LEND ACADEMY

PODCAST TRANSCRIPTION SESSION NO. 79: STEVE BISBEE

Welcome to the Lend Academy Podcast, Episode No. 79. This is your host, Peter Renton, Founder of Lend Academy.

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Peter Renton: Today on the show, I am delighted to welcome Steve Bisbee. He is the President & CEO at eOriginal, a company that he co-founded about 20 years ago. So eOriginal is a fascinating company, they have basically created a technology to verify original documents electronically, there's a whole host of services they do around that. We actually dig into their technology in some depth in this interview, we talk about what the actual services are that they're providing for the marketplace lending sector and for other verticals for that matter. We talk a lot about how transparency is important, why it's important, we talk a little bit about regulation as well as demands from the investor side of this business. It was a fascinating interview. I hope you enjoy the show!

Welcome to the podcast, Steve.

Steve Bisbee: Good afternoon, Peter.

Peter: Okay, so let's get started. I want to get a bit of background about yourself. I know you've been in your current role for quite some time, but can you give us some background about yourself and your company.

Steve: Certainly, so I have been the President of eOriginal really since its founding, I was one of the co-founders. I was also the co-inventor of the eOriginal technology some 20 years ago, and at that time…I've been a small serial entrepreneur and at that time I was involved in real estate. I had a title insurance company and we were struggling at that time with how to have a fully electronic mortgage transaction. There is a national association called the American Land Title Association (ALTA) that was looking for people to volunteer to see if they could come up with a solution to be able to create a fully electronic mortgage transaction.

I was asked to join that effort, which I did, and we were able to see looking forward in the future, certainly not at that time because this is in some ways pre-Internet for financial services, but that documents were going to be able to be created electronically, presented electronically, signed electronically, delivered electronically, managed electronically so then I became involved in the process in the volumes, the challenges in that particular industry.

But there was one aspect of the mortgage closing which really became a stopping point and it was in a mortgage closing...you're signing a promissory note and that promissory note, that mortgage note, is a negotiable instrument. And by negotiable it means that one or two parties may contract, the borrower and lender may contract, but that document then gets sold off into a secondary market. And in order for that document to be able to be sold off in the secondary market, there has to be only one of them. There has to be a unique document and there's a series of laws around what constitutes a negotiable instrument and how it works. The problem in the digital world was you're able to take a document and replicate it any number of times and have it absolutely identical to each other.

So to attack that particular problem, I, with my co-inventor who was the technologist, we leveraged the technology, PTI technology, which had been created for our weapons messaging system, US weapons messaging system. To that, we added not only the ability to create a message which you know was unchanged when it was created, from the time it was created, but also to separate one message from another, meaning one information object from another. And the technology included atomic time stamping and some other sort of onion layers around that information object to create an electronic original. So that was the foundation of the company.

We began to build out the technology, we worked with Fannie and Freddie, major lenders and major title companies. It took us a number of years and substantial investment of time and effort but by the year 2000 we did the first fully electronic mortgage closing. So that was the foundation of the eOriginal. It was really built around mortgage closing, but we found that need for that information object, that unique negotiable instrument wasn't only true in mortgage, but was also true in almost every financial services sector where you had collateralization or securitization.

So with GE Capital, we built a leasing application that was going to be taken out, platform was to be taken out into the market and then with Rabobank and a group out of Canada we built an international trade application as well. So that's how eOriginal got started and what our first products were.

Peter: Okay, so I want to just dig in a little bit into the weeds, if I can, and just talk about your actual technology. I appreciate that summary, but can we kind of get into just an example. Let's just say you've got an original promissory note, can you just explain exactly how...when someone is going and looking, doing an audit for example, how are they going to know that this electronic document is the original document that was signed. What is the technology like?

Steve: Very good question because the information object itself, even though you're able to pull it up and it'll have certain verifications indicia on it, you really need a record of what has occurred. So you have the information object, let's say it's the mortgage note. Along with that note, you have an audit trail, an audit log, and that has sort of a chain of evidence, chain of custody and it has the record of all the rights and privileges that apply to that document at a particular state in time.

