Giving Consumer Disclosures On-Line: Is ESIGN the Path to the Paperless Loan?

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Introduction

Enacted to facilitate electronic commerce, the Electronic Signatures in Global and National Commerce Act (ESIGN)[1] validates the use of electronic signatures and electronic agreements, but also imposes significant new requirements on electronic consumer transactions that trigger consumer disclosures in credit and other transactions. These new requirements apparently arose in part from a congressional concern about the increasing number of consumer electronic transactions and a desire to preserve the existing rights of consumers to receive certain information in writing.[2] ESIGN amounts to a congressional attempt to reconcile technological advances with consumer protection. Thus, ESIGN both enables and encumbers the developing world of electronic credit transactions. This Article examines the obligations that ESIGN imposes on a creditor offering true paperless credit transactions to consumers.

Growth of Electronic Commerce

The World Wide Web provides consumers with access to a seemingly unlimited amount of information and purchase options at the press of a key or the click of the mouse. Increasingly, consumers research and purchase software, housewares, electronics, airline tickets, furniture, motor vehicles, and other consumer-purpose

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1. 15 U.S.C. §§ 7001-7031 (2000).

2. Fed. Trade Comm'n, Bureau of Consumer Protection, 2001 Report to Congress: Electronic Signatures in Global and National Commerce Act: The Consumer Consent Provision in Section 101(c)(1)(C)(ii) (June 2001), *available at* http://www.ftc.gov/os/2001/06/esign7.htm [hereinafter 2001 Report].

goods "on-line."[3] The Census Bureau has estimated that U.S. e-commerce sales by retail establishments in the first quarter of 2001 rose thirty-three percent from the first quarter of 2000.[4] According to Forrester Research, U.S. on-line retail revenues hit approximately $38 billion in 2000. Forrester projects that North America will lead global e-commerce to $6.9 trillion by 2004.[5] The scope of the Internet and its ease of use have created a new type of commerce, one that permits a consumer to purchase almost any product, at almost anytime, from the consumer's home—and to do so on credit. Of course, to date, almost all consumer purchases made on-line have been consummated with credit cards. This Article first briefly discusses the requirements of ESIGN and then compares the ease of consummating a purchase on-line with a credit card as opposed to obtaining a paperless extension of credit to pay for the same purchase.[6]

REGULATION OF ELECTRONIC COMMERCE

ELECTRONIC SIGNATURES IN GLOBAL AND NATIONAL COMMERCE ACT

On June 30, 2000, Congress enacted ESIGN to facilitate the use of electronic records and signatures in interstate and foreign commerce by ensuring the validity, effect, and enforceability of signatures and contracts executed in an electronic form.[7] In its June 2001 Report to Congress, the Federal Trade Commission restated the intent of Congress that ESIGN should have a positive impact on the growth of e-commerce and should increase consumer confidence in the integrity and credibility of the emerging electronic marketplace.[8] ESIGN validates the use of electronic signatures, which may consist of any "electronic sound, symbol, or process " that is "attached to or logically associated with a contract or other record and executed or adopted by a person with the intent to sign the record."[9] It also gives electronic agreements and records[10] the same enforceability as those made on paper. These provisions removed doubts as to whether electronic transactions, such as paperless credit extensions, would be enforceable in court. ESIGN, however, also contains additional requirements that are imposed on electronic commerce whenever information is required to be given to the consumer in writing.

3. *See* CYBERATLAS, E-COMMERCE SHOWS SIGNS OF WAKING FROM SUMMER SLUMBER, *at* http://cyberatlas.internet.com/markets/retailing/print/0,,6061_871621,00.html.

4. Press Release, Department of Commerce, Rel. No. CB01-83: Estimated Quarterly U.S. Retail E-commerce Sales: 4th Quarter 1999-1st Quarter 2001 (May 16, 2001), *available at* http://www.census.gov/mrts/www/current.html; Press Release, Department of Commerce, Rel. No. CB01-28: Estimated Quarterly U.S. Retail E-commerce Sales: 4th Quarter 1999-4th Quarter 2000 (Feb. 16, 2001), *available at* http://www.census.gov/mrts/www/20004q.html.

