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BILL ANALYSIS

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House Bill 5537 (as reported without amendment)
Sponsor: Representative Andrew Richner
House Committee: Insurance and Financial Services
Senate Committee: Financial Services

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RATIONALE

In 1999, the Uniform Law Commissioners (ULC) promulgated the Uniform Electronic Transactions Act. According to the ULC, the Uniform Electronic Transactions Act (UETA) represents the first comprehensive effort to provide uniform rules to govern transactions in electronic commerce, which refers to the practice of doing business via computers and telephone or television cable lines. Since electronic transactions are conducted by the communication of digitized information from one person to another, they are inherently paperless. The legal enforceability of these transactions may be called into question, therefore, if a statute requires information or an agreement to be set forth in writing. The uniform Act was drafted in response to this concern, as well as concerns about the impact of electronic commerce on consumers. According to the ULC, "...the primary objective of this act is to establish the legal equivalence of electronic records and signatures with paper writings and manually-signed signatures, removing barriers to electronic commerce". The ULC also reports that 22 states have enacted UETA, and about a half-dozen others are considering it. It has been suggested that Michigan should adopt the Act, as well.

CONTENT

The bill would enact the "Uniform Electronic Transactions Act" to do the following:

- Provide for the legal effect of electronic records and electronic signatures.
- Prescribe criteria that would satisfy requirements of a law that information be in writing, a record be posted, a signature or record be verified, or a record be retained.
- Provide for the attribution of an electronic record or electronic signature to a person.
- Allow contracts to be formed by electronic agents (computer programs) in automated transactions.
- Establish rules that would apply if a change or

error in an electronic record occurred during transmission.

- Establish rules for the sending and receipt of electronic records.
- Specify the person who would have control of a "transferable record", and describe the rights of that person.
- Require the Department of Management and Budget to determine whether State departments would use electronic records and signatures.
- Specify that, in a criminal or civil proceeding, evidence of a record or signature could not be excluded solely because it was in electronic form.

In general, UETA would apply only to transactions in which the parties had agreed to conduct business electronically, and would not apply to most transactions subject to the Uniform Commercial Code. The Act would not require a record or signature to be created, communicated, or processed electronically. Provisions of UETA could be varied by agreement, unless otherwise prohibited.

Legal Effect of Electronic Record or Signature

A record or signature could not be denied legal effect or enforceability solely because it was in electronic form. A contract could not be denied legal effect or enforceability solely because an electronic record was used in its formation.

If a law required a record to be in writing, an electronic record would satisfy the law. If a law required a signature, an electronic signature would satisfy the law.

Definitions

The Act would define "record" as "information that is inscribed on a tangible medium or that is stored in an

electronic or other medium and is retrievable in perceivable form. "Electronic" would mean relating to technology having electrical, digital, magnetic, wireless, optical, electromagnetic, or similar capabilities.

"Electronic record" would mean a record created, generated, sent, communicated, received, or stored by electronic means. "Electronic signature" would mean an electronic sound, symbol, or process attached to or logically associated with a record and executed or adopted by a person with the intent to sign the record.

"Transaction" would mean an action or set of actions occurring between two or more people relating to the conduct of business, commercial, or governmental affairs.

Application & Construction of UETA

The Act would apply to electronic records and electronic signatures relating to a transaction, except to the extent that it was governed by either of the following:

- A law governing the creation and execution of wills, codicils, or testamentary trusts.
- The Uniform Commercial Code (UCC), except as provided below.

The Act would apply to a transaction to the extent it was governed by Section 1107 or 1206 or Article 2 or 2A of the UCC. (Section 1107 states that any claim or right arising out of an alleged breach can be discharged without consideration by a written waiver or renunciation signed and delivered by the aggrieved party. Under Section 1206, an unwritten contract for the sale of personal property generally is not enforceable beyond \$5,000. Article 2 of the UCC governs sales and applies to "transactions in goods". Article 2A governs leases of goods.)

The Act would apply to any electronic record or electronic signature created, generated, sent, communicated, received, or stored on or after UETA's effective date. A transaction subject to UETA also would be subject to other applicable substantive law.

The Act would apply only to transactions between parties who had each agreed to conduct transactions by electronic means. Whether parties had made this agreement would be determined from the context and surrounding circumstances, including the parties' conduct. A party who agreed to conduct a transaction by electronic means could refuse to conduct other transactions by electronic means; this right could not be waived by agreement.

