

## E-Sign Act

**15 U.S.C. § 7001 : US Code - Section 7001:** General rule of validity

(a) In general

Notwithstanding any statute, regulation, or other rule of law (other than this subchapter and subchapter II of this chapter), with respect to any transaction in or affecting interstate or...

(1) a signature, contract, or other record relating to such transaction may not be denied legal effect, validity, or...

**15 U.S.C. § 7003 : US Code - Section 7003:** *Specific exceptions*

(a) (3) *the Uniform Commercial Code, as in effect in any State, other than sections 1-107 and 1-206 and Articles 2 and 2A.*

## UETA

### UETA - SECTION 3. SCOPE.

(a) Except as otherwise provided in subsection (b), this [Act] applies to electronic records and electronic signatures relating to a transaction.

(b) *This [Act] does not apply to a transaction to the extent it is governed by:*

(2) *[The Uniform Commercial Code other than Sections 1-107 and 1-206, Article 2, and Article 2A.*

## Electronic Promissory Notes Electronic Security Instruments

A Promissory Note can either be a Negotiable Instrument or Non-Negotiable Instrument. E-Sign and UETA both exclude Negotiable Instruments governed by UCC Article 3.

The Security Instrument securing the Negotiable Instrument is governed by UCC Article 9 which is also listed as excluded under E-Sign and UETA.

The process of converting a paper negotiable instrument into an electronic negotiable instrument lacks basic laws to support its existence. Same is true for an electronically created Negotiable Instrument. (Henceforth Electronic Promissory Note or as MERS refers, "E-Notes")

Common practice involves MERS being named as Nominee for a lender and lender assigns on the Security Instrument in public records and to remain as such while the Electronic Negotiable Instrument is conveyed through multiple parties to be offered as collateral to a Secondary Market offering.

Two facts emerge from these actions; Investors that purchase Certificates backed by Electronic Promissory Notes as collateral have in fact purchased a Certificate in which the Electronic Promissory Note's do not lawfully exist.

The second fact is the Security Instrument that once secured the Original Paper Note at the conception of the indebtedness has been rendered nullity by actions of the lenders and therefore even if the Electronic Negotiable Instrument did exist, a Null Security Instrument has been offered up as part of the Collateral purchased by Investors.

**TEXAS**  
**PROPERTY CODE**

**CHAPTER 13**  
**EFFECTS OF RECORDING**

**§ 13.001**

**VALIDITY OF UNRECORDED INSTRUMENT**

*(a) A conveyance of real property or an interest in real property or a mortgage or deed of trust is void as to a creditor or to a subsequent purchaser for a valuable consideration without notice unless the instrument has been acknowledged, sworn to, or proved and filed for record as required by law.*

**TEXAS LOCAL**  
**GOVERNMENT CODE**

**CHAPTER 192**

**INSTRUMENTS TO BE RECORDED**  
**BY COUNTIES**

**§ 192.001**

**GENERAL ITEMS**

*The county clerk shall record each deed, mortgage, or other instrument that is required or permitted by law to be recorded.*

**TEXAS LOCAL**  
**GOVERNMENT CODE**

**CHAPTER 192**

**INSTRUMENTS TO BE RECORDED**  
**BY COUNTIES**

**§ 192.007**

**RECORDS OF RELEASES AND OTHER**  
**ACTIONS**

*(a) To release, transfer, assign, or take another action relating to an instrument that is filed, registered, or recorded in the office of the county clerk, a person must file, register, or record another instrument relating to the action in the same manner as the original instrument was required to be filed, registered, or recorded.*



Texas - The Lone Star State

## Federal Reserve Bank

### New York

*"From: [ucclaw-l-bounces@lists.washlaw.edu](mailto:ucclaw-l-bounces@lists.washlaw.edu)  
On Behalf Of [Joseph.Sommer@ny.frb.org](mailto:Joseph.Sommer@ny.frb.org)  
Sent: Friday, March 26, 2010 11:15 AM  
To: xxx-xxx-xxx  
Subject: Re: [Ucclaw-l] Electronic Promissory Notes*

*If I were confronted with an "electronic promissory note", I would walk very slowly away and break into a run as soon as I can. They are a logical impossibility, along with electronic chattel paper and UCC 7 electronic warehouse receipts.*

*The word "electronic" is miserably defined in all the statutes. But we all kinda sorta know what it means: something in a computer, rather than in some more fixed medium. Of course, a computer is made of matter and energy, just like a slip of paper or the side of a cow. So it must mean something special to be "in a computer."*

*And it does! Most records are stably associated with a particular agglomeration of matter which--if it is not realty--can be physically transferred from one person to another. This includes paper, cows, and DVDs. If the piece of paper or Old Bossy or the DVD is uniquely distinguishable from any other piece of paper or cow or DVD that bears the same data structure, we have the basis for a system of negotiability.*