In financial services, the instrument may have…well let's take the mortgage note, in a transaction...the rights and privileges at the time of origination and who gets to play on the document at the origination stage or the underwriting stage or the closing stage or the post-closing where you're doing audit or you're going out into a secondary market or you're going out to a custodian, you're providing it to an auditor or regulatory body....it's a multi-party, multi-state environment you have to manage and this document, this information object actually travels along that chain. So in order for you to be able to recognize that this is the original, you have to have the record of everything that occurred about that document throughout its life cycle.

So you have the document, but you also have the audit log. The audit log includes the information about who created it, who had permissions to create it. You can take it down as granular as who has viewed it, certainly everyone that signed it and when it was signed; you must have the ability to determine its integrity, meaning that it hasn't changed since the time it was executed. So it’s the document and that audit log that enables you to determine that it's an electronic original.

Peter: Okay, so we're not just talking about a PDF which is how most documents get thrown around the internet that are easily copied. Do you have a proprietary format for these documents?

Steve: What we have is a proprietary process because one of the things we discovered early on…and when you think when we started, we were using TIFF not PDF, but we do use PDF almost universally today. It's not the format of the information object; it is the process around it and how it is digitally sealed and controlled throughout its life cycle. So it could be a PDF, but it could be a video stream; it could be...you know, we have voice signature where you are actually able to capture a voice as an information object and embed that into a document along with an audit log.

So it's not so much the format of the document itself and maybe today we'll have the opportunity to talk a little bit where we see the transition from the world being document-centric in financial services to data-centric in financial services and eventually we may see what we think about as documentation taking on a different turn in the next few years.

Peter: Okay, okay, so when you've got the original documents, you said this could be an ordinary PDF that anyone can open, but you've got this...like a partner file, shall we say, it's got to be some kind of readable document that others can say, right, I see this PDF has been opened 27 times in the last 12 months and these are the people who opened them and that's the core to your technology, it sounds like, is it?

Steve; Yeah and also the PTI so every one that is utilizing our technology is provided with a digital certificate and so every instrument that has been included in the transaction, it may be seven or eight in an auto transaction, maybe 60 in a mortgage transaction, every one of those documents is digitally sealed with a digital certificate and there's a date and timestamp in it and other elements that help create that being the electronic original.

And because you can, at any time…that's sitting in the clear in the eOriginal system and then anytime that that instrument is rendered in any manner, whether it be printed or just rendered on a screen, there's a watermark which is embedded…digitally sealed into that information object as well. So you'll always know you're looking at a copy and you do not have the original; the rendering is not the original. But as you mentioned PDF, most documents today are rendered in

PDF and we enable them to be executed in PDF. Even our partners like DocuSign, they're executing documents in PDF. Once they're executed, the digital sealing is complete and then it can be put into eOriginal to be managed throughout its life cycle in a post execution environment as well.

Peter: Okay, okay, I get that. That's great. So let's just move on to more of the business side of it. You obviously started off in the mortgage industry and I know now, obviously now we're talking, you're in the marketplace lending industry, you guys have been around for a while, but before we get to that...so as you built your company you focused on the mortgage industry and then where else did you go?

Steve: You may remember, Peter, we had a tech bubble burst in the early 2000s.

Peter: Yes, indeed.

Steve: Most of the companies that were involved in digital signature or digital documentation, at that time, went away. Capital dried up, any new initiatives dried up, a company that was called Docutech went under, it came back as DocuSign under Tom Gonser and there is a bunch of the (inaudible) players today, but eOriginal was able to maintain itself through that. Actually, we transitioned from being a…we were in an ASP-hosted environment originally by EDS and then IBM and we took that opportunity to create an enterprise-class software which could be run in the hosting environment or behind the firewall.

So when we came out in 2002/2003, we found that the mortgage industry was not going to be rapid adopters of digital technology. We can have that discussion another day, but it certainly proved to be true. So we ended up moving into the automotive finance area and our first major customer in automotive finance was a company called Dealertrack. Dealertrack had created a credit application portal for financial institutions in the dealer so the F&I officer in the dealer would be able to go into this portal, sort of like a LendingTree, select the different lending opportunities for a particular customer for an auto loan.