5. *See* COMMERCE NET, WORLDWIDE INDUSTRY STATISTICS (2002), *at* http://www.commerce.net/research/stats/indust.html.

6. The ESIGN requirements related to the hypothetical credit sale transaction discussed in this Article would apply equally to a direct loan made over the Internet.

7. 15 U.S.C. § 7001(a) (2000).

8. 2001 REPORT, *supra* note 2, at ii.

9. 15 U.S.C. § 7006(5).

10. "Electronic record" is broadly defined to include "a contract or other record created, generated, sent, communicated, received, or stored by electronic means." *Id.* § 7006(4).

In a paperless credit transaction, some of the disclosures to which ESIGN would apply include an adverse action notice under the Equal Credit Opportunity Act (ECOA)[11] and cost of credit disclosures under the Truth in Lending Act (TILA).[12]

The consumer consent provisions of ESIGN were enacted to "ensure[ ] that consumers who choose to enter the world of electronic transactions will have no less access to information and protection than those who engage in traditional paper transactions."[13] Under ESIGN, information required by law to be in writing may be provided to the consumer electronically, if the consumer affirmatively consents to receive the information electronically and the business clearly and conspicuously discloses certain information to the consumer prior to obtaining the consumer's consent.[14] A consumer's consent to receive electronic records is only valid, however, if the consumer "consents electronically, or confirms his or her consent electronically, in a manner that reasonably demonstrates that the consumer can access information in the electronic form that will be used to provide the information that is the subject of the consent."[15]

A consumer may affirmatively consent to receive electronic disclosures only after being provided a clear and conspicuous statement informing the consumer: (i) of any right or option to have the disclosures made available on paper or in other non-electronic form;[16] (ii) of the right to withdraw consent to receive electronic disclosures and any conditions, consequences, or fees if consent is withdrawn;[17] and (iii) whether the consent applies only to a particular transaction or to identified categories of disclosures that will be provided or made available electronically during the course of the consumer's relationship with the business.[18] A merchant must provide the consumer with a description of how to withdraw consent to receive electronic disclosures[19] and the procedure for notifying the business of any change in the consumer's "electronic address" or other information needed to contact the consumer.[20] A merchant must also notify the consumer how the consumer may obtain a paper copy of the electronic disclosure and whether any fee will be charged for such a copy.[21]

In addition to the disclosures enumerated above, a business must communicate the hardware and software requirements for access to and retention of (e.g., downloading or printing) the electronic disclosures, before the consumer may consent

11. *Id.* § 1691(d)(2).
12. *Id.* §§ 1601-1666j.
13. 2001 REPORT, *supra* note 2, at 12.
14. 15 U.S.C. § 7001(c) (2000).
15. *Id.* § 7001(c)(1)(C)(ii). It is important to note that failure to obtain electronic consent or confirmation of consent by the consumer in accordance with the provisions of ESIGN does not, by itself, affect the effectiveness, validity, or enforceability of the contract subject to the consent.
16. *Id.* § 7001(c)(1)(B)(i).
17. *Id.* If a consumer withdraws consent, ESIGN provides that a business may terminate the parties' relationship. *Id.*
18. *Id.* § 7001(c)(1)(B)(ii).
19. *Id.* § 7001(c)(1)(B)(iii).
20. *Id.*
21. It is not clear that ESIGN requires a creditor to provide written copies of disclosures provided under the consumer disclosure provisions of the Act. *Id.* § 7001(c)(1)(B)(iv).

