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ALABAMA COOPERATIVE Extension SYSTEM

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Fraud and the Internet: Online Shopping

Consumer education is the process of gaining the knowledge and skills needed to manage consumer resources and taking appropriate action to influence the factors that affect consumer decisions.

Know the Facts

According to a Harris Interactive survey commissioned by the National Consumer League (NCL), 31% or approximately 35 million people participate in online auctions. Ninety-four percent of the respondents are somewhat or very confident that they will get what they paid for as the winning bidder of an online auction. However, 41% of online auction buyers reported having a problem.

During 1999, consumers lost more than $3.2 million to Internet fraud according to incident reports compiled by the NCL's Internet Fraud Watch (IFW). A 38% increase in Internet fraud complaints in 1999, coupled with an average consumer loss of as much as $580, suggest an urgent need for consumer education about shopping online. “Many consumers shop online and have good experiences, but the increases we've seen in both the number of complaints and the amounts of money lost, point to the need for more consumer protection and increased education,” said Susan Grant, director of IFW.

IFW reported that online auction sales remained the number one Internet fraud for 1999, increasing from 68% in 1998 to 87% in 1999. Other top frauds for 1999, in order, are non-auction sales of general merchandise, Internet access services, computer equipment/software, and work-at-home plans.

Despite the fact that auction complaints rank number one among Internet fraud, there are higher consumer losses due to Internet fraud with general merchandise and computer hardware/software purchases. On average, consumers lost $580 per person to online purchases of computer equipment or software and $465 to general merchandise sales. Other items lost, but not attributed to online auctions, ranged from jewelry to t-shirts.

The average loss per consumer to online auction sales was $293. In incidents reported to IFW, consumers overwhelmingly pay for goods with checks and money orders, losing the rights they would have if they used a credit card. Perhaps because many consumers are unable to pay with a credit card for online auctions, credit cards accounted for only 3% of those transactions. Nevertheless, consumers can usually charge other online purchases; credit cards accounted for 29% of general merchandise sales and 23% of computer equipment and software purchases.

“Paying with a credit card is the safest way to shop online. Federal law protects credit card users if they do not get what the seller promised them or if unauthorized charges are made on their accounts,” said Grant. Additionally, IFW's top ten list for 2000 shows that online auctions remain the top fraud and consumers that have been victims are more likely to have paid with a check or money order.

Why Shop Online?

The Internet opens a world of products and services, including some that may not normally be available in your area. Information, however, is easy to find and comparing prices from different sellers takes only a few minutes. By shopping around on the Internet, you can find some terrific bargains at stores that you might never travel to in the physical world. Plus, you can do it conveniently at any time of the day or night. Looking for an out-of-print book or that perfect gift for someone with a particular hobby? The Internet makes it possible to find such items without leaving home!

What are the Risks?

While there are great shopping opportunities on the Internet, there are also some risks to consider.

Financial Fraud

When you provide your credit card, debit card or other payment information online, it could be intercepted by thieves. Dishonest employees or computer “hackers” could steal financial information stored in company databases.

Dishonest or Irresponsible Sellers

There are plenty of legitimate companies online, but there are also fraudulent sellers out to cheat consumers. Setting up a fancy Web page or posing as a reputable seller in an online auction is not difficult to do. For example, sending offers or soliciting charitable donations by e-mail is easy and inexpensive. Dishonest sellers may even misrepresent what they are offering, take your payment and never provide the merchandise or resolve the problem.

Invasions of Privacy

Many Web sites ask for personal information to grant access to their site, to complete a transaction, or for marketing purposes.

Consumer Protection

Financial Privacy Rule

The Federal Trade Commission (FTC) has published a rule as required by section 504(a) of the Gramm-Leach-Bliley (GLB) Act. The GLB Act, enacted on November 12, 1999, places certain restrictions on financial institutions when disclosing non-public consumer information to third parties. The Act directed the FTC and other federal agencies to develop rules to enforce the requirements set forth in the legislation.

There is still discussion and concern that this legislation in its present form is not working in the best interest of the consumer. Again, Congress is looking into an extensive rewrite of the GLB Privacy Act. The revised provision of the bill will require financial institutions to obtain a consumer's permission before disclosing non-public personal information to affiliates or third parties. In other words, if companies want to sell a consumer's personal information to non-affiliated businesses, they must give the consumer a chance to say no to such practice. This is referred to as “opting out”. However, a small percentage of consumers responded to the opt-out notices they received in the mail from banks, credit card companies insurance companies and other financial institutions.

As part of the revision to the GLB Act, some states are pre-empted from enacting privacy laws that are inconsistent with this Act.

Currently, a financial institution is required under the Act to provide consumers with a privacy policy at the time of establishing a customer relationship. The Act defines a customer relationship as a continuing relationship between a consumer and a financial institution whereby the institution provides a financial product or service to a consumer that is to be used primarily for personal, family or household purposes. The Act also describes the conditions under which a financial institution may disclose non-public personal information about a consumer, whether or not it has established a customer relationship with that consumer to a non-affiliated third party. Under the Act, such information cannot be shown without providing the consumer with the institution's privacy policy and the opportunity to opt out of the information sharing. This policy is subject to certain exceptions. Despite the broad notion of financial institutions dictated by the Act, the notice states that many entities that come within the broad definition of financial institutions will unlikely be subject to the disclosure requirements of the Act because not all financial institutions have consumers or establish customer relationships. For example, management consulting is a financial activity, but it is unlikely that any individual obtains management consulting services for personal, family or household purposes.

Similarly, not every product or service that a financial institution provides to an individual is a financial product or service that establishes the individual's status as a consumer entitled to the required notice and opt out agreement. A product or service that does not result from a financial activity is not within the scope of the Act. Therefore, “a department store that issues its own credit card directly to consumers provides a financial service (credit) to consumers who use the card, but when it sells merchandise, it provides a non-financial product or service,” said Grant.

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