They came to us because we had been successful in the mortgage industry to enable them to have the same process or similar process which we would apply to auto loans. And so the laws around negotiable instruments in the mortgage industry, they are a little bit different than they are in the automotive in terms of where they are…so in the automotive industry it's under the UCC 9105 for chattel paper. So that really became our core business for a number of years.

So we've supported not only Dealertrack, but RouteOne which is a competitor to DealerTrack. We then began to work with various financing sources, manufacturers, banks where they were doing direct lending like Bank of America, people like JD Byrider, Credit Acceptance Corporation. We provided the ability to do electronic leases from Tesla and so vehicle finance became a large part of our business during that time frame and it was then that we, in auto finance, that we did the first securitization of fully digital loan documents. That was done for Nissan Motor Acceptance Corporation in 2005. The primary rating agency at that time was Standard and Poor's.

Peter: Interesting.

Steve: So we had vehicle finance, we had equipment lease with people like Cisco and DLL and others; we began to move into solar energy with people like 12:50 BrightGrid and SunEdison, Kilowatt Financial, security monitoring with Vivint and Protection 1 and others. And then in general banking with consumers where people were executing consumer loans as well; Vacation Ownership where people have partial ownerships, whether it was deeded or under trust agreements being able to take them out in the market because what we found was that in almost every instance in financial services, there was a need for money… but that money was then somehow moved from the initial participants out into a secondary market, either through collaterization or securitization.

Peter: Right, okay. So it sounds like you've done quite a lot of different verticals over the years, so when did marketplace lending first get on your radar?

Steve: Marketplace lending is...we attempt to follow, I can't say we are really wonderful at it. We certainly don't have a presence like yourself, but we tend to follow any of the developing technologies in digital delivery of financial services. So the first article that I saw was in BusinessWeek online in 2006 and it was about Prosper Marketplace is the eBay of loans.

Peter: Right.

Steve: And at that time, we were working with eBay with the idea of being able to do online auto loans so I was very interested in what is in Prosper, what is the marketplace and how are they like eBay? So the article was about Prosper and Zopa in Britain. It was a completely new model for connecting borrowers and lenders, especially small borrowers and small lenders outside of traditional institutions, and I truly believed it was going to be the catalyst for a fundamental change in the availability of capital for small business and start-ups.

I thought it was a way to offer sort of regular people a higher yield in their money compared to what they got in deposits in CDs and for small businesses, of which I've had a few, really get away from the torture of getting small business loans to get a business up and going. In 2006, I thought it was going to come into the US like a firestorm in the next few years and once again, I was wrong.

Peter: (laughs) Yes, indeed. Well, you are very early on when it comes to your awareness of the sector. So then I guess the next question that follows on from that is when did you really get involved? Obviously it remained a retail-focused sector for many years, obviously not so anymore. When did you get involved?

Steve: Really in 2012, we were watching it, we were seeing the growth of it and we began to see some additional participants, but we really didn't see the volumes that would merit our investing in the sort of marketplace initiative for us, but in 2012 there was a top five investment bank that we were working with that was looking at investing in marketplace lenders and they suggested that we explore marketplace lending enabling their digital transactions to enable them to leverage and maintain the integrity and the auditability of digital transactions that we were enabling in the traditional financial services world.

So people, in order to be able to not only create, but manage, pool and securitize assets...it takes a lot of heavy lifting in terms of ensuring the verifiability, the auditability, the integrity of these documents so that when they go out into a secondary market, that the issuer's council are not going to be able to support them in terms of the legality, but also, more importantly, the rating agencies are not going to give them a lower rating or any differentiation in the rating when they're going out into the secondary market just because they are digital.