to receive electronic disclosures.[22] In order for the consent to be effective, the consumer must demonstrate electronically (either by providing electronic consent or confirming consent electronically) that the consumer can access information in the electronic form in which the disclosures will be provided.[23] Finally, if there is a change in the hardware or software requirements needed to access or retain electronic disclosures after a consumer consents to receive disclosures electronically, such that the consumer may not be able to access or retain future electronic disclosures, the consumer must receive a new description of the hardware and software requirements for access to or retention of the electronic disclosures and be given the right to withdraw his or her original consent.[24] A merchant may not impose a fee if the consumer withdraws consent due to an imminent change to hardware or software requirements.[25] After software or hardware changes, consent or confirmation of consent must be repeated successfully using the modified hardware or software.[26]

ESIGN requires the creditor to walk the consumer through the detailed information described above before a consumer may even receive the information required by substantive law, be it the ECOA, TILA, or any state disclosure law. The consumer then must perform the electronic consent or confirmation ritual.[27] Once this digital dance of information and confirmation has been performed, the consumer is permitted to receive his or her required disclosures. If the consumer remains on-line at this point,[28] the consumer has gained the hard-won right to purchase goods on credit, or to borrow money electronically, and is permitted to read and electronically execute a credit agreement or promissory note.

Thus, as noted, ESIGN both facilitates and hinders electronic commerce. Until ESIGN, creditors lacked guidance as to whether a federal or state disclosure law that required information to be provided in "writing" permitted that information to be presented electronically. Among the many unanswered questions were: If the law required the writing to be in a form that the consumer could keep, would an electronic download of that information suffice? Could a creditor rely on the fact that the consumer had hit the "print" button on the browser? Did it matter

22. *Id.* § 7001(c)(1)(C)(i).

23. *Id.* § 7001(c)(1)(C)(ii). If a consumer has to provide consent to receive electronic disclosures electronically, the consumer is required to have access to a computer, and possibly an email account, at the time consumer consent is obtained. This provision effectively prohibits transactions entered into electronically while the consumer is at the merchant's place of business or any written consent to receive electronic disclosures submitted in face-to-face transactions between merchants and consumers.

24. *Id.* § 7001(c)(1)(D)(i).

25. *Id.*

26. *Id.* § 7001(c)(1)(D)(ii).

27. *Id.* § 7001(c)(1)(C)(ii).

28. Paul Gallagher, president of Fidelity Service Company, the transfer agent for Fidelity's mutual fund business, testified at a Federal Trade Commission Workshop on ESIGN that enrollment in Fidelity's electronic disclosure program fell by 5,000 following the implementation of the ESIGN consumer consent requirements. Mr. Gallagher noted the possibility that the "consent piece really is in effect becoming more of a hurdle than really a benefit to consumers at the end of the day." FED. TRADE COMM'N, ESIGN PUBLIC WORKSHOP (meeting transcript) (Apr. 3, 2001), *available at* http://www.ftc.gov/bcp/workshops/esign/transcripts.htm.

whether there was paper in the printer? ESIGN has swept away these concerns as it "provides a framework for how businesses can comply with the underlying statutory or regulatory requirement to provide written information to consumers electronically—whether the information is a disclosure, a notice, or a statement of rights and obligations—within the context of a business-to-consumer transaction."[29] Nevertheless, ESIGN has added a new and different level of complexity to on-line borrowing.[30]

Arguably, ESIGN may provide consumers who are aware of its provisions with a confidence that they are protected by the law. Further, compliance with the consent requirements of ESIGN may reassure consumers about the legitimacy of an on-line merchant.[31] It is also possible that conformity with ESIGN will help to prevent deception and fraud,[32] although your authors predict that ESIGN will have no more of a chilling effect on the electronic charlatan than paper disclosures had on ending fraud in the last millennium.[33] On the other hand, compliance with the ESIGN consumer consent provisions will encumber electronic commerce by adding several new steps to each transaction, thereby causing confusion and—worse for the American consumer—delay, which may lead some customers to reject the use of electronic media.[34] In addition, the costs and uncertainties associated with implementing these consumer disclosure provisions continue to plague businesses engaged in e-commerce.[35] Moreover, these costs and other burdens almost certainly discourage new businesses from venturing into the realm of e-commerce. Other businesses, wanting to take advantage of the increased consumer presence on the Internet, may attempt to avoid the consumer consent provisions of ESIGN by initiating a transaction electronically, and then providing written disclosures to consumers via regular or express mail. But again, this reduces the utility of e-commerce.