Unless otherwise prohibited by UETA, a provision of

the Act could be varied by agreement. The Act would not require a record or signature to be created, generated, sent, communicated, received, stored, or otherwise processed or used by electronic means or in electronic form.

The Act would have to be construed and applied as follows:

- To electronic transactions consistent with other applicable law.
- To be consistent with reasonable practices concerning electronic transactions and with their continued expansion.
- To effectuate UETA's general purpose to make uniform the law with respect to electronic transactions among the states.

Writing or Posting Requirements

If parties had agreed to conduct a transaction by electronic means and a law required a person to provide, send, or deliver information in writing to another person, that requirement would be satisfied if the information were provided, sent, or delivered in an electronic record capable of retention by the recipient at the time of receipt. An electronic record would not be capable of retention by the recipient if the sender or its information processing system inhibited the recipient's ability to print or store the record.

If a law required a record to be posted or displayed in a certain manner, to be sent, communicated, or transmitted by a specified method, or to contain information that was formatted in a certain manner, all of the following rules would apply:

- The record would have to be posted or displayed in the manner specified by law.
- The record would have to be sent, communicated, or transmitted by the method specified by law (except as provided below regarding the U.S. mail).
- The record would have to contain the information formatted in the manner specified by law.

The requirements described above could be varied as follows:

- To the extent a law other than UETA that required information to be provided, sent, or delivered in writing allowed that requirement to be varied by agreement.
- To the extent a law other than UETA that required a record to be sent, communicated, or transmitted by regular U.S. mail allowed that requirement to be varied by agreement.

Verification Requirement

If a law required a signature or record to be notarized, acknowledged, verified, or made under oath, the requirement would be satisfied if the electronic signature of the person authorized to perform those acts, together with all other information required to be included by other applicable law, were attached to or logically associated with the signature or record.

Retention Requirement

If a law required a record to be retained, the requirement would be satisfied by the retention of an electronic record of the information if the record 1) accurately reflected the information set forth in the record after it was first generated in its final form as an electronic record or otherwise, and 2) remained accessible for later reference. A person could satisfy this requirement by using the services of another person if these criteria were satisfied. A requirement to retain a record in accordance with this provision would not apply to any information whose sole purpose was to enable the record to be sent, communicated, or received.

If a law required a record to be presented or retained in its original form, or provided consequences if the record were not presented or retained in its original form, that law would be satisfied by an electronic record retained in accordance with the retention requirement stated above. If a law required retention of a check, that requirement would be satisfied by the retention of an electronic record of the information on the front and back of the check in accordance with the above retention requirement.

A record retained as an electronic record in accordance with the retention requirement would satisfy a law requiring a person to retain a record for evidentiary, audit, or similar purposes, unless a law enacted after UETA's effective date specifically prohibited the use of an electronic record for the specified purpose.

These provisions would not preclude a governmental agency of this State from specifying additional requirements for the retention of a record subject to the agency's jurisdiction.

Attribution of Electronic Record or Signature

An electronic record or electronic signature would be attributable to a person if it were the act of the person. The act of the person could be shown in any manner, including a showing of the efficacy of any security procedure applied to determine the person to whom the record or signature was attributable. The effect of an electronic record or electronic signature attributable to a person under these provisions would be determined from the context and

surrounding circumstances at the time of its creation, execution, or adoption, including any agreements of the parties, and otherwise as provided by law.

Automated Transactions

"Automated transaction" would mean a transaction conducted or performed, in whole or in part, by electronic means or electronic records, in which the acts or records of one or both parties were not reviewed by an individual in the ordinary course in forming a contract, performing under an existing contract, or fulfilling an obligation required by the transaction. In an automated transaction, the rules described below would apply.

A contract could be formed by the interaction of electronic agents of the parties, even if no individual were aware of or reviewed the agents' actions or the resulting terms and agreements.

A contract could be formed by the interaction of an electronic agent and an individual, acting on his or her own behalf or for another person, including an interaction in which the individual performed actions that he or she was free to refuse to perform and that he or she knew or had reason to know would cause the electronic agent to complete the transaction or performance.

The terms of the contract would be determined by the substantive law applicable to it.