So that was what we accomplished, it was not a small accomplishment and this investor thought that they would feel a lot more comfortable moving into funding marketplace lenders if they had that same kind of visibility and integrity of the instruments that are digital. We have always believed in marketplace lending because a lot of what we've done is taking industries that are paper-based and doing that transformation to digital. That usually involves the hybrid process, it involves very difficult transformation and oftentimes, it initially costs more money because you're running both a paper environment and a digital environment until you reach a certain percentage of value. Whereas, in marketplace lending it began digital, it stayed digital and it's a real advantage for us to try to support it.

So the first real player that we began to work with was in January 2013 when we engaged with SoFi and SoFi was even a leader there; they were totally focused on customer experience. It was so wonderful to run into somebody in financial services that still had passion. That was not common in financial services here in this country. They were just really confident about what they were going to do.

They were our first customer really in marketplace lending and by the time we got into 2014, we had our second, our third and our fourth, but I personally didn't really understand how the marketplace lending model was going to permeate financial services at that time. And until we went to the ABS Conference in Vegas in 2014, and saw that the securitization market was really looking forward to participating in marketplace lending because it was new fields for them and we saw sort of a convergence there of the desire to bring marketplace lending into the securitization market and the need for marketplace lenders and investors to be able to get there.

Peter: Sure, yeah, okay. So you mentioned SoFi and I didn't actually know that they were your first client. That's fascinating, and it makes perfect sense. They really are a leader in many ways. Can you share others...who else are you working with today, are there others you can share names of?

Steve: Sure, most of them are public; Funding Circle, I mean, I think if we went through them sort of chronologically...SoFi and then Funding Circle and then Upstart, Financeit which is a very interesting company out of Canada and Payoff, Earnest, BorrowersFirst, ApplePie and most recently, Lending Club. So these are names I know that you're familiar with and we've partnered with other players like our relationship with Funding Circle was based on a relationship with Millennium Trust as the custodian.

Peter: Right.

Steve: Some of the players…our involvement with the origination platforms was really due to our relationship with the investors. The investors felt more comfortable if the originators were using eOriginal as the platform for creating these negotiable instruments in their particular space. So we've become a little bit symbiotic in terms of how we work with the platforms themselves. Since that time, there are dozens of other companies; Renovate America, Boat Financing, Credibility Capital, DealStruck, Mosaic, Kilowatt and others. So this has become a very important, not only part of our business, but part of our vision as where we see financial services is going.

Peter: Sure, so I want to just talk a little bit about Lending Club, I don't want to pick on them. I recently had Scott Sanborn on the podcast, but clearly they had an incident in May and I'm curious about...you've obviously been in this industry now for almost...coming up on four years, how did the incident in May, which we know in some ways was a data integrity issue, how has that impacted your business?

Steve: I think there's been two impacts. The first was when it happened. Everybody sort of just like...there was a lot of negative reaction, there was a concern about what this would do to the marketplace lending funding, but we did see almost immediately. In fact, the investors that were involved in that turned right around back and did invest in Lending Club, but for us in particular, it had a very positive impact. I think we're already seeing the positive impact it’s having in the marketplace lending world itself where people are regarding the need for transparency and for verification and knowing what you purchase is so crucial.

As someone you know pretty well, Mr. Brustkern [CEO of NSR Invest] noted that the best loan selection systems are only as reliable as the data that they receive so if you have inaccurate data representing the loans then the investors are likely to make imprudent decisions about what to buy. So, I think this was always the concern. The event at Lending Club sort of brought it to the fore.

The advantages is that marketplace lenders in fintech, they can adjust much more quickly than traditional lenders. So we are seeing that the marketplace lenders and the investors' side are beginning to look for the ability to have that verification and to have that transparency which is really only available in a digital world.

Peter: Right, so let's just talk about investors for a second because obviously you've got two sides of the transaction here if you're doing securitizations, you've got the platforms that originate the loans and then you’ve got the investors who want to purchase on either in a pooled transaction like a securitization and whole loans. Are you being approached by investors today to help them out as well? I mean, what are the differences, I guess, between the needs of investors and the needs of the platforms?