*However, computer records are not stably associated with any particular piece of matter. Instead, they are stably associated with a system, which contains many pieces of matter amongst which the record may be sitting, at any given moment. Or the record could be sitting in 12 places in the system; it makes no difference. You don't need a unique piece of matter to uniquely identify an obligation--there is no unique matter (or energy) associated with the record. You just need an authoritative registry.*

*Hence the logical impossibility of an electronic promissory note. "Promissory note" means unique piece of matter. "Electronic" means that there is no unique piece of matter, and we're dealing with authoritative registries.*

*UCC 8 gets this right. It has two property systems that rely on unique pieces of matter (registered and unregistered certificates), and two systems that rely on authoritative registries (transfer agents and securities intermediaries.) The cotton warehouse system gets this right, and talks in great detail about authoritative registries. UCC 7, 9 and UETA screwed up. They are bad law—literally incomprehensibly bad law.*

*The courts will probably eventually define 7, 9, and UETA into registry systems of some kind. But until then, I would treat electronic negotiability systems as if they were rabid cows."*

***“To: Jennifer J. Johnson, Secretary  
Board of Governors  
Federal Reserve System***

*Mortgage Electronic Registration Systems, Inc. is a wholly-owned subsidiary of MERSCORP, Inc. which serves as the mortgagee or beneficiary of record in the local land records for loans registered on the MERS® System. As mortgagee or beneficiary, it holds mortgage liens on behalf of promissory note owners...*

*As of the date of this comment and request letter, more than 63 million residential mortgage loans are registered on the MERS System...*

*We request that the Board of Governors consider broadening the current definition of “the date of transfer” to provide alternative dates that would be included in the “the date of transfer” definition, so that definition is not restricted to be only “the date of acquisition recognized in the books and records of the covered person.” There is evidence that there are other dates that can be treated as the “date of transfer.” For example, the current process established and utilized by Members who participate in the MERS® InvestorID program is to identify “the date of transfer” as the seller’s closing date. Mechanically, once the seller enters the date of transfer, recognized as the seller’s closing date, on the MERS® System and the purchaser confirms this transaction, the MERS® System generates the disclosure notices to consumers...*

[j.mcguire@swbell.net](mailto:j.mcguire@swbell.net)

*Allowing Members to continue operating under the existing MERS® InvestorID program which captures the seller’s closing date would quickly and efficiently maximize industry compliance with the Interim Final Rule.”*

### **Uniform Commercial Code – Article 3**

#### **§ 3-201. NEGOTIATION**

(a) "Negotiation" means a transfer of possession, whether voluntary or involuntary, of an instrument by a person other than the issuer to a person who thereby becomes its holder.

(b) Except for negotiation by a remitter, if an instrument is payable to an identified person, negotiation requires transfer of possession of the instrument and its indorsement by the holder. If an instrument is payable to bearer, it may be negotiated by transfer of possession alone.

#### **§ 3-203. TRANSFER OF INSTRUMENT; RIGHTS ACQUIRED BY TRANSFER**

(a) An instrument is transferred when it is delivered by a person other than its issuer for the purpose of giving to the person receiving delivery the right to enforce the instrument.

(b) Transfer of an instrument, whether or not the transfer is a negotiation, vests in the transferee any right of the transferor to enforce the instrument, including any right as a holder in due course, but the transferee cannot acquire rights of a holder in due course by a transfer, directly or indirectly, from a holder in due course if the transferee engaged in fraud or illegality affecting the instrument.

(c) Unless otherwise agreed, if an instrument is transferred for value and the transferee does not become a holder because of lack of indorsement by the transferor, the transferee has a specifically enforceable right to the unqualified indorsement of the transferor, but negotiation of the instrument does not occur until the indorsement is made.

(d) If a transferor purports to transfer less than the entire instrument, negotiation of the instrument does not occur. The transferee obtains no rights under this Article and has only the rights of a partial assignee.

*“The Federal Reserve Board today named eight new members to its Consumer Advisory Council to replace members whose terms have expired, and designated a new Chairman and Vice Chairman of the Council for 1997.”*



Seal of the United States Federal Reserve System

The symbol is not to convey the impression that the author is a banking association, firm or partnership or a member of the Federal Reserve System (per [18 U.S.C § 709](#)).

