

Consumer Finance Monitor (Season 4, Episode 22): A Close Look at the Use of Blockchain Technology in Consumer Finance, with Special Guest Debbie Hoffman, Associate General Counsel, Western Union

Speakers: Alan Kaplinsky, Debbie Hoffman

Alan Kaplinsky:

Welcome to the Consumer Finance Monitor Podcast, where we explore important new developments in the world of consumer finance and what they mean for your business, your customers and the industry. I'm your host today, Alan Kaplinsky with the Ballard Spahr law firm, and I want to remind our listeners that in addition to our podcast show, which is called Consumer Finance Monitor, we have a blog, which we've maintained now for almost 10 years, and I would encourage you to subscribe to our blog. We cover everything that's going on in the consumer finance world, including the topic that we're going to address today. You can find our podcast show. It's on our website.

Alan Kaplinsky:

It's on essentially whatever platform you use to access your favorite podcast shows, you will be able to find our podcast show, and so today, we're going to talk about a subject that we haven't previously addressed on our show because there aren't too many people that I would consider to be really expert in the area. Fortunately, the person who I'm about to introduce to you, our paths crossed a couple of years ago when I chaired a Practicing Law Institute, Annual Institute on Consumer Financial Services, and we were doing a segment on new technology in the consumer finance world. As I was searching for the right speaker, fortunately, I found out about Debbie Hoffman, who is our guests today, and I learned about how knowledgeable Debbie is in the area, and so the topic we're going to talk about today, after I give Debbie the appropriate introduction, is what are the use applications in the consumer finance world for blockchain? We're not going to be talking about cryptocurrency and what's going on in that area, which, of course is all connected to blockchain, but we're going to talk about other use applications. Let me introduce Debbie to you, and then we'll get into a discussion of this topic.

Alan Kaplinsky:

Debbie serves as Associate General Counsel at Western Union, and she heads up the Technology, IP, Real Estate and Procurement team. She's also an adjunct professor at Albany Law School and teaches a graduate program course called Understanding Blockchain, Cryptocurrencies and Law. Prior to joining Western Union, Debbie founded her own company called Symmetry Blockchain Advisors, which focused on endeavors related to the education strategy and implementation of blockchain solutions, with a focus on the real estate finance industry. Debbie, a very warm welcome to our show today.

Debbie Hoffman:

Thank you, Alan. It's great to be here, and I'm excited to introduce your listeners a little bit more to blockchain.

Alan Kaplinsky:

Okay. I know that there are people who listen to our show who are very expert in the area of consumer finance, but when it comes to some of the newer technologies, maybe not so expert, and I found that you're one of the few people I know that's really, in a simple way, able to define blockchain, so really, as a way of a level set here, I'm wondering if you could do that for me and our listeners.

Debbie Hoffman:

Absolutely. Most listeners have probably heard of cryptocurrency and Bitcoin, but what they may not know is that blockchain is the underlying technology that was basically first introduced when Bitcoin was introduced in 2009, so blockchain became much more known originally through Bitcoin, but then in the mid-teens of 2014, '15, '16, and especially in '17, it started to boom in industries as a platform for data sharing and for sharing of currency as well, simultaneous sharing of information. Basically, what it is, is it's a ledger system in which you can record information and share it among parties, and the parties do not have to be affiliated. It could be what we call untrusted parties, and you share this information from party to party in this ledger. This ledger that is what we call immutable, it cannot be erased.

Debbie Hoffman:

It's a permanent ledger. It's a ledger that has transparency, meaning you can look at the ledger and determine who had access to it exactly and when, and the very unusual characteristic of this blockchain technology is that the way it's stored, it is stored on a variety of computers. We call them nodes in blockchain language, instead of just being stored on one or two backup servers, so there's this whole concept of, the cryptocurrency concept that it's much, much harder to hack, so it's a cybersecurity. It can be actually a cybersecurity protection of sorts because of this, what we call this decentralized ledger.

Alan Kaplinsky:

Okay. Debbie, what do you see as the main benefits of using blockchain in the consumer finance world?