Steve: The needs of the investors are much simpler because they're not doing the creation. And so in fact we've talked about them here, they're the ones who sort of have the ball mitt, they're the ones that are receiving it and so they're very data-driven and the primary goal that they want to be able to achieve is knowing that that which they purchase is that which is being represented. So they're driving the originators to move to digital and they are spurring on the acceptance in the lending space. We have about 40 investors that have entered into various forms of what we call collateral control agreements with us and are also involved in some of the investors in the marketplace lending world that you'd know like Eaglewood. I think you know John Barlow who is one of our advisory board members.

Peter: Sure.

Steve: ….like Blue Elephant, [?] Finance and Route 66 and Jefferies and Tide Pool…the three of the top five institutional investors are involved with us and they really are beginning to drive what is going to be the...I'm sort of tired of the word transparency to be honest with you (Peter laughs), but they're the ones that are really going to drive the accountability and the verifiability of the assets. So what they're really looking for is that when they're doing the purchase, they get their data tape and they want to know that that which is represented in the data that's being delivered to them by the seller comports with the assets.

So one of the things that we have built and it wasn't for this because we had built this before the incident in May...this actually was something that had been suggested to us by one of the regulators....eOriginal has the ability not only to manage the information object which is the document and the audit log which I referred to, but we also have the ability to capture the data that was used to create that information object. Just like we have that audit trail, the audit log attached to that document, we can attach that data so we freeze that data in time that was used to create that document and then at a later date when someone receives that data that represents that information object of that document or that loan document, we're able to do that verification against that.

So we know that that which you're receiving is that which is being presented to you and this is very, very important because investors, in particular, if they are driven by anything...I would say it's by that quality, that knowledge, but it's also speed. The investors are looking to make sure that they're able to do these transactions quickly, they want to be able to lower their arbitrage costs; it will lower their speed for funding and one of the things that the digital format enables you to do is to create an almost programmatic process to getting your assets out to a secondary market.

Peter: Right.

Steve: So like SoFi who in 2014, did no securitizations and in 2015, did six or seven for a little under $2 billion and are actively working today and this is just one of the probably premier examples…they are able to do this in a rapid fashion and because they spend so much care in terms of setting up the processes to be able to done digitally and programmatically.

Peter: Right, so instead of taking two or three weeks to do this manually, which is I imagine how….and then doing it manually by taking a subset of a pool of loans...obviously you can do this in a matter of I imagine minutes or hours. Is that true?

Steve: That's correct. It really depends on the size of the pool.

Peter: Sure.

Steve: Because remember, one of the things that eOriginal does is that we verify the integrity of every single document in that pool and we verify the integrity of every signature in every digital seal at any time that these assets are transferred. So it's not quite like sending an e-mail...

Peter: (laughs) Right.

Steve: …but even if you were sending an e-mail, if you're sending half a billion dollars in assets, it's going to take some time, but it's within hours, it's not within, as you said in days. One of the, I think principal advantages is, again, if you take the care and you know who your partners are going to be in this financial transaction, you can automate a lot of the different steps in a securitization by leveraging technology.

Peter: Sure, so I want just talk about regulation for a second because this is obviously an issue that regulators...data integrity is something that they are very clued in on, they want this to be....this is an online process so they want to make sure that data integrity which is obvious in a paper-based environment is able to become just as obvious in a digital environment. I presume you're having conversations with regulators, I mean, what are you hearing from them about what you guys are doing?

Steve: The regulators are....there's a sort of conflicting challenges. So when you have the ability to do what we just described where you're able to monitor these transactions and basically you could monitor these transactions in real time, you know, the documents and the data and how they're moving within a transaction. And so you could actually do the verification of...are the representations in this document the same that was done in the disclosure. You could get alerts that if you're out of conformance, you can get alerts if you're out of your guidelines or if you're out of your compliance tolerances, either at the pool level or a transaction level or even a document level.

So the advantage of being able to do this all electronically in a digital format is that your risk and compliance people internally can have a much better view into what's happening in the transactions. The conflicting utilization of that benefit is that a regulator would love to have that access and is that appropriate or not is going to be an issue we're going to see coming forward in the next year or a couple of years. But from the regulators' perspective it is impossible for them to get the level of auditability and visibility unless you're in a digital environment so the regulators are looking for the same thing that the investors are looking for.