*“Paul E. Mullings”*

*“McLean, Virginia”*

*“Mr. Mullings is President and CEO of the Mortgage Electronic Registration System, Inc. (MERS), established in February 1996. MERS is a national registration system that tracks mortgage rights for the benefit of consumers and the real estate finance industry. The idea was conceived by a technology committee of the Mortgage Bankers Association of America (MBA). Mr. Mullings served as a member of the MBA's Board of Governors from 1995 to 1996, and is a past vice-chairman of its fair lending committee. He currently serves on the MBA's legislative committee. Previously, Mr. Mullings was President and CEO of First Interstate Bank's Residential Mortgage Company, where he was responsible for mortgage origination, servicing, and secondary marketing for thirteen western states. He has served on Fannie Mae's National Advisory Council. In 1992 he was named "Outstanding Banker of the Year" by the Los Angeles Urban Bankers.”*

“Ms. Jennifer J. Johnson  
Secretary  
Board of Governors of the Federal  
Reserve System



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### Covered Person

Section 226.39 (a)(1) defines a "covered person" as:

"a person...that becomes the owner of an existing mortgage loan by acquiring legal title to the debt obligation, whether through a purchase, assignment, or other transfer, and who acquires more than one mortgage loan in any twelve-month period. For purposes of this section, a servicer of a mortgage loan shall not be treated as the owner of the obligation if the servicer holds title to the loan or it is assigned to the servicer solely for the administrative convenience of the servicer in servicing the obligation." 12 C.F.R. §226.39(a)(1). 74 Fed. Reg. 60151 (November 20, 2009)

### Nominees:

MBA seeks confirmation that the definition of "covered person" does not include "nominees" who take assignment of a mortgage on behalf of the party with legal title. Specifically, we seek confirmation that the Mortgage Electronic Registration System (MERS) as "nominee" for the owner or assignee of the mortgage would not be a "covered person" because it does not own the mortgages.

### Recording Location

The Board correctly states that transfers of ownership of the debt are almost never recorded because ownership of the debt is perfected through possession....

Since most transfers of the debt are not recorded....

John A. Courson  
President and Chief Executive Officer”

### *Author Comment:*

*Perfection of the security instrument to allow the indebtedness to be “Secured” governed by Article 9 and the laws of local jurisdiction.*

*Perfection/Non-Perfection as to Priority between subsequent purchasers is governed by Article 9.*

**“MERS**

***Designed to track and identify  
electronic promissory notes”***

*Electronic registry for tracking  
servicing rights and beneficial  
ownership interests in mortgage loans.*

***Mortgagee***

*MERS is the mortgagee in a nominee  
capacity for the beneficial owner of a  
mortgage loan in the land records.*

***Registration vs. Recording***

*MERS is not a system of legal record  
nor a replacement for the public land  
records. Mortgages must be recorded  
in the county land records.*

*MERS is a tracking system. No  
interests are transferred on the  
MERS® System, only tracked.*

*MERS executes documents through  
Certifying Officers who are employees  
of the members.*

***Mortgage Electronic Registration  
Systems, Inc. (“MERS”)***

*A bankruptcy-remote subsidiary of  
MERSCORP, Inc. whose sole purpose  
is to serve as mortgagee in the land  
records for loans registered on the  
MERS® System.*

***MERS as Original Mortgagee  
 (“MOM”)***

*Use Deeds of Trust or Mortgages with  
MERS as Original Beneficiary or  
Mortgagee using standard language  
approved by Fannie Mae, Freddie  
Mac, FHA and VA.*

***Assignment to MERS***

*Use an assignment to MERS for an  
existing non-MOM mortgage.”*

*Borrower mortgages, grants and  
conveys the Property to MERS.*

*If Lender executes the lien release  
instead of MERS, it will cloud title.”*

# Legal Framework

## Uniform eNote Clause

### **Borrower's agreement to the electronic transaction**

*"I expressly state that I have signed this electronically created Note (the "Electronic Note") using an Electronic Signature..."*

### **eNote Registry**

*"the identity of the Note Holder and any person to whom this Electronic Note is later transferred will be recorded in a registry maintained by [MERS]..."*

### **eNote Registry**

*"The current identity of the Note Holder and the location of the authoritative copy..., will be available from the Note Holder or Loan Servicer, as applicable."*

*"The only copy of this Electronic Note that is the authoritative copy is the copy that is within the control of the person identified as the Note Holder in the...Registry (or that person's designee)."*

## Fannie Mae's Requirements

### **eMortgage Guide**

*Available on eFannieMae.com (search on "eMortgage")*

### **Lender readiness process**

#### **Contract**

*Amendment to Master Agreement that incorporates eMortgage Guide*

#### **Documents other than note**

*Selling Guide permits most documents to be created electronically or to be imaged*

#### **Key Points**

- *Uniform eNote*
- *eSignatures*
- *Borrower Attribution*
- *Registration on MERS within 1 Day of eClosing*

## Practical Considerations

*Enforceability*

*Modifications*

*Foreclosure*

*Payoffs*

*"*



## “Servicing Guide Part VIII

## Non-Judicial Foreclosure

### Section 105

### Conduct of Foreclosure Proceedings

#### Judicial Foreclosure

*Effective immediately, MERS must not be named as a plaintiff in any judicial action filed to foreclose on a mortgage owned or securitized by Fannie Mae. MERS is the mortgagee of record when either a mortgage names MERS as the original mortgagee and is recorded in the applicable land records, or a completed and recorded assignment names MERS as the mortgage assignee. Therefore, in most jurisdictions, the servicer will need to prepare a mortgage assignment from MERS to the servicer, and then bring the foreclosure in its own name, unless the Servicing Guide requires that the foreclosure be brought in the name of Fannie Mae. In that event, the assignment will need to be from MERS to Fannie Mae.*

