Mortgage Broker Commissions and Incentives - A Primer

After getting business in the door and completing the funding of a loan, the third most difficult job for the average Mortgage Broker could very well be the task of calculating and paying commissions for the agents involved in the transaction and other relevant parties.

The typical mortgage brokerage varies from 2 to 30 agents working in a local office. Lending houses can have much larger agent and payee populations. Most agencies are independently owned by an owner-broker and address customers in their local area, but there are also large brokerage consisting of many local offices. There are more than 44,000 mortgage brokerage companies in the US and they employ more than 360,000 people. In 2003 these agencies originated more than $2.5 trillion worth of mortgages.

Commissions to agents/brokers are easily the lion's share of the expense of the typical brokerage. "Our commissions related expenses amount to 80 percent of our total expenses", says Dennis Loosli of Community Lender, "we have to pay a lot of attention to this". How to accurately and timely calculate the correct amount of commission remains a very important task even after the transaction is completed. Errors in calculation and late payments of commission could easily lead to agents' distrust and frustration towards the brokerage. There are cases of inaccurate commission calculations resulting in lawsuits by the personnel involved. It is not much better from the brokerage perspective, since trying to get all the loan information and calculating the commissions and bonuses regularly is a difficult error-ridden task with a lot of manual work.

Different roles

The primary recipients of commissions are of course the agents/brokers employed by the brokerage. Some brokerages also employ loan processors, who do all the paper work, coordinate with the lender and the customer, and will get a fixed processing fee from each loan closed. Most brokerages are concerned with the calculation and payment of commission for only these personnel. They are variously known as Brokers, Loan Execs, Loan Officers, Loan Processors, etc.

Some brokerages may have a senior level of brokers responsible for other brokers. These personnel are variously known as Sr. Loan Officers, Sales Manager, Local Office Manager, etc. In addition to closing loans personally and getting the commissions, these personnel may be eligible for commissions on loans closed by subordinate staff. Most brokerages also have an Owner Broker who may also need their commissions calculated, just to keep their records straight.

Some brokerages pay a referral fee to people outside the firm, such as Real Estate Agents. These payments will also need to be calculated as part of the commission calculations.

What to incent

The primary activity for which sales commissions are paid is the activity of Loan Originations. This accounts for 90% or more of all commissions and incentives paid out to personnel. Typically the completion of a loan (Loan Closing) triggers the payment of this sales commission.

For loan originations the following components can be incented for, separately or together. Origination Fee (Points), Additional Points (additional points negotiated by the broker), Premium Spread (if interest rate more than the Loan Product's interest rate, the bank provides a rebate), Additional Fees and Costs (such as appraisal fee, processing fee, credit report fee, etc. negotiated by the broker). There could be additional components or the listed components could be broken down into more detailed components based on the particular firm's needs. Typically the entire set of components is referred to as Loan Income, Net Revenue or Gross Profit.

There can also be deductions related to loan originations which may be used to reduce the income related to a loan. These can be occasional deductions such as when the brokerage ends up paying the appraisal fee for a loan, it can get deducted from the specific loan's income. Some firms can also deduct a standard fee on all loan origination commissions to cover processing, marketing costs, etc.

The other key incentive is in the area of referrals. Referrals of loans to the brokerage generate incentives for the referrers. These referrers need to be tracked and paid as well.

How to Incent

There are as many ways of incenting personnel as there are firms in the mortgage brokerage industry. But here are some common methods that companies have used in implementing their incentives.

Frequency of payment

Firms pay out their loan sales commissions weekly, bi-weekly or monthly. Referral Incentives and Bonuses maybe paid out monthly, quarterly or even annually.

Loan Sales Commissions

Loan Sales commissions are based on the loan income. The loan income can be various components of revenue related to a loan as well as possible deductions. Companies typically provide a portion of the loan income to the broker involved. This is typically a percentage varying anywhere between 40 to 80 percent of the loan income.

Percentages can vary for many reasons. The various reasons to vary percentages include:

- seniority of the personnel
- use of a preferred provider for the loan
- whether the loan is referred or not

- loan programs such as VA, FHA
- type loans such as Conventional, Jumbo, Heloc, Refinance, etc
- source of loan
- loan size

Percentages can also vary based on tiers of achievement of Loan Revenue, Loan Income or even number of loans. For example the percentages can vary as in the following example:

Loan Volume	Commission %
1 – 1,000,000	50%
1,000,001 – 3,000,000	60%
3,000,001 and above	70%

Referral Incentive

Referrers of loans to the brokerage typically get a flat payment per loan. The flat payment can also be varied based on volume of referrals brought in by the particular referrer. These incentives are typically paid out monthly.

Bonuses

In addition to the Loan Sales Commissions it is common to provide bonuses based on number of loans, total loan volume and other total performance measures. These bonuses could be monthly, quarterly and rarely, annual. The bonuses could be based on tiers of performance or in comparison to a performance goal.

Splits

The loan income is basically split between the brokerage and the broker. The broker portion is considered the sales commission. In addition the commission could be setup to split between multiple brokers such as a senior and trainee broker.

Overrides

In firms where there are loan sales managers, the loan sales managers can get an override commission on every loan closed by brokers reporting into them.

Challenges

Designing the plan

The initial challenge is the task of designing a suitable commission and incentives plan for the firm. Prior to designing the plan the firm has to undertake an analysis of the goals of the company and performance it wants to achieve. Various answers could ensue from this analysis. For example:

- we need to sell a lot more jumbo loans
- we need to incent high volume producers higher
- we need to increase our referrals business so we have a lot of deals to work with

Administering the plans

Once the priorities of the firm are established the next challenge is to setup and administer the plan. The task of tracking all the loan and referral transactions, entering it into a calculation system by the specified time period is quite a bit of effort.

After that, the various calculation rules have to be applied to the transactions to figure out the payment for individual brokers. Summaries have to be calculated to provide information for cumulative bonuses. Splits and overrides also have to be calculated. Trying to do all of this on a regular basis weekly and bi-weekly, accurately becomes very difficult for the average firm.

"Almost everyone one of our personnel end up having a unique pay calculation. Changes to these plans is quite painful to implement. They get very frustrated with not getting a report showing all the details of their calculations. What I wanted is a way to calculate and administer plans with a single button click and provide clear reporting to my staff", according to Dennis Loosli.

Solutions to this problem typically take the shape of paper calculations or at the most, Excel spreadsheets. Both tend to create inaccuracies and subsequent issues with the brokers involved. The recommendation is to administer this using a software system.

Communication

The entire calculation then has to be presented as clear statements to the broker. All the transactions involved in the calculation as well as adjustments should be provided in detail to inspire confidence and comfort in the company's process.

The statement should ideally accompany the payments to the broker and should be provided in a timely manner. Various methods of delivery should be considered, including paper reports, emails and the web for easy accessibility to the broker.

Conclusion

Sales commission calculations are a difficult and painful process for most mortgage brokerages. Simplifying the design and administration of these plans can help companies reduce this distraction, eliminate payment errors and liabilities, increase the broker's morale, efficiency and possibly revenues and income.

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