Debbie Hoffman:

Thanks, Alan. As I was just kind of saying what it was, if we take that to the consumer finance world, it's a way that you can transfer data effectively through the consumer finance supply chain, so if you look at any kind of loan or auto loan, student loan, mortgage loan, personal credit cards, you can share this data with a variety of, what I called earlier, untrusted parties, which allows for data transparency for recordkeeping, for real-time transactions, for audit trails, and obviously for audit trails both internally and externally, so it's a way that you can process this data from all these different parties within that lending ecosystem in a much more efficient way and in a way that's ultimately going to reduce the cost to the consumer.

Alan Kaplinsky:

Right. Okay. In the last year that we've been through, there've been a lot of changes that have occurred. Very, very difficult time obviously, so how does this affect the adoption of blockchain in the consumer finance process?

Debbie Hoffman:

When I look at what the world was in consumer finance, and we all do, obviously, it was not just the volume, but the actual world in which we worked, it was mostly paper, or a lot of paper before 2020. In 2020, everything became digital. It became all about putting information in a digital system, and what we started to see was, really, as the pandemic came on in March and April of 2020, was the way all the parties, the lenders, the GSEs, the state regulators found ways in which to operate in this lending environment in a more digital manner, and so they, for instance, the SAFE Act allowed for opening up of remote licensing, and as well as all the other players, so there were so many companies that realized, "This is the wave of the future. We have to go digital," and we saw those in acquisitions.

Debbie Hoffman:

We saw that in some of the smaller, anywhere from Docutech by First American and ICE to Ellie Mae, is that the wave of the future is fully digital, and so this concept of having a fully digital loan can be extended to ... That's the most basic concept that you need to have to have blockchain technology implemented because you need everything to be digital for blockchain to work. I think what it is, what 2020, 2021, the early part did for us is really push this industry forward in a much faster pace than it might've taken during other times.

Alan Kaplinsky:

Yeah. Sure, sure. What about so-called smart contracts? I hear a lot about that lately, and does that have ... First of all, what are they, and what's the impact in the consumer finance industry?

Debbie Hoffman:

All right, so let's start with what a smart contract is.

Alan Kaplinsky:

Yeah.

Debbie Hoffman:

It's a, basically a contract- It's a language that is a contract to show a language that's embedded into software, so it's become self-executing, and so I think of it as a workflow that is not just within an internal party, but has external parties, like I keep saying these unrelated parties. A lot of attorneys might argue that it's not exactly a contract, it's contract language that's embedded into code. It's a combination of both. You could argue both sides on that one, but it's automated, so in the context of consumer finance, or I'm going to just take it down to the real estate level itself, if a buyer makes a down payment in the amount of, let's say \$20,000 and, to purchase the home, if that's the execution, if that's the down payment price, the smart contract could automatically execute and say, "Okay, buyer, put the money in escrow," so now, a notice has to be sent to the inspector and the appraiser to continue with their work.

Debbie Hoffman:

It's an automatic workflow. You don't need a person there hitting a button saying, "Okay. Go get the appraiser on it. Go get the inspector on it." It just automatically would happen if it was coded into the smart contract.

Debbie Hoffman:

That's kind of the way it works, and you can think about that in everything that we do in consumer finance, so from credit history, when you do the credit history checks, the identity checks, you can do it in KYC and AML, you could, obviously in the release of funds, so there's just a variety of ways that smart contracts could be coded into the operations internally within a lender.

Alan Kaplinsky:

Is this being used right now in certain areas, like for example, you mentioned, gave us an example somebody buying a home, and which I just did last year, and there were a lot of things that had to fall into place, getting an appraiser, getting somebody to get title insurance and get homeowners insurance on the house, and there were all these pieces, and I would typically just rely on my real estate broker, or I had a lawyer too, and she would tell me what I need to focus on now. Are you saying that if I had been part of a smart contract, that that all would have just happened without human involvement?

Debbie Hoffman:

Yeah, so you're absolutely ... The answer to that is in a perfect blockchain world, that's the concept. What we're seeing now is a much more basic implementation of smart contracts because it's in nascency, so we see it at certain parts of the chain. I've seen it in UCC lending. I've seen it in, actually in commercial loans, some of the commercial loans that I've seen, so we have not seen it that much in execution level in the real estate residential market, or we've seen it a little bit in some of the other markets, but it's very early on because ...