*The assignment from MERS to the servicer should be in recordable form (e.g., executed and notarized) and, in some jurisdictions, it will need to be recorded. In other jurisdictions, it may be held by the servicer or the foreclosure attorney without being recorded. Because the assignment will be completed before the foreclosure begins (and recorded if required by applicable law), MERS will no longer be the mortgagee. Therefore, MERS should not be named as a plaintiff in the foreclosure complaint or other judicial filings.*

*In any non-judicial foreclosure proceedings, the servicer has the option of either assigning the mortgage from MERS to the servicer (in accordance with the process outlined above for judicial foreclosures), or proceeding with the foreclosure with MERS as the mortgagee of record.*

*If MERS remains the mortgagee of record, the servicer must ensure that the foreclosure attorney or trustee accurately identifies the status of MERS. MERS may never be identified as the “owner” or the “holder” of the Note or Security Instrument being foreclosed. MERS may be identified as the beneficiary of the deed of trust being foreclosed, but only if MERS is also identified as a nominee for the servicer, or as a nominee for Fannie Mae if our Servicing Guide requires the foreclosure to be brought in Fannie Mae’s name.*

*The servicer should consult with its foreclosure attorney or trustee to determine the specific legal requirements of each jurisdiction in which it conducts non-judicial foreclosures of mortgages in which MERS is the mortgagee of record. Further, if MERS remains the mortgagee of record, then the servicer should also consult with its foreclosure attorney or trustee to determine the appropriate manner for identifying MERS’ interest in the subject mortgage.*

*In any event, if an assignment has been recorded from MERS to either the servicer or Fannie Mae, and the borrower reinstates the mortgage prior to completion of the foreclosure proceedings, the servicer may choose to re-assign the mortgage to MERS and re-register the mortgage with MERS. Any such action will be at the discretion and expense of the servicer.”*

**“SECTION 2.01. Conveyance of Mortgage Loans.**

(a) *Each Seller, concurrently with the execution and delivery hereof, hereby sells, transfers, assigns, sets over and otherwise conveys to the Depositor, without recourse, all its respective right, title and interest in and to the related Initial Mortgage Loans*

(b) *Immediately upon the conveyance of the Initial Mortgage Loans referred to in clause (a), the Depositor sells, transfers, assigns, sets over and otherwise conveys to the Trustee for the benefit of the Certificateholders, without recourse, all the right, title and interest of the Depositor in and to the Trust Fund together with the Depositor's right to require each Seller to cure any breach of a representation or warranty made herein by such Seller or to repurchase or substitute for any affected Mortgage Loan in accordance herewith.*

(c) *In connection with the transfer and assignment set forth in clause (b) above, the Depositor has delivered or caused to be delivered to the Trustee (or, in the case of the Delay Delivery Mortgage Loans that are Initial Mortgage Loans, will deliver or cause to be delivered to the Trustee within thirty (30) days following the Closing Date and in the case of the Delay Delivery Mortgage Loans that are Supplemental Mortgage Loans, will deliver or cause to be delivered to the Trustee within twenty (20) days following the applicable Supplemental Transfer Date) for the benefit of the Certificateholders the following documents or instruments with respect to each Mortgage Loan so assigned: ...*

*(A) the original Mortgage Note endorsed by manual or facsimile signature in blank in the following form: "Pay to the order of \_\_\_\_\_ without recourse," with all intervening endorsements showing a complete chain of endorsement from the originator to the Person endorsing the Mortgage Note (each such endorsement being sufficient to transfer all right, title and interest of the party so endorsing, as note holder or assignee thereof, in and to that Mortgage Note); or*

*(B) with respect to any Lost Mortgage Note, a lost note affidavit from Countrywide stating that the original Mortgage Note was lost or destroyed, together with a copy of such Mortgage Note;*

*(ii) except as provided below and for each Mortgage Loan that is not a MERS Mortgage Loan, the original recorded Mortgage or a copy of such Mortgage certified by Countrywide as being a true and complete copy of the Mortgage (or, in the case of a Mortgage for which the related Mortgaged Property is located in the Commonwealth of Puerto Rico, a true copy of the Mortgage certified as such by the applicable notary) and*

*in the case of each MERS Mortgage Loan, the original Mortgage, noting the presence of the MIN of the Mortgage Loans and either language indicating that the Mortgage Loan is a MOM Loan if the Mortgage Loan is a MOM Loan or if the Mortgage Loan was not a MOM Loan at origination, the original Mortgage and the assignment thereof to MERS, with evidence of recording indicated thereon, or a copy of the Mortgage certified by the public recording office in which such Mortgage has been recorded;*

