toward doing more conventional mortgages and FHA."

Flying high as a 'full eagle'

According to FHA data, the government–insured program's share of all home financing dropped from 14.1 percent to 3.8 percent from 1999 to 2006. Knowlton says Inlanta's relatively early embrace of FHA at the tail end of FHA's "lean years" prompted the company to strive to be more knowledgeable and experienced with the program as more and more subprime refugees flocked to FHA.

Inlanta's FHA volume has made a quantum leap over the last five years. In 2005, about 3 percent of the company's origination volume was FHA. In contrast, Inlanta's FHA volume in 2009 was nearly 50 percent of its production. Through April 30 year-to-date, 45 percent of Inlanta's volume was FHA, with about 7 percent of production from the U.S. Department of Agriculture (USDA) Rural Development program, 2 percent of production being Department of Veterans Affairs (VA) loans, with the balance made up of conventional conforming loans, says Badciong.

"So, going from 3 percent in 2005 up to 50 percent in 2009, that was a pretty big jump and it took a lot of education between those years to teach our loan officers everything they needed to know about the program," says Badciong.

Inlanta's investment in FHA training and education paid off when HUD awarded the company "full-eagle" status with Direct Endorsement authority.

"It was one of our best moves that we ever made as a company," says Badciong. "It was essential to our survival as a company."

Prior to Inlanta's full-eagle status, the company toiled as a correspondent lender where it would take a borrower's application but had to outsource the underwriting to other lenders. It was an expensive process for Inlanta both in terms of a higher price charged to the company to sell its loans and for the maddeningly slow turnaround time—often weeks, not days.

Acquiring Direct Endorsement authority added a proverbial booster rocket to the company's FHA business, as it now can approve files quickly for borrowers. The faster turnaround and ability to avoid underwriting backlogs at other FHA operations translates into a huge competitive advantage for Inlanta, says Badciong.

Branching out with partners

In 2002, Knowlton says the company devised a way to both allow for its measured expansion while also keeping some of its best originators from quitting and opening their own offices. The approach the company went with was a system of branch partnerships.

An adaptation and improvement from the net branch model, Inlanta's partner branches combine the agility and independence of a mortgage broker with the administrative and logistical support (i.e., marketing, human resources, information technology, etc.) of a major company.

"In the heyday of the business, a situation we would run across a lot was branch managers would feel they would have a better opportunity if they would leave and open their own business. What we [devised] is what I call an inverted P&L [profit and loss statement]," explains Knowlton.

"We'd take the fees off the top of the P&L, and the balance belongs to the branch. They're still employees, they all work for us, we assume all the risk—but if you have a good operating branch manager who is knowledgeable and strong, and controlling expenses, it can be a win-win for them. That's how we've changed and adapted to the way the market was changing."

As Inlanta's branch recruitment manager, Ramis says the lion's share of his duties consist of being the "main go-to person" for branch managers even as he recruits new partners to manage new offices in new locales. Ramis has to avoid micro-managing the branches while at the same time ensuring the loans they originate meet Inlanta's exacting standards for quality and ethical dealings.

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"As a partner office with Inlanta, you're becoming an employee. That mortgage broker is now becoming a branch manager. His loan officers are coming on and becoming loan officers of our company," explains Ramis.

"We're going to interview all the people and make sure they're all a good fit for our organization, and we're going to make sure they're doing things correctly. We may be monitoring them more than they were used to and more than a 'traditional' net branch would have done in the past," Ramis says.

Although the system is long on reward and short on

risk for branch managers, Knowlton says the branch partner concept has been a critical and successful component of boosting Inlanta's profit and expansion efforts.

Adapting to FHA's changes

As a lender that does just about half its business with FHA, the program's several recently announced changes—in no small part due to the unprecedented turmoil in the mortgage market and the overall financial sector—have kept FHA participants like Inlanta Mortgage scrambling to adapt and keep the proverbial ground under them.

Most recently, in April, FHA announced the adoption of new regulations significantly raising the net-worth requirements for FHA-approved lenders and making lenders liable for oversight of the mortgage brokers with whom they do business.