("Electronic agent" would mean a computer program or an electronic or other automated means used independently to initiate an action or respond to electronic records or performances in whole or in part, without review or action by an individual.)

Change or Error in Electronic Record

If a change or error in an electronic record occurred in a transmission between parties to a transaction, the rules described below would apply.

(1) If the parties had agreed to use a security procedure to detect changes or errors and only one party had conformed to the procedure, and the nonconforming party would have detected the change or error had that party also conformed, the conforming party could void the effect of the changed or erroneous record.

(2) In an automated transaction involving an individual, he or she could void the effect of an electronic record that resulted from an error made by the individual in dealing with the electronic agent of another person, if the agent did not provide for the prevention or correction of the error and, at the time the individual learned of the error, all of the following

applied:

- The individual promptly notified the other person of the error and that the individual did not intend to be bound by the electronic record received by the other person.
- The individual took reasonable steps to return to the other person or to destroy any consideration received as a result of the erroneous record.
- The individual had not used or received any benefit or value from any consideration received from the other person.

(3) If neither of the preceding rules applied, the error would have the same effect as provided by law.

Neither the second nor the third rule could be varied by agreement.

Sending & Receiving Electronic Record

Unless otherwise agreed between the sender and the recipient, an electronic record would be sent when it complied with all of the following:

- It was addressed properly or otherwise directed properly to an information processing system that the recipient used for the purpose of receiving electronic records or information of the type sent and from which the recipient was able to retrieve the electronic record.
- It was in a form capable of being processed by that system.
- The record entered an information processing system outside the control of the sender or of a person who sent the record on behalf of the sender, or entered a region of the system used by the recipient that was under the recipient's control.

Unless otherwise agreed between the sender and the recipient, an electronic record would be received when it 1) entered an information processing system that the recipient used for the purpose of receiving electronic records or information of the type sent and from which the recipient was able to retrieve the electronic record, and 2) was in a form capable of being processed by that system. This would apply even if the place the information processing system was located were different from the place the electronic record was considered to be received (as described below). An electronic record would be received under this rule even if no individual were aware of its receipt.

Unless otherwise expressly provided in the electronic record or agreed between the sender and the recipient, an electronic record would be considered to be sent from the sender's place of business and to be received at the recipient's place of business. For purposes of this provision, the following would apply:

- If the sender or recipient had more than one place of business, the place of business of that person would be the place having the closest relationship to the underlying transaction.
- If the sender or recipient did not have a place of business, the place of business would be the sender's or recipient's residence.

Receipt of an electronic acknowledgment from an information processing system described above (in the rule regarding receipt) would establish that a record was received but, by itself, would not establish that the content sent corresponded to the content received.

If a person were aware that an electronic record purportedly sent or purportedly received under the preceding rules were not actually sent or received, the legal effect of the sending or receipt would be determined by other applicable law. Except as permitted by the other law, these requirements could not be varied by agreement.

Transferable Records

As used in the following provisions, "transferable record" would mean an electronic record that would be a "note" under Sections 3101 to 3801 (Article 3) of the UCC, or a "document" under Sections 7101 to 7603 (Article 7) of the UCC, if the electronic record were in writing, and the issuer of the record had expressly agreed it was a transferable record. (Under Article 3, an instrument is a "note" if it is a promise; that is, a written undertaking to pay money signed by the person undertaking to pay. Under Article 7, a "document" is a document of title, which includes a bill of lading, dock warrant or receipt, warehouse receipt, or order for the delivery of goods, and any other document that in the regular course of business or financing is treated as adequately evidencing that the person in possession of it is entitled to receive, hold, and dispose of the document and the goods it conveys.)

A person would have control of a transferable record if a system employed for evidencing the transfer of interests in the record reliably established that person as the person to whom the record was issued or transferred. A system would satisfy this criterion, and a person would be considered to have control of a transferable record, if the record were created, stored, and assigned in a manner that all of the following would apply:

- There existed a single authoritative copy of the transferable record that was unique, identifiable, and (except as provided below) unalterable.
- The authoritative copy identified the person asserting control as either the person to whom the record was issued, or, if the authoritative copy indicated that the transferable record had been transferred, the person to whom the record was most recently transferred.
- The authoritative copy was communicated to and maintained by the person asserting control or its designated custodian.
- Copies or revisions that added or changed an identified assignee of the authoritative copy could be made only with the consent of the person asserting control.
- Each copy of the authoritative copy, and any copy of a copy, was readily identifiable as a copy that was not the authoritative copy.
- Any revision of the authoritative copy was readily identifiable as authorized or unauthorized.