*(iii) in the case of each Mortgage Loan that is not a MERS Mortgage Loan, a duly executed assignment of the Mortgage (which may be included in a blanket assignment or assignments), together with, except as provided below, all interim recorded assignments of such mortgage (each such assignment, when duly and validly completed, to be in recordable form and sufficient to effect the assignment of and transfer to the assignee thereof, under the Mortgage to which the assignment relates); provided that, if the related Mortgage has not been returned from the applicable public recording office, such assignment of the Mortgage may exclude the information to be provided by the recording office; provided, further, that such assignment of Mortgage need not be delivered in the case of a Mortgage for which the related Mortgaged Property is located in the Commonwealth of Puerto Rico;...*

*(F) The executed UCC-3 financing statements or other appropriate UCC financing statements required by state law, evidencing a complete and unbroken line from the mortgagee to the Trustee with evidence of recording thereon (or in a form suitable for recordation).*

*In addition, in connection with the assignment of any MERS Mortgage Loan, each Seller agrees that it will cause, at the Trustee's expense, the MERS(R) System to indicate that the Mortgage Loans sold by such Seller to the Depositor have been assigned by that Seller to the Trustee in accordance with this Agreement (and any Supplemental Transfer Agreement, as applicable) for the benefit of the Certificateholders by including (or deleting, in the case of Mortgage Loans which are repurchased in accordance with this Agreement) in such computer files the information required by the MERS(R) System to identify the series of the Certificates issued in connection with such Mortgage Loans. Each Seller further agrees that it will not, and will not permit the Master Servicer to, and the Master Servicer agrees that it will not, alter the information referenced in this paragraph with respect to any Mortgage Loan sold by such Seller to the Depositor during the term of this Agreement unless and until such Mortgage Loan is repurchased in accordance with the terms of this Agreement”*

## “To: All MERS Members

### Changes to Assignment to MERS

*MERS has revised its sample assignment form to clarify that Mortgage Electronic Registration Systems, Inc. (MERS) is the assignee of the mortgage lien, not the MERS member lender. Confusion resulted from having the clause “as nominee for” after the MERS name causing some erroneous indexing of the MERS member as the assignee in place of MERS, the true assignee. By removing the “nominee” wording, there can be no mistaking the fact that all interested parties intend MERS to be the assignee. The removal of the “nominee” language does not change the relationship between MERS and its Members as defined in the MERS Governing Documents.*

#### ASSIGNMENT OF MORTGAGE

*Example of an assignment to MERS from a non-MERS servicer or investor.*

Lenders Loan Number: MIN: <u>[insert 18-digit MIN]</u>	MERS Phone: 1-888-679-6377
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FOR VALUE RECEIVED, XYZ Mortgage Company, Inc., its successors and assigns, hereby assigns and transfers to Mortgage Electronic Registration Systems, Inc., its successors and assigns P.O. Box 2026, Flint, Michigan 48501-2026, all its right, title and interest in and to a certain mortgage executed by John Doe and Mary Doe, husband and wife to XYZ Mortgage Company, Inc. and bearing the date of the 12<sup>th</sup> day of September, A.D. 1998, and recorded on the 14<sup>th</sup> day of September A.D. 1998 in the office of the Recorder of Imaginary County, State of California in Book 1V at Pages 32-34.

For Nassau, Suffolk, Westchester, and Dutchess Counties, New York, use MERS corporate address: 1595 Spring Hill Road, Suite 310, Vienna, VA 22182

MERS name and address are added to the Assignment here. *If the state of incorporation for MERS is required, please note that MERS is organized and existing under the laws of Delaware, not Virginia.*

Sample Only

Signed on the 15<sup>th</sup> day of March A.D. 2002.

XYZ Mortgage Company, Inc. (Assignor)  
By \_\_\_\_\_ Assistant Secretary

State of California }  
County of Imaginary } ss:

On the 13<sup>th</sup> day of March A.D. 2002, before me, a Notary Public, personally appeared name of person signing document (above), to me known, who being duly sworn, did say that he or she is the Assistant Secretary of XYZ Mortgage Company, Inc., and that said instrument was signed on behalf of said corporation.

\_\_\_\_\_  
Notary Public

Address of Preparer:  
XYZ Mortgage Company, Inc.  
1234 Sample Street  
Assignment, CA 98765  
Attn: Final Documents Dept.

The MIN and MERS telephone number may be placed at the bottom of the assignment or within close proximity of the lender's loan number if recording jurisdictions allow. In any case, the county requirements should always be followed.