THE PAPERLESS CREDIT TRANSACTION

The remainder of this Article will review two electronic transactions involving the on-line purchase of a home entertainment system. In the first scenario, Con-

29. 2001 REPORT, *supra* note 2, at 2.

30. The Federal Reserve Board issued interim revisions to its regulations implementing the Truth in Lending Act, the Equal Credit Opportunity Act, the Consumer Leasing Act, the Truth in Savings Act, and the Electronic Funds Transfer Act attempting to interpret the requirements of these statutes in light of ESIGN. These revisions were supposed to become mandatorily effective on October 1, 2001. If the mandatory effective date had not been lifted, the interim revisions would have created further complications for a creditor attempting to piece together a paperless credit transaction. For a more thorough discussion of these interim revisions, see James A. Huizinga et al., *Electronic Disclosures Under the Federal Reserve Board's Consumer Protection Regulations*, 57 BUS. LAW. 1197 2002.

31. 2001 Report, *supra* note 2, at 6.

32. *Id.* at 7.

33. Your authors believe that the answer to fraud and deception is enforcement, not disclosures. The purpose of most consumer disclosures has been to create educated consumers, not to stop fraud. *See* RALPH J. ROHNER & FREDERICK H. MILLER, TRUTH IN LENDING 3-34 (Robert A. Cook et al. eds., 2000) (discussing the origins of the Truth in Lending Act). The charlatan can often commit fraud and deception while providing perfectly accurate disclosures. Where that is not possible, charlatans have found that lies flow as readily on paper—or on screen—as they do from the tongues of rogues.

34. 2001 REPORT, *supra* note 2, at 9.

35. *Id.*

sumer A will purchase the home entertainment system using a credit card. Because there are no disclosures required to be in writing in this credit card transaction, the consumer consent provisions of ESIGN do not apply. In the second transaction, however, Consumer B will purchase the home entertainment system by signing, electronically, a retail installment sale agreement. This credit sale transaction, offered as a payment option at the merchant's Web site, will be applied for, accepted, and closed on the Internet in compliance with ESIGN.

Credit Card Transaction

Consumer A accesses a popular Web site with the intent to research and purchase a home entertainment system. After reviewing several types of home entertainment systems, Consumer A decides to purchase the featured Sony Rear Projection HDTV and a Bose Home Theater Surround Sound System for a total price of $4,798. Consumer A adds both products to his "shopping cart," accepts free shipping, and proceeds to checkout. At checkout, Consumer A reviews the items in his shopping cart and the total price. He has the opportunity to choose from several payment options, including credit card, electronic check, or obtaining credit directly from the on-line merchant in the form of a retail installment sale agreement. Choosing the credit card payment option, Consumer A submits his shipping information, credit card information, and billing address. Consumer A pauses while the transaction is processing, after which he receives a receipt and a notice that his purchase will ship within seven to ten business days. Within minutes of selecting his purchase, Consumer A closes his Internet browser and resumes work.

Credit Sale Transaction

Consumer B accesses a popular Web site with the intent to research and purchase a home entertainment system. After reviewing several types of home entertainment systems, Consumer B decides to purchase the featured Sony Rear Projection HDTV and a Bose Home Theater Surround Sound System for the total price of $4,798. Consumer B adds both products to her "shopping cart," accepts free shipping, and proceeds to checkout. At checkout, Consumer B reviews the items in her shopping cart and the total price. She also has the opportunity to choose from several payment options, including credit card, electronic check, or obtaining credit directly from the on-line merchant in the form of a retail installment sale agreement. Choosing the credit sale option, she is forwarded to a credit application form, which she is asked to complete with her personal and financial information. At the end of this credit application, the electronic waltz of ESIGN begins as Consumer B examines the following ESIGN disclosures. It is important to remember that these are only the disclosures that Consumer B must review in order to receive the substantive disclosures required by the Truth in Lending Act or the Equal Credit Opportunity Act:

PLEASE READ THE FOLLOWING TO COMPLETE THE APPLICATION PROCESS ON-LINE

By clicking the *Submit Application* button below, you are submitting your application for credit, and you are consenting to receive the following notices and disclosures electronically:

(a) Disclosures and notices detailing acceptance or denial of credit, including those required by the Equal Credit Opportunity Act;

(b) Cost of credit disclosures, including those required by the Truth in Lending Act.[36]

You may withdraw your consent to receive these electronic disclosures at any time prior to signing the Credit Sale Agreement by canceling this electronic transaction and selecting an alternative payment option. You may cancel this electronic application now by *clicking here*.[37]

You may obtain a paper copy of any disclosure or notice provided electronically to you by calling HudCo Home Entertainment, Inc. at 888-333-9999. You will be charged $2.50 for each copy requested.[38]

Before consenting to receive electronic disclosures, we will ask you to print or download a copy of this application to ensure that you can access the electronic disclosures we will provide to you.[39]

To print any notice or disclosure we provide to you electronically, you will need a printer available to your operating system with letter-sized paper or larger. To download any notice or disclosure, you will need an available storage medium such as a hard drive or floppy drive, with at least 2 KB available.[40]

Please print or download a copy of your credit application now to confirm that you can access and retain subsequent disclosures, which will be provided in the same format as this credit application.[41] If you CANNOT print or store your

36. 15 U.S.C. § 7001(c)(1)(B)(ii) (2000).

37. *Id.* § 7001(c)(1)(B)(i), (iii).

38. Again, it is not clear that ESIGN requires a creditor to provide written copies of disclosures provided under the consumer disclosure provisions of ESIGN. *See supra* note 21.

39. This requirement, together with the consumer's later confirmation that this process has been successful, provides a reasonable demonstration that the consumer is able to access the disclosures in the electronic format provided. 15 U.S.C. § 7001(c)(1)(C)(ii). This example assumes that subsequent disclosures will be provided in the same format as the credit application. If disclosures were to be provided in a different format, a separate reasonable demonstration involving that format would be required. *Id.* § 7001(c)(1)(D). Note that ESIGN only requires a consumer to reasonably demonstrate that they can "access" the disclosures, where other provisions in ESIGN speak of "access to and retention of" electronic disclosures and "access or retain" disclosures. *Compare id.* § 7001(c)(1)(C)(ii) *with id.* § 7001(c)(1)(C)(i) *and id.* § 7001(c)(1)(D). Thus, in this example it seems likely that the reasonable demonstration of a consumer's ability to retain the credit application by downloading or printing is overkill.

40. *Id.* § 7001(c)(1)(C)(i).

41. While it appears that ESIGN does not have any retention requirement, contradictory references to "retention" in ESIGN suggest that a conservative creditor should advise the consumer to print or download the application.

application properly or you do not wish to accept electronic notices and disclosures, please *click here* to select an alternative payment option.

By clicking the [*Submit Application*] button below, I understand that I am:

1. Submitting my application for credit to HudCo Home Entertainment, Inc.
2. Consenting to receive the disclosures and notices described above, electronically.
3. Confirming that I have successfully printed or downloaded my credit application.

[*SUBMIT APPLICATION*]

HudCo Home Entertainment, Inc. then reviews the application for credit. If Consumer B's application for credit is denied, Consumer B must receive an adverse action notice under the ECOA.[42] The ECOA, and its implementing regulation, Regulation B, provide that an adverse action notification must be in writing and thus the electronic delivery of such a notice is subject to ESIGN.[43]

Because Consumer B consented to receive credit approval or denial notices electronically in accordance with ESIGN, the adverse action notice could appear directly on Consumer B's computer screen within moments after the credit application is submitted. Consumer B is advised to print or download the adverse action notice. While not required at this point, the cautious creditor may add at the end of the adverse action notice the following admonition: "You should read this notice carefully and print or download a copy of this notice for your records. To print, click on the Print button on your browser. To download a copy, go to File/Save As." Then the transaction, while not entirely satisfactory from Consumer B's standpoint, has at least been conducted completely in accordance with ESIGN.