Except as otherwise agreed, a person having control of a transferable record would be the holder, as defined in Section 1201 of the UCC, of the transferable record and would have the same rights and defenses as a holder of an equivalent record or writing under that section, including (if the applicable requirements under Section 1201 were satisfied) the rights and defenses of a holder in due course, a holder to which a negotiable document of title had been duly negotiated, or a purchaser. Delivery, possession, and indorsement would not be required to obtain or exercise any of the rights under these provisions. (Section 1201 of the UCC defines "holder", with respect to a negotiable instrument, as the person in possession if the instrument is payable to bearer or, in the case of an instrument payable to an identified person, if that person is in possession. With respect to a document of title, "holder" means the person in possession if the goods are deliverable to bearer or to the order of the person in possession.)

Except as otherwise agreed, an obligor under a transferable record would have the same rights and defenses as an equivalent obligor under equivalent records or writings under Section 1201 of the UCC.

If requested by a person against whom enforcement was sought, the person seeking to enforce the transferable record would have to provide reasonable proof that the person was in control of the record. Proof could include access to the authoritative copy of the record and related business records sufficient to review the terms of the record and to establish the identity of the person having control of it.

Governmental Agencies

The Department of Management and Budget (DMB) would have to determine for each department whether, and the extent to which, the department would create and retain electronic records and convert written records to electronic records. Subject to this requirement, the DMB would have to determine whether, and the extent to which, each State department would send and accept electronic records and electronic signatures to and from other persons and otherwise create, generate, communicate, store, process, use, and rely upon electronic records and signatures.

To the extent that a governmental agency used electronic records and electronic signatures, the DMB, giving due consideration to security, could specify any or all of the following:

- The manner and format in which the electronic records would have to be created, generated, sent, communicated, received, and stored, and the systems established for those purposes.
- If an electronic record were required to be signed by electronic means, the type of electronic signature required, the manner and format in which it was to be affixed to the record, and the identity of or criteria that had to be met by any third party used by a person filing a document.
- Control procedures and appropriate procedures to ensure adequate preservation, disposition, integrity, security, confidentiality, and auditability of electronic records.
- Any other required attributes for electronic records that were specified for corresponding nonelectronic records or reasonably necessary under the circumstances.

Except as otherwise provided by the DMB, UETA would not require a governmental agency or official of this State to use or permit the use of electronic records or electronic signatures.

The DMB could encourage and promote consistency and interoperability with similar standards adopted by other governmental agencies of this State and other states and the Federal government, and nongovernmental persons interacting with governmental agencies of this State. If appropriate, these standards could specify differing requirements from which governmental agencies and officials of this State could choose in implementing the most appropriate standard for a particular application.

("Governmental agency" would mean an executive, legislative, or judicial agency, department, board, commission, authority, institution, or instrumentality of the Federal, state, or local government.)

BACKGROUND

The National Conference of Commissioners on

Uniform State Laws (the Uniform Law Commission) is a nonprofit, unincorporated association, composed of state commissioners on uniform laws from each state, the District of Columbia, the Commonwealth of Puerto Rico, and the U.S. Virgin Islands. The purpose of the ULC is to study and review the law of the states in order to determine which areas should be uniform. Since its organization in 1892, the Conference has drafted more than 200 uniform laws, such as the Uniform Probate Code, the Uniform Child Custody Jurisdiction Act, the Uniform Anatomical Gift Act, and the Uniform Interstate Family Support Act. The uniform laws drafted by the ULC have no force until they are adopted by a state legislature.

According to the ULC, the Uniform Electronic Transactions Act "...was drafted to eliminate any doubt concerning the enforceability of electronic transactions, whether in the form of retail Internet transactions, electronic credit transactions, electronic data interchange, or e-mail usage. UETA is designed to put electronic transactions on a par with paper transactions."