MIN: <u>[insert 18-digit MIN]</u>	MERS Phone: 1-888-679-6377
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# Electronic Signatures - Electronic Negotiable Instruments

James McGuire

## E-Sign Act

Electronic Signatures in Global and National Commerce Act<sup>1</sup>

**Subcommittee on Domestic Monetary Policy, Technology, and Economic Growth,  
Committee on Financial Services Washington, DC.**<sup>2</sup>

*Saturday, June 30th, 2000, President Clinton signed the historic E-SIGN legislation granting electronic records and signatures legal enforceability on a par with written documents. Enactment of E-SIGN was driven by the explosion in online commerce and the bipartisan desire of Congress and the Clinton Administration to facilitate its continued expansion.*

*This legislation gave legal recognition and effect to electronic signatures, contracts and records.*

*And now for an opening statement, the Chairman of the full committee who has a long and abiding interest in this legislation, Mr. Oxley.”*

*“Thank you, Mr. Chairman, and thanks for holding this hearing on E-SIGN and encouraging the use of electronic signatures in the financial services industry. This is the first technology-related hearing for the subcommittee, and I look forward to continuing our review of tech issues as they affect financial services.*

*The Electronic Signatures in Global and National Commerce Act enabled electronic signatures to satisfy the legal requirements for paper signatures. I worked closely with Chairman Bliley last session on the passage of E-SIGN, and I was a Member of the Conference Committee that wrote the current law.*

*The goal of E-SIGN was to simplify electronic business transactions, enabling consumers to sign a mortgage, take out a student loan, or open an IRA account from their own computer. Exchanging records and agreements electronically instead of on paper is good for the*

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<sup>1</sup> <http://uscode.house.gov/download/pls/15C96.txt>

<sup>2</sup> U.S. House of Representatives, Subcommittee on Domestic Policy, Technology, and Economic Growth, June 28, 2001

*environment, less burdensome for consumers, and more cost effective for businesses. Members of the Conference Committee envisioned that ESIGN would open up the floodgates to many new transactions that individuals and businesses would be able to do online while at the same time giving people greater confidence and convenience when shopping online.*

**STATEMENT OF EILEEN HARRINGTON, ASSOCIATE DIRECTOR FOR MARKETING PRACTICES, FEDERAL TRADE COMMISSION BUREAU OF CONSUMER PROTECTION**

*“In Section 105(b) of ESIGN, the Congress directed the FTC and the Department of Commerce to issue a report on the impact on electronic commerce and consumers of the reasonable demonstration requirement of the consumer consent provisions of the Act. Specifically, the Congress asked us to report on the benefits of that provision to consumers, the burdens that the provision imposes on e-commerce, whether the benefits outweigh the burdens, the effect of the provision in preventing fraud, and whether any statutory changes would be appropriate.*

*Our testimony today will be limited to a discussion of these issues which were the focus of our review and the report from Commerce and the FTC. To fulfill our mandate, we conducted outreach efforts, which included issuance of a notice in the Federal Register inviting comment, a public workshop, and extensive outreach to consumer, industry, and other Government organizations.”*

*“To comply with the mandate to solicit comment from the general public and consumer representatives in e-commerce businesses, as I mentioned we published a Federal Register notice inviting comment. We sent that notice and the press releases by both agencies to literally hundreds of businesses and organizations that we know have an interest in the development of electronic commerce. And in response to our outreach efforts, we received 32 comments from consumer organizations, software and computer companies, banks, members of the financial services industry, and academics.”*

**STATEMENT OF THOMAS E. CROCKER, PARTNER, ALSTON & BIRD, LLP**

*“Mr. Chairman, Chairman Oxley, and Members of the subcommittee, my name is Thomas Crocker. I am partner in the Washington office of the law firm of Alston & Bird. My involvement with the ESIGN Act goes back to 1997. When representing the then-CitiCorp, I helped draft a predecessor version of the ESIGN Act in the 105th Congress. More recently, we represented Charles Schwab & Company and the Securities Industry Association in all phases of the development, consideration, and eventual enactment of the ESIGN Act in the 106th Congress.”*

*“Our findings confirmed what we had long suspected to be the case—that use of the ESIGN Act has been slow to take off and that compliance with it is limited at best. Its embraced by U.S. industry at large has been spotty. Why is this so? Based on our work with various clients seeking to understand and implement the ESIGN Act, we believe that although well-intended, the ESIGN Act in its present form fails to deliver on the promises of uniformity, consistency, and legal certainty.”*

**STATEMENT OF JEREMIAH S. BUCKLEY, PARTNER, GOODWIN PROCTOR; GENERAL COUNSEL, THE ELECTRONIC FINANCIAL SERVICES COUNCIL**

*“However, based on my experience, the complexities and ambiguities of the statute have already resulted in a tangible level of discomfort in industry that procedures, once adopted, might be held inadequate or out of compliance when the law is eventually interpreted by courts or Federal or State agencies.”*

*“These instruments must be originated to the satisfaction of the secondary market purchasers of mortgages and chattel paper and others who trade in or finance these instruments. In order that this happen, each financial services industry will have to develop a series of conventions or guidelines regarding what electronic practices and procedures will be acceptable to companies doing business in that particular industry.*