Debbie Hoffman:

I think there's a lot of reasons of it because, but it has a lot to be developed as far as being implemented on a wide scale level.

Alan Kaplinsky:

Right, and I take it after a loan gets originated, if there's servicing that needs to be done on that loan, that also can be built into the smart contract, that doesn't-

Debbie Hoffman:

Yeah.

Alan Kaplinsky:

Yeah.

Debbie Hoffman:

Yeah. I think there could be a whole work stream within a service or to have built-in operations using smart contracts, so everything that's done on an everyday level, you could really have that much more automated by use of smart contracts.

Alan Kaplinsky:

Yeah.

Debbie Hoffman:

Absolutely, yeah. Yeah.

Alan Kaplinsky:

Okay. How does blockchain address the concept of identity, and what are the implications in the consumer finance industry?

Debbie Hoffman:

Alan, when you, right now, when a borrower goes and gets a loan and they're signing their note, and the title company comes to take the notary, what do they have to show the title company?

Alan Kaplinsky:

Yeah, the identification.

Debbie Hoffman:

They'd have to show their driver's license, right?

Alan Kaplinsky:

Yeah. Right, right.

Debbie Hoffman:

So our driver's license right now is the key, or our passport or some kind of identification, to doing everything we do, and all in consumer finance, but of course, in everything else, from travel to when we go to the doctors, so the concept of digital identity is actually one that has been brought out by blockchain because it enables this collection of data points on a platform that's stored on this blockchain protocol, and it basically creates identity by having all these data attributes, and there's not one single owner. It's basically the concept of identity on the blockchain is that you kind of own the pieces that you put into it and you can release them to the entities that need them, so your doctor doesn't need everything about you. They need certain bits and pieces about your identity you could show to them, and so this whole concept of digital identity obviously is really interesting for consumer finance because identity is such an integral part of finance. While I'm fascinated by the fact that we

have these remote notarizations and that they're really gaining steam, I do think that the future is eliminating the notary and having this whole concept of identity directly on the blockchain.

Alan Kaplinsky:

Yeah, but what impact might it have in preventing identity theft? Does it have any potential there?

Debbie Hoffman:

I think the question for that is, I actually think that's a fabulous question, because I think that people are going to have more concern about putting their data attributes on a protocol, but I think the key here is that if it's built correctly, a blockchain is, like I said earlier, it's a distributed ledger, so all of these ... The way it's stored is in not one server, so in order to ... It'd be much more difficult to hack a blockchain protocol with these data attributes in it. That's number one.

Debbie Hoffman:

Number two is the concept is that you could have control over those data attributes. You're not giving it to a third-party to verify your identity, so that's, again, the second part of it. There's a lot to be addressed there, I think. I don't know that I have all the answers, but I do know that the entities that are looking at putting identity on the blockchain are addressing these kinds of points as they build out these protocols.

Alan Kaplinsky:

Right, right, right, right. You mentioned KYC, and for our listeners, we're referring to the Know Your Customer rule, and AML, Anti-Money Laundering, you mentioned that the process in the context of smart contracts. How else could blockchain work in these procedures?

Debbie Hoffman:

I am a proponent that blockchain technology can not only enhance how institutions engage in compliance procedures, but I think that it actually could revolutionize the entire compliance ecosystem. What I mean by that is it has the potential to streamline the AML process because of all of the due diligence that goes into fulfilling the KYC process in an efficient manner. Let me just give you a few examples of that. For instance, we talked about data points. It could improve the method by which all the data is managed in this AML process.

Debbie Hoffman:

Secure identity management, I just talked a little bit about identity, but basically, you can share this data across risk officers and regulatory bodies as they need them. Recordkeeping and reporting, you can have access to the ledger by the parties that need it when you're doing these processes, you can have automated reporting, you could have real-time updates, and probably most importantly is transparency, so you can identify a client, you can do due diligence on an enterprise-wide level, the immutability of the ledger that you could see who was putting what in, when they were putting it in, and again, you're sharing it across that entire enterprise so that red flags are more easily identified by sharing that data through the enterprise. That's kind of the, at a high level. I've read a lot about this. I've written a little bit about it, and I'm just very ... There's a lot of platforms out there being developed to address KYC procedures.

