The New Disrupter: Blockchain & Smart Contracts

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Despite being the largest asset class in the world, the real estate industry lags in innovations related to efficiency and security. The advent of blockchain technology and smart contracts is poised to have an effect on the real estate industry on a scale that hasn't been seen since the internet. These effects will touch all aspects of the industry – including how we invest in, finance, construct, manage and exchange real estate assets – and the professions centered around it.

Blockchain, at its essence, is a simple concept: a transactional ledger. Cryptocurrencies like bitcoin are its most well known application, but the technology can be used to record and facilitate transactions involving virtually anything of value. What sets blockchain apart is its ability to provide a level of security and trustworthiness far greater than traditional transactional vehicles.

Specifically, blockchain is a decentralized, peer-to-peer network (which come in both public and private forms) where each participant interacts in a secure and immutable manner. Blockchain transactions are shared and verified among the participants using a protocol called a "consensus" and, once entered into the ledger, the transactions cannot be modified.

A smart contract is a "self-executing" electronic agreement recorded onto the blockchain. At its core, it is still a contract in that it includes the terms and conditions that outline or govern a relationship (or exchange of promises) between contracting parties, except the contractual provisions are encoded in the document using an algorithm. A smart contract streamlines the transaction process through automatic enforcement or execution of certain provisions upon the occurrence of a condition precedent. This "if X occurs, then Y happens" automation is what makes this tool efficient and revolutionary. Negotiation will still be a factor – not every term or condition of the contract is "coded" or automated, and standard provisions can and must remain – but once the substantive, functional provisions of the smart contract are agreed upon, the blockchain can take over and the deal can proceed without third-party intervention. Ultimately, this automation will increase security and trust, and minimize disputes.

Ohio has already taken the steps necessary to allow transactional parties to utilize this technology. On August 3, 2018, Governor Kasich signed into law Senate Bill 220, amending the Uniform Electronic Transactions Act (Ohio Rev. Code. 1306.01, et seq.) to allow for electronic records and electronic signatures to be "secured through blockchain technology." There is no doubt a growing trend – both in the public and private sectors – to adopt these technologies. Understanding how best to maximize the benefits of this technology could lead to greater efficiency and, thus, to greater profits. The following are just some of the ways in which these new technologies will impact and revolutionize our industry.

Tokenization

"Tokenization" refers to the process of representing an interest in a real estate asset with a blockchain-based token. While not real estate specific (the concept applies to anything of value), in this context it can be viewed as eliminating the traditional wealth barriers to entry into the real estate market for investors, particularly with the most lucrative projects and assets. These investments are essentially liquid, with investors able to resell their shares on the open market.

Projects are already being capitalized using tokens. A luxury $30 million Manhattan condo development was the first major asset in Manhattan to be tokenized on Ethereum. Inveniam Capital Partners has announced plans to tokenize $260 million in four private real estate and debt transactions, including a WeWork-occupied building in downtown Miami valued at $65.5 million, making it likely the largest piece of real estate to be financed this way to date. Real estate and finance company Elevated Returns has announced plans to tokenize $1 billion worth of property. Expect to see this trend continue.

Title insurance

Many jurisdictions are exploring adopting blockchain-based title registries. Not to say this isn't challenging – there are some 3,600 counties, towns and other jurisdictions that handle real property records in the United States – but about 1,700 such jurisdictions have already adopted some form of e-recording platform.

This is something the title industry is very interested in, as it has far-reaching implications with respect to title search, escrow and title insurance. Our paper-based system creates opportunities for errors and fraud, and a blockchain-based system would reduce these opportunities, as well as streamline the search and transfer process.

Property management

Utilizing blockchain-based smart contracts, property managers can automate and streamline the entire property management process. For example, a smart contract could automate tenant billing, payments to third-party vendors, cash flow management, equipment warranties and building maintenance, significantly reducing administrative costs and time through efficiencies. Adopting these technologies will be critical to compete in the marketplace.

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Construction industry

Smart contracts have the potential to be very impactful on the construction industry and how contractors conduct business. The automation of smart contracts is being utilized to streamline projects in a variety of contexts, including application for payment approval, substantial completion, actual completion, warranty walkthrough, acceptance, etc. Imagine, for example, being able to automate material delivery scheduling, using sensors to keep track of inventory. Those that are able to complete these types of administrative tasks electronically will increase efficiency in time, cost and use of resources (both human and physical).

There is no doubt that the use and applications of these technologies will only grow. For those of us who earn a living in this industry, it is imperative to both understand the wide range of applications, and have a working knowledge of the underlying technology in order to remain competitive. P

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