*We at the Electronic Financial Services Council are participating in promoting the development of these guidelines or conventions. Over the last 7 months, Freddie Mac, one of our members, has developed specifications for the purchase of electronically originated loans in the secondary market. Freddie Mac and Fannie Mae are currently negotiating with lenders to arrange forward commitments for the purchase of electronically originated mortgages. And as a result, we expect a gradual, but steady, growth in the paperless mortgage transactions.”*

*“In the absence of court decisions affirming the evidentiary validity of electronic records, those seeking to do business electronically are understandably proceeding with caution.”*

**STATEMENT OF LOUIS F. ROSENTHAL, EXECUTIVE VICE PRESIDENT, ABN AMRO NORTH AMERICA, INC., ON BEHALF OF THE FINANCIAL SERVICES ROUNDTABLE AND BITS**

*“ESIGN creates a uniform national framework for the use of electronic signatures, contracts and other records.”*

*“Finally, our members are concerned that some Federal regulatory agencies are interpreting ESIGN in an overly restrictive manner. We urge Congress to continue to review agency*

*interpretations, along with the OMB Guidance on which many of them are based, to ensure regulations implementing ESIGN are consistent with the goals of the Act.”*

**Credit Union National Association<sup>3</sup>**  
**Project to Revise Articles 3 & 4 of the Uniform Commercial Code**

Michelle Q. Profit - Assistant General Counsel

*“The undersigned financial institution organizations are writing to you to urge that electronic negotiable instruments be included within the scope of the National Conference of Commissioners on Uniform State Laws (NCCUSL) current effort to revise UCC Articles 3 and 4. We believe this UCC Article 3 and 4 revision project represents a unique and critical opportunity for NCCUSL to provide leadership to the states and the financial institution community on the timely and important issue of electronic negotiable instruments.*

*We were quite surprised by the announcement this spring that it had been preliminarily decided not to include electronic negotiable instruments within the scope of the UCC Articles 3 and 4 revision project.”*

*For the foregoing reasons, the undersigned organizations urge the inclusion of electronic negotiable instruments within the scope of the current UCC Articles 3 and 4 revision project.”*

**ABA Business Law Section**  
**Committee on the Uniform Commercial Code**

Linda J. Rusch - Chair, Committee on the Uniform Commercial Code

*“The Electronic Signatures in Global and National Commerce Act (codified at 15 U.S.C. § 7001 et seq) (“Esign”) provides that the “provisions of Section 7001 of this title shall not apply to a contract or other record to the extent it is governed by. . . the Uniform Commercial Code, as in effect in any State, other than sections 1-107 and 1-206 and Articles 2 and 2A.” 15 U.S.C. § 7003.*

*This exclusion from the provisions of Section 7001 for contracts or records subject to the Uniform Commercial Code should be maintained. The Uniform Commercial Code as in effect and as revised accommodates electronic commerce in a carefully considered manner. Section 7001 is not necessary to facilitate electronic commerce in these transactions, and would be potentially harmful to established and evolving paper-based and electronic commercial transactions which are governed by the Uniform Commercial Code.*

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<sup>3</sup> [http://www.cuna.org/reg\\_advocacy/comment\\_letters/cl\\_102700.html](http://www.cuna.org/reg_advocacy/comment_letters/cl_102700.html)

**Uniform Commercial Code Article 3** governs negotiable instruments, including checks and promissory notes. Negotiable instruments must be in writing and signed. To the extent that parties want to engage in electronic payment mechanisms, Article 3 does not prevent parties from doing so. Thus parties may use funds transfer, debit cards, credit cards, ACH transactions or other forms of electronic payment mechanisms. All of those other types of payment mechanisms are governed by law other than Article 3 and Article 3 does not prevent their use. Article 3 provisions would merely not apply to those electronic payment mechanisms.

The primary purpose of Article 3 is to provide for the rights of third parties who take the negotiable instrument. Article 3 is premised on a regime of possession and indorsement of an instrument and the rights and obligations that accompany that possession and indorsement. To allow for electronic negotiable instruments there must be a concept that is the functional equivalent to possession and indorsement in order to adequately protect third party rights. The difficulty in making such a wholesale change was recognized at the time that both the Uniform Electronic Transactions Act (UETA) and Esign were promulgated by setting up the concept of a "control" system to substitute for the possession and indorsement concept as it applies to electronic notes. UETA Section 16 and Esign Section 7021. Nothing has changed to make that concern less real. Adequately protecting third party rights and assuring commercial market stability cannot be done by two party contracts in the absence of a statutory scheme that is designed to accommodate electronic negotiable instruments. Applying Section 7001 provisions would sweep away the writing and signature barriers as applied to the creation and enforcement of a negotiable instrument. This change would create havoc as there would be substitute for the possession and indorsement concepts that currently govern the rights and obligations of third parties as to a negotiable instrument.