Alan Kaplinsky:

Right, right. Another question that I have for you, Debbie, is wire transfer fraud in the closing process. Can blockchain technology help in dealing with that?

Debbie Hoffman:

Yeah, so that's one of our big, hot points right now in our industry, that the last minute instructions go to the purchaser and they've been hacked, and then they send their lifetime savings to the wrong entity, right? A blockchain would allow for this transparency, this traceability and the recordkeeping during the closing process. I'm not saying just at the one step where they have to do the wiring, but in the entire process, so ultimately, this platform that you communicate on, and you have all the parties on there, you have the buyers and the sellers and the other stakeholders using this platform that is very transparent would prevent that. It's, again, it's not just at the last level, it would have to be during more of the whole entire process.

Alan Kaplinsky:

Right, right, right. Okay. What about peer-to-peer lending? Is blockchain being used in that area, or does it have potential for use in that area?

Debbie Hoffman:

Yeah, Alan, it's being used in all ... Blockchains are being used in peer-to-peer and student loans, auto loans. It's become very popular in those areas because it offers to individuals who might not ... Basically, individuals who might not qualify for a loan are able to figure out ways to borrow money through this peer-to-peer lending that is on ... I mean, we've seen it not only on blockchain, but on other platforms as well, and so the whole concept of this peer-to-peer lending has exploded in the last year, with something called decentralized finance or DeFi, as people refer to it.

Alan Kaplinsky:

Mm-hmm (affirmative). Right. Okay. In 2020, there are, as you pointed out, there's been a lot of buzz about the term DeFi, decentralized finance as it applies in the blockchain. How does it apply here?

Debbie Hoffman:

The concept of DeFi is to democratize finance by replacing institutions with peer-to-peer relationships that can provide for a wide variety of financial services. It includes banking, loans and mortgages, and even in complex trading. What we think about today when we think of direct, we think about something that still has a middleman, so PayPal or Venmo, but that's still facilitating the work. In blockchain, if you use DeFi as a [block 00:22:24] ... It enables more of this direct access to a consumer in a financial transaction, and just another, just to throw a kind of a buzzword out there that we've seen in DeFi is something called decentralized apps or dApps in a variety of ways, so trading and securities and insurance, decentralized exchanges, E-wallets, NFTs, which has been very, very hot in 2021, and something called Flash Loans.

Debbie Hoffman:

There's definitely some risks associated with DeFi, and I think it's very new ... It's still new and exploding, but it is something to watch.

Alan Kaplinsky:

Yeah. Are there companies that you're watching as they apply the blockchain technology in consumer finance?

Debbie Hoffman:

There's a bunch of companies out there that were watching lead the way. It doesn't mean that others won't follow, but it's the ones that are really making headlines as far as experimenting in this. The biggest one that we see in the news these days, I think is called Figure. Mike Cagney, he was the founder of SoFi, and he has been out there, really discussing some really great details about what blockchain can do, especially in mortgage lending. Figure is probably the, like I said, one of the biggest names, and it states that it uses blockchain for origination, custody, trading and securitization.

Debbie Hoffman:

The company's done a whole bunch of things out there, especially, it started off with HELOCs, and they've raised a lot of money. The second one I noticed is Symbiont. People say that different ways, but I say Symbiont or Symbiont, I guess. It advertises that it's a market leading smart contract platform for institutional applications of blockchain. There's also been...

Debbie Hoffman:

Again, there's been announcements. I'm not inside of these companies, but the announcements are, for instance, trading assets, entirely devoid of paper or testing blockchain-enabled, asset-backed securities or storing investment data. SALT is one of the earlier companies, and when I say earlier, I'm talking like four or five years, not even that long ago, but it gained a lot of popularity, is one of the first blockchain lenders. Users of the SALT platform can borrow money using crypto and Bitcoin or Ethereum as collateral, and the loans are based on the value of the collateral and not on a credit score, so it opens up a whole different type of lending. Then, we have the more institutional lenders.