If Consumer B's application is accepted, the transaction may progress to the credit agreement. TILA and Regulation Z require the delivery of certain credit information, in writing, prior to the consummation of the credit transaction.[44] Such cost of credit disclosures are subject to the requirements of ESIGN.[45] Because Consumer B consented to receive cost of credit disclosures electronically in accordance with ESIGN, the creditor may provide the federal disclosures, and any additional state law credit disclosures, electronically on the computer screen. Upon receiving and reviewing the disclosures, Consumer B is advised to print or download the disclosures. While not required at this point, the cautious creditor may add at the end of the credit disclosures the following admonition: "You should read these disclosures carefully; they explain the cost of your purchase on credit. You should print or download a copy of these disclosures for your records. To print, click on the Print button on your browser. To download a copy, go to File/Save As."

42. 15 U.S.C. § 1691 (2000); 12 C.F.R. § 202.9 (2001).
43. 15 U.S.C. § 7001(c)(1).
44. *Id.* § 1601; 12 C.F.R. § 226.
45. 15 U.S.C. § 7001(c)(1).

Finally, all of the consumer disclosures are out of the way and Consumer B may now receive, and electronically sign, the credit sale agreement.[46] The credit sale agreement is then presented on the screen and Consumer B is asked to sign the agreement. ESIGN makes this last step easy and efficient. An electronic signature may be any electronic process, provided that the consumer understands the importance of his or her actions.[47] A creditor that permits a consumer to click an on-screen button to effectuate the consumer's signature may want to include a notice similar to the following immediately above the button: "By clicking on the 'I Accept' button below, you agree to the terms and conditions set forth in this Credit Sale Agreement. By clicking on the 'I Accept' button you are accepting this Credit Sale Agreement with your legally binding signature."

[*I ACCEPT*]

At this point in the transaction, Consumer B pauses for a moment while the transaction is processing, after which she receives a receipt and a notice that her purchase will ship within seven to ten business days. Finished, she closes her Internet browser and resumes work.

In both of our sample transactions, the consumers purchased the same home entertainment package on credit. The results are the same: both consumers are now legally obligated to pay $4,798 plus finance charges. The credit card transaction was almost instantaneous, but the paperless credit sale transaction was a lengthy process, complicated in large part by the inclusion of the consumer consent provisions required by ESIGN.

Conclusion

ESIGN has enabled a new age of paperless credit transactions by validating the use of electronic signatures and electronic agreements. The consumer consent provisions of ESIGN, however, are lengthy and cumbersome, adding a new level of electronic paperwork to an on-line transaction. Thus, while ESIGN makes it possible for on-line merchants to offer consumers new credit options, it may make it less likely that these new paperless credit transactions will replace the credit card as the primary currency of the Internet. It is more likely that the paperless credit transaction will be reserved as a tool to offer quick credit approval to those consumers who either do not have a credit card or who, for other reasons, do not wish to use a credit card to purchase goods on-line. Creditors attempting to encourage the use of on-line credit transactions may find it necessary to offer substantial incentives to consumers to compensate for the additional time and energy necessary in navigating the consumer-consent provisions of ESIGN.

46. In most credit sale transactions, the truth in lending disclosures and the credit sale agreement are combined into a single document. This, however, is not required unless the applicable state law contains a "single-document rule," and may not be preferable in an on-line transaction.

47. 15 U.S.C. § 7006(5).

In conclusion, while ESIGN promotes the availability of on-line credit transactions, its implementation probably ensures that credit cards will remain the primary currency of the Internet and thus poses burdens for those who wish to offer electronic credit. For now, ESIGN serves only as the foundation for, but not the path to, the paperless loan.