After UETA was promulgated, President Clinton signed the Electronic Signatures in Global and National Commerce Act (E-Sign) on June 30, 2000. This Act will take effect on October 1, 2000. According to the chairperson of the ULC committee that drafted UETA, "Both acts validate the use of electronic records and signatures; they overlap significantly. Each statute provides that electronic contracts and signatures shall not be denied legal effect or enforceability because they are electronic. Nevertheless, the two acts are not identical, either in scope or substance" ("Federal Preemption and Electronic Commerce", by Patricia Brumfield Fry). This source further reports that states may modify, limit, or supercede the electronic contracting provisions of E-Sign under limited conditions. If a state has enacted UETA as approved and recommended by the ULC, the state law will govern.

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

This bill is virtually identical to the uniform Act promulgated by the Uniform Law Commission. By enacting UETA, Michigan would join the effort to overcome legal impediments to electronic commerce. As the Prefatory Note to UETA points out, "With the advent of electronic means of communication and information transfer, ...methods for doing business have evolved to take advantage of the speed, efficiencies, and cost benefits of electronic technologies. These developments have occurred in the face of existing legal barriers to the legal efficacy of records and documents which exist solely in electronic media... By establishing the equivalence of an electronic record of the information, the Uniform Electronic Transactions Act (UETA) removes these barriers without affecting the underlying legal rules and requirements." The Act sets forth a clear framework for covered transactions, and avoids unwarranted surprises for parties dealing in this relatively new medium.

The uniform Act is procedural, rather than substantive. It ensures that electronic transactions are as enforceable as paper transactions that are

signed manually, but without changing any of the substantive rules of law that apply. The Act specifically states that a transaction subject to UETA also is subject to other applicable substantive law. In addition, with a few exceptions, the parties' agreement will control. Furthermore, UETA does not require anyone to use electronic transactions or rely on electronic records and signatures. Both parties to a transaction must agree to conduct business electronically, and even if they do agree regarding one transaction, a party may refuse to continue doing business electronically.

Electronic commerce has skyrocketed in recent years, and is likely to continue to grow with or without uniform rules. Having the rules in place, however, will ensure the legal effect and enforceability of electronic transactions, standardize the parties' expectations and responsibilities, and protect consumers. Since legal requirements for paper copies and manual signatures can delay transactions and increase costs, promoting electronic commerce will help to promote commerce overall.

Opposing Argument

Some people believe that states should exempt consumer protection statutes from the scope of UETA. These statutes often require that information be in writing, or that a consumer separately sign or initial a particular provision of an agreement, to ensure that he or she is aware of it. Other consumer protection statutes may require that certain information be presented in a particular manner or format. In addition, UETA does not require disclosures of the types of needed hardware and software, how a person may request a paper copy, or how to withdraw consent to transact business electronically. Although a parties' consent is required, it may be inferred from conduct. Also, unlike E-Sign, UETA does not exempt certain consumer notices, such as a notice of foreclosure, termination of insurance benefits, or product recalls. According to the Consumers Union, states that enact UETA should enact exemptions that match the Federal exemptions. The Consumers Union also suggests that, to avoid litigation over the applicability of Federal consumer protections, a state that enacts UETA after the effective date of E-Sign should include language stating that nothing in the state law is intended to limit, modify, or supercede requirements of E-Sign.

Response: The uniform Act preserves consumer protections in a number of ways. For example, if a law requires information to be delivered in writing, it must be in an electronic record that is capable of being retained by the recipient. If a law requires a separate signature or initials, UETA does not allow that requirement to be avoided; it simply allows the signature or initials to be electronic. Also, if a law requires a record to be posted, displayed, or

formatted in a certain manner, that requirement must be met. In addition, UETA does not disturb bodies of substantive law that protect against conduct such as unconscionability, fraud, and duress. According to UETA's Prefatory Note, "The preservation of existing safeguards, together with the ability to opt out of the electronic medium entirely, demonstrate the lack of any need generally to exclude consumer protection laws from the operation of this Act... Consumers and others will not be well served by restrictions which preclude the employment of electronic technologies sought and desired by consumers."

Legislative Analyst: S. Lowe

FISCAL IMPACT

Participation in electronic transactions would be voluntary; thus, the costs or savings are indeterminate. By using a third party intermediary, the Department of Management and Budget does not expect that State departments would incur significant technology investment costs if they chose to conduct electronic transactions. The savings would depend upon the extent to which departments would conduct electronic transactions. There could be savings for both the State and local governmental units in the form of reduced costs for application processing and record storage.

Fiscal Analyst: J. Runnels

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.