**Conclusion** - As can be seen from the above comments, the current exclusion for the Uniform Commercial Code from the provisions of Esign Section 7001 should be continued.<sup>(10)</sup> To subject the Uniform Commercial Code to the generalized approach of Section 7001 is in large part unnecessary given the carefully crafted accommodations to electronic commerce already in place and would create much disruption and uncertainty in the transactions governed by the Uniform Commercial Code.

### **C. Analysis -- Are the Exceptions Still Necessary to Protect Consumers?<sup>4</sup>**

"The ESIGN Act provides that the "provisions of Section 7001 of this title shall not apply to a contract or other record to the extent it is governed by . . . the Uniform Commercial Code, as in effect in any State, other than sections 1-107 and 1-206 and Articles 2 and 2A."<sup>(73)</sup> This

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<sup>4</sup> <http://www.ntia.doc.gov/comments/2002/esign/report2003/partc.htm>



*provision establishes that transactions, contracts, and records subject to the identified sections may rely upon E-SIGN, as applicable, for validity. Those governed by one of the remaining Articles of the UCC -- Article 3 (Negotiable Instruments), Article 4 (Bank Deposits and Collections), Article 4A (Funds Transfers), Article 5 (Letters of Credit), Article 6 (Bulk Sales), Article 7 (Documents of Title), Article 8 (Investment Securities), and Article 9 (Secured Transactions) -- may not rely on E-SIGN for validity, but must instead look to other laws, including the Articles themselves, for validity.*

*given that several of the articles are based on the concept of negotiability of a signed writing, the proponents asserted that "simply substituting electronic records and authentications for writing and signature requirements . . . would have a significant unintended impact on substantive commercial law rules." A wholesale 'electronification of these articles would create new electronic payment products, such as electronic negotiable instruments, including checks, without providing an appropriate framework for handling them. Rules addressing physical possession, endorsement, and physical delivery that affect the right to own and enforce the subject writings "would make no sense, and would be impossible to satisfy, if the writing requirement were replaced with electronic records."*

#### ***CUNA & Affiliates***

#### ***Re: The Uniform Commercial Code Exception to the Electronic Signatures in Global and National Commerce Act (E-SIGN Act)***

*Michelle Q. Profit - Assistant General Counsel*

*Under current law, Articles 3 and 4 of the UCC do not allow for checks or other negotiable instruments to be created or transferred in electronic form.*

*The E-SIGN Act expressly exempts Articles 3 and 4 from its application. Therefore, the E-SIGN Act does not override Articles 3 and 4 to make electronic negotiable instruments the equivalent of their paper counterparts.*

#### ***Electronic Financial Services Council***

#### ***Re: The State Uniform Commercial Code Exception of the Electronic Signatures In Global and National Commerce Act, Docket No. 010222048-2313-07***

*Jeremiah S. Buckley – General Counsel*

*The UCC Exclusion first appeared in the Uniform Electronic Transactions Act ("UETA"). E-SIGN adopted the same exclusion, along with many other provisions of the UETA. Both the UETA and E-SIGN excluded Articles 3 through 9 of the UCC for one or more of the following reasons:*

*· The Article contained rules related to the use of writings as physical tokens and included integral rules on physical possession, indorsement and physical delivery that affected the right to own and enforce the writings – these rules would make no sense, and would be impossible to satisfy, if the writing requirements were replaced with electronic records (Articles 3, 4, 5, 7, 8 and 9);*

**Federal Reserve Bank of Atlanta**

**Re: The State Uniform Commercial Code Exception of the Electronic Signatures In  
Global and National Commerce Act, Docket No. 010222048-2313-07**

*Patrick K. Barron*

*The Reserve Bank believes that the UCC exception in E-SIGN should be retained. The Reserve Bank actively supports the adoption of new, more efficient technologies in the payments system, but we believe that the elimination of E-SIGN's UCC exception would not result in an orderly transition from paper based processes to electronic processes.*

*...the UCC does not depart from the tenet that a negotiable instrument must be a signed writing.*

*Simply changing the law by substituting electronic records and authentication would not account for the complex issues raised by making an electronic copy the legal equivalent of an original check. Eliminating the E-SIGN exception for Articles 3 and 4 would amount to a wholesale “electronification” of negotiable instruments without providing a legal or business framework for handling electronic instruments.*

**National Conference of Commissioners on Uniform State Laws**

*Re: Docket No.: 010222048-2313-07 (Request for Comments)*

*William H. Henning - Chair, PEB*

*I am writing as Chair of the Permanent Editorial Board for the Uniform Commercial Code (PEB). The PEB is a joint board established by the Code's co-sponsors, the American Law Institute and the National Conference of Commissioners on Uniform State Laws.*

*The analysis concludes that the E-SIGN exclusion for the UCC continues to be necessary and that significant harm to both consumers and commercial entities will result if it is repealed or in any way cut back.*