Debbie Hoffman:

We've been hearing about J.P. Morgan's use of blockchain and crypto a lot lately. One of its pilots has used blockchain to manage auto loans to keep track of the cars, to help prevent fraud, and just to have real-time data, to prevent a dealership from double financing the same car. Then, there's also a bunch of entrepreneurial companies that are really leveraging blockchain in different ways. It'll be interesting to see how those companies partner up with more of the longer time companies. One of them that I have followed and worked with a little bit is Bee Mortgage App, which is using the blockchain for a, what Bee Mortgage calls an automated process and sharing of data to provide a one-stop shopping experience for distressed consumers.

Debbie Hoffman:

There's quite a bit out there. I mean, we'll see which ones continue to make headlines and which ones really grow the opportunities in blockchain and consumer finance.

Alan Kaplinsky:

Right. Debbie, as we draw to the end of our podcast show, you've described a system or a blockchain technology that is got ... It's already, I guess I would say has found a home for many aspects of the consumer, many parts of the consumer finance industry, but like any technology, be it our AI or data aggregation, I assume there are some risks and regulatory hurdles that have to be overcome, a lot of education, I would guess of if you've got a regulator, not too many of them are going to be as knowledgeable as whatever company you're talking about that's using blockchain. Maybe you can describe in a general way what some of these risks are and hurdles.

Debbie Hoffman:

Yes, Alan, thank you. I'm actually thinking I'm going to focus in on ... There's a few, but the main ones I think are some regulatory hurdles, and so it's really because you have to know how to apply the law of what you're building, and so there's a few things you have to look at there. First, you want to look at, "What's the jurisdiction?" so, "What is ...". Of course, you can agree to a governing law and contracts, but just more generally, so you have cross-border, you have global jurisdictions, you have federal, and you have state guidelines, and there's a whole bunch of regulatory agencies that are looking at this from different ways.

Debbie Hoffman:

First, you kind of ... Then, you also have to consider those agencies. Are we looking at the CFPB? Are we looking at the OCC? Are there tax implications?

Debbie Hoffman:

Very specific to crypto, there's three that I'm going to highlight, because those three have been the most that we've seen in the news, so I want to make sure that the listeners kind of know where those play in the blockchain space. FinCEN applies to

those that are using an exchange in cryptocurrency, so it's very specific to cryptocurrency. The Bank Secrecy Act applies to money transmission and virtual currency, so it could come into play in a variety of ways. The SEC is a huge one because of the fact that the information stored on a ledger can sometimes be considered traded as security, so it's not just information, it could be something of value that increases in value, so you need to have some SEC guidance there. Then, the CFTC also applies to commodities and digital currency.

Debbie Hoffman:

While I've been talking mostly about blockchain as a ledger, these all come into play potentially on how you're using the ledger and how you're using your data. Then, there's other things like data privacy that you need to consider, and you need like GDPR, what kind of information is going on there, and does California law come into play, so I think the biggest ... What I'm getting at is the biggest hurdles are these regulatory hurdles and making sure that you have some guidance with how you're operating your ... Not just how you're operating, but how you're building your blockchain and how you're implementing it, and what are the regulatory guidance that you need to follow when you're doing that?

Alan Kaplinsky:

Yeah. Just following up on your answer, do you perceive a need for special laws to be enacted, either at the federal level or at the state level that would facilitate the wider use of blockchain technology? Are there areas of great uncertainty right now, I mean, like such as we've got a uniform commercial code that deals with mostly paper-based transactions, but some digital transactions? I don't know if things that occur on the blockchain, are they covered by the UCC, or what is the lay of the land there, just in a general way?

Debbie Hoffman:

Yeah, I think you hit the nail on the head by identifying ... The fact is that a lot of the laws don't anticipate this technology being used in the way that it is, and so there's both state and federal law emerging, and there's even across the country, there's different states that have bills that are being passed to try and clarify some of this. There was actually a bill ... Yeah, there's just been all different states where we could probably go in on each state and talk about what's going on in each state, and so I think there's just a tremendous need to make sure when you, again, when you do this, that you have somebody who's up-to-date on that, number one, but number two is, I guess I kind of, I want to make sure that you also look at the laws that are applicable to the business in which you are operating, and so that's kind of the key, is defining the business and how the laws apply to it and how they could be interpreted with the implementation of new technology, and exactly what you were saying, paper versus digital and that kind of thing.