All new lender applicants for FHA now must possess a minimum net-worth of $1 million, while current FHA lenders have been given a period of one year to possess the mandatory minimum $1 million net worth. In addition, within three years, all lenders will need to show additional net worth of 1 percent of total volume in excess of $25 million of single-family insured mortgages up to a maximum of $2.5 million.

"[FHA] did a nice job doing a gradual implementation of that requirement," says Badciong. "When Fannie Mae took their net-worth requirement to $2.5 million, [it was in just about] a year's time that they had to go from $1 million up to $2.5 million. FHA has been generous enough to give three years to hit that $2.5 million benchmark."

This follows another set of policy changes FHA announced in January to better manage risk, including an increase in the upfront mortgage insurance premium (MIP) from 1.75 percent to 2.25 percent; reducing seller concessions from 6 percent to 3 percent; and requiring new borrowers to have a minimum FICO® score of 580 to qualify for FHA's 3.5 percent down-payment program. New borrowers with less than a 580 FICO score will be required to put down at least 10 percent.

Given housing market conditions in the Midwest and the caliber of Inlanta's target customer, Badciong says she doesn't expect FHA's MIP changes to have a significant impact on the company's production overall.

"The nice thing about the upfront mortgage insurance premium is making sure the loan originator and the customer understands that it doesn't have to be financed into the loan amount. It can be paid for outside of closing. So if the increased upfront premium is a hurdle to the borrower qualifying for a little bit higher loan amount, you can use your seller concessions," explains Badciong. "Being able to price it into the loan a little more and pay it on their behalf can mean that they can qualify for that loan."

Badciong notes she is similarly unconcerned with FHA's announced cuts in allowable seller concessions, noting that lenders were similarly concerned with the loss of the down-payment-assistance programs but they adapted and moved on.

While it can be maddening, at times, to try to keep up with and adapt to the various changes and tweaks in FHA policy, Badciong recognizes the government's risk-management intent. But all of that tweaking comes at a cost, she says.

"The increased scrutiny on quality control for lenders is a cost. Any time we have a cost, someone has to pay for that cost. We're not a nonprofit organization, although it seems like that sometimes. Ultimately you have to make money, and the people that pay you the money are the consumers," says Badciong. "I don't think FHA wants to stay in this position. They want private market share to come back in to the mortgage industry. [The question is,] how quickly can our economy support that?"

Building from relationships

Inlanta Mortgage's professed conservative values do not by any means inhibit ambition. While he aspires to achieve a national presence for his company, Knowlton says he's looking for slow and steady growth.

"We're conservative Midwest people, and we're looking to grow the company at a reasonable pace over time," says Knowlton. "We would rather run $40 million a month in volume profitably than $60 million doing volume for volume's sake."

The tangible result of Inlanta's strict, institutionalized adherence to fair play has been relationship-building and the consequential repeat business and referral business resulting from those carefully crafted and maintained relationships, says Jim Snyder, a 15-year veteran Inlanta originator.

Inlanta manages and constantly updates a database of clients the company uses to keep in touch with them long after the initial transaction is completed. More often than not, says Snyder, this bears fruit in the form of repeat and referral customers, and positive word-of-mouth.

"We emphasize strengthening relationships with the customer by the service we give them. . . . The clients we get in my office are either repeat customers, relatives, friends [or] co-workers. That is basically the advertising that we have. The only way you can get that to work is, obviously, you have to do a good job for them at the time," explains Snyder. "From the relationship-management that we do, I've had clients call me recently who I worked with in 2002–2003. Without that relationship, who would call [us] after seven years?"

The more Inlanta Mortgage grows, the more new opportunities for growth appear—one transaction, one relationship, one branch office at a time. For the moment, says Ramis, Inlanta's territory remains clustered within Middle America, but its expansion goals remain more about finding the right fit than conforming to some geographic manifest destiny.

"I don't see any cap on [growth potential throughout the United States]. We want to continue to maintain the service for our existing offices and be able to handle the new offices that come on, get them transitioned, get them set up and operating, and continue to grow from there," says Ramis. **MB**

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