They're looking for real time visibility, they're looking for that verification, they're looking for transparency and they're looking for the ability to have automated notices and alerts when you're out of compliance or out of tolerance because there's no way that they can have the horsepower or the manpower to be able to monitor in any other manner. And the traditional audit capability of the regulator which occur after the events, regulators understand that this is not to the advantage of the consumer. To protect a consumer, the preference, the desire, and in some cases, the passion among the regulators is to make sure that the consumer is protected as the consumer goes through the transaction not just in a post-transaction environment when irregularities are reported.

Peter: Okay, sure. Well, we're almost out of time and there's much more to talk about. Before I let you go, I want to just get your perspective on whether or not you think the marketplace lending industry...I mean, obviously it has gone through a lot this year, do you think there's truly been like a mindset, a shift this year? I'd like to get that particular piece and then if it's really still not there, what else needs to happen in our industry to make sure that...you know, really this whole idea of transparency, we've said it many times, but it's obviously so critical in what we're doing here. So what are your thoughts on how it's changed and where we have still yet to go?

Steve: I think one of the essential changes is going to be the move into greater utilization of securitization. You remember when marketplace lending was really peer to peer and then to reduce their cost of capital, they moved into funds and insurance and hedge funds and then they had institutional lenders, but for marketplace lenders to really compete and to be able to keep their cost of capital down to keep their interest rates up, and their yield…there is such an incredible need for yield right now.

We're going to see a greater movement into the securitization market and we're seeing investors looking for that capability to invest in those types of securities. So I think the marketplace lenders are going to be looking at that process to get to the scalability. Marketplace lending is still a very small portion of our overall financial services revenue in the United States. The idea of getting consensus for more transparency, that's just going to come on its own. The ability to produce these truly authenticated documents to protect the marketplace participants, I think that's going to be coming.

But one of the things that we're seeing and Mr. Barlow raised a year ago is that we're seeing a convergence…when you look at the regulatory environment where the different marketplace lenders were standing on their own not so long ago. But as Congress and state regulators begin to move into the market and look at marketplace lenders, we're seeing marketplace lenders forming associations, beginning to lobby, beginning to look like a traditional financial institution, they're looking at the scalability that comes from the securitization markets. They're now having to deal with regulations, the issues around the banks and getting state licenses. The national license is for banks and how they're utilized by marketplace lenders.

The recent proposal that there will be a separate tool for marketplace lenders in terms of regulation. We're seeing marketplace lending move more into the issues and approach of traditional financial institutions and conversely, we're seeing the utilization of the tools of marketplace lending by traditional institutions. We saw it with Goldman Sachs and Marcus, we are seeing traditional institutions purchase marketplace lending or marketplace lending tools. They're looking at how they can, for the first time in many years, they're truly...without being lip service, they're truly focusing on the customer experience in large banks. So I think we're going to see much more rapidly than I had anticipated...we're going to start seeing that convergence of what was marketplace lending and traditional lenders really all moving to different types of digital lending environments and platforms.

Peter: Well, I completely agree. We're going to leave it there, but I really appreciate your coming on, Steve, it was fascinating to hear your story.

Steve: I appreciate the opportunity, thank you.

Peter: Okay, see you. Bye.

I just want to pick up on that last point that Steve made because it's been something that I've been thinking about for quite some time and that really is the convergence of the online lending, marketplace lending platforms with traditional lending which is still very much an offline process. I am very convinced that all lending is moving online, that I think you're going to find within five or ten years, it will be impossible to take out a loan in sort of an offline manner. Everything is going to be coming through online simply because it's a more efficient process and many other things that Steve mentioned.

For a company like his, when all lending is online and like he said it has taken mortgages a long time to get there, they may be the last holdouts but in consumer lending and all kinds of different verticals of lending, it's moving online, it's an unstoppable trend and companies like eOriginal are really going to be one of the major beneficiaries of that change.

Anyway on that note, I will sign off. I very much appreciate your listening and I'll catch you next time. Bye.

(closing music)