Alan Kaplinsky:

Yeah. Yeah. One other question, I'm curious, we haven't talked very much about crypto, but to what extent do you think the future of blockchain and the use applications that don't relate to crypto are dependent upon ultimately the success of crypto? We don't ... I guess you could say the final shoe hasn't really dropped in the crypto area.

Alan Kaplinsky:

A lot of people thought it was just a fad and it's going to go away. A lot of minds have been changed over the past few years, and it certainly looks like it's here to stay, but there's still a lot of uncertainty about crypto-

Debbie Hoffman:

Right. No doubt.

Alan Kaplinsky:

Yeah. Yeah. What do you think? Do you think ... I mean, is everything ... Is the blockchain tied to wherever crypto goes?

Debbie Hoffman:

I've been doing blockchain for a few years now, several years now.

Alan Kaplinsky:

Yeah.

Debbie Hoffman:

It's really interesting because there was a period when crypto was not ... It was high in 2017, a little bit in '18, but in 2000, towards the latter half of '18 and to '19, it got to be not that ... It wasn't in the headlines as much, and so people thought even the blockchain was a thing of the past, even though these companies were developing, continuing to develop blockchain protocols that, as I just talked about, could really make a difference in industries. What crypto does is, it's really, I didn't get into that much, but there is a whole liquidity factor that you can add into a blockchain protocol, so it's really critical to blockchain protocols as well, the transfer of money. What the headlines do is they enable people to...

Debbie Hoffman:

They get intrigued by crypto and they get intrigued by, "Oh, Bitcoin is rising. It passed 49 up to 50, up to \$50, down to 50," and so people are so intrigued by that, and then they ... So they learn about it, and then they learn about this whole underlying technology of blockchain, so what it does is it helps the industry, no doubt grow because of people's interest in crypto, but ultimately, I do think that they will separate out the crypto versus the blockchain protocol, and I do think blockchain protocol will continue to grow, but no doubt, we need those crypto headlines to enable that growth, to help the funding of blockchain protocols.

Alan Kaplinsky:

Right. Got it. Okay. Well, I don't know if there's anything else you'd like to add that you think our listeners ought to be aware of, Debbie, that we haven't covered, and if so, here's your opportunity to do that, but if not, I think we can wrap things up.

Debbie Hoffman:

Okay. The only thing I'm going to say is don't be daunted by the fact that you are not a technologist and walk away and say, "I can't understand blockchain because I'm not a technologist." If we all did that to our iPhones, none of us would probably use, or very few of us would use our phones, or Androids, so walk away with enough armor of what blockchain is to know that it's a, what it can do in the industry, how it can change this data storage and transfer, and not necessarily always trying to understand the nitty-gritty of the technology beneath it. I mean, you can if you want to, but you shouldn't be daunted by that. One of my biggest nits is when people say to me, "Oh, I don't understand blockchain, and I don't have the time to basically figure this all out," so you don't have to. You just have to understand what it can do for whatever industry you're working in.

Alan Kaplinsky:

Well, Debbie, thank you for absolving me and my colleagues in the consumer finance industry of being timid in this area. It is something that I think is difficult for a lot of people to grasp and to put their heads around, but I take what you just said very seriously. Debbie, want to thank you very much for joining us today, and you've been very helpful in shedding a lot of light on an area where we haven't previously gone with our podcast show, and I'm sure in the coming months and years, there are going to be many, many more developments, and if there are, we'll want to certainly bring you back on our show to talk about it, but thank you.

Debbie Hoffman:

Thank you, Alan. It was an honor and a privilege to be on your show today.

Alan Kaplinsky:

I want to thank all of our listeners today for downloading this podcast, and just again, remind you that we release a new show every Thursday. You can find it on Google, Apple, Spotify or our website, or essentially any podcast platform you may use, and be sure to subscribe to our blog, and we also do a lot of webcasts, so to make sure you're on our invitation list to get the invitations, you ought to go on our website and there's a way to communicate with us there. Thank you once again.