

Texas Consumer & Commercial Law Update

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Welcome

This edition of the **Texas Consumer & Commercial Law Update** focuses on debt elimination scams currently being perpetrated on the public. These scams have become increasingly prevalent due to the ease with which the Internet allows unscrupulous individuals to promote their scams with a patina of legitimacy. This eNewsletter discusses the supposed theories underpinning debt elimination scams and summarizes the main arguments being used to overcome them.

This Edition

Scam Number 1 - Bogus Arbitrations

How this scam works:

Consumers are told by fraudsters that "national banks cannot lend credit." Then, the scam artists purport to arbitrate this issue in a bogus arbitration forum.

Consumers pay scam artists an up-front fee to "eliminate their debt," which can often cost the consumer thousands of dollars. Scam artists provide support and documentation to consumers and help them eliminate debt in a "consumer friendly arbitration forum because the arbitration forums chosen in the account agreement are biased." These documents include forms that purport to change the contractually chosen arbitration forum - such as the American Arbitration Association, National Arbitration Forum, or JAMS - to one that is run by the promoter of the scam.

Question 1. Is there any truth to the theory that national banks cannot lend credit?

Answer:

No. This legal theory propounded by the scam artists is frivolous. The National Bank Act specifically grants National Banking Associations the power to loan money on personal security, including the power to extend credit via credit cards. 12 USC §24 (Seventh); see *Colorado Springs National Bank v. United States*, 505 F.2d 1185, 1189-90 (10th Cir. 1974).

Question 2. Can a customer of the bank unilaterally choose an arbitration forum to resolve disputes?

Answer:

No. It is well recognized that such a change may not be made by a credit card customer without the agreement of the bank or an order of a court of competent jurisdiction. The Federal Arbitration Act (FAA) expressly provides that where a method for appointment is set out in the arbitration agreement, the agreed upon method of appointment "shall be followed." 9 U.S.C. §5. Several courts relying on §5 have determined that "[a]rbitration awards made by arbitrators not appointed under the method provided in the parties' contract must be vacated." *Cargill Rice, Inc. v. Empresa Nicaraguense Dealimentos Basicos*, 25 F.3d 223, 226 (4th Cir. 1994).

Question 3. Has any individual who obtained a bogus arbitration award been successful in confirming the award in court?

Answer:

No. Although attempts have been made to confirm awards received from these forums, there is no record of anyone successfully confirming such an award. Moreover, courts have sanctioned some who attempted to confirm such an award. For example in *Seiler v. MBNA*, Cause No. 434652 (Sup. Ct. Ca. 2002) the court, in denying the petition to confirm an arbitration "award" from a bogus forum (and referring the matter to the local district attorney), stated "[t]he petition and facts presented in the matter constitute one of the more palpable efforts of an individual to abuse the processes of the courts of the State of California in the undersigned's experience." The court further stated that "[t]he lack of integrity of such patently crude, legally unenforceable language demonstrates a sham enterprise by the perpetrating parties."

Question 4. To better identify the potential existence of a debt elimination scam, who are the players involved?

Answer:

Please email us at [Texas Law Update](mailto:TexasLawUpdate@mcglinchey.com) to request a list of scam programs.

These various players advertise that they can eliminate debt legally and successfully. Debtors are sometimes required to sign a contract that includes a confidentiality provision and certification that they are not undercover agents working for the government. For a substantial fee, usually several thousand dollars, the scam perpetrators provide form letters to send to credit card companies, as well as forms and instructions pertaining to the new "friendly arbitration forum."

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Scam Number 2 - Vapor Money

How this scam works:

Scammers misuse information from Congressional hearings and Federal Reserve press releases to convince debtors that Federal Reserve Notes are not money. They argue that any loan granted with Federal Reserve Notes is illegal and therefore the bank cannot legally require the debtor to repay the loan.

In the home mortgage context, scammers claim that an original loan funded via wire transfer is invalid. As such, banks in effect create "vapor money" since there is no actual advance of "real" money. The homeowner then creates an online account with the scammer, completes an application and sends a cashier's check, typically in the amount of \$3000, to the scammer in hopes that the first lien and second lien mortgages will be eliminated.

The scammer sets up a complex trust in the homeowner's name and the scammer appoints himself as a trustee. Title to the property is transferred to the trust. The "trustee" approaches the lender and makes a "presentment" to the bank in the form of a "cash-backed bond" purportedly equal to double the amount of the promissory note. The "bond" is allegedly a "valid rated instrument backed by a \$120 million Letter of Credit against the assets of an 85 year old \$800 million Swiss Trust Company."

The "bond" is not real. The scammer explains that if the bank accepts the bond and cashes it without providing proof that a loan was made to the borrower, the lender then has agreed that the client/trust has been damaged ten times the amount of the bond. At the same time, the scammer sends out a "legal complaint" in the form of a "CPA report" outlining 40 or more different federal laws that purportedly have been violated in the lending process. Per the terms of the "complaint," the lending institution has a certain time frame in which to respond. The debtor (homeowner) files a fake release of the original lien with the county clerk's office. The debtor then applies for a loan with another lender who thinks the property is unencumbered.

At the conclusion of this process, the borrower is in worse condition because two lenders believe that they have valid security interests in the property and both lenders will pursue foreclosure. The borrower is then placed in bankruptcy and a suit is filed on behalf of the homeowner alleging that no enforceable debt accrued to either lender because the loans were funded through a wire transfer rather than cash.

Question 1. Have the courts done anything to the organizers of the scam?

Answer:

Yes. In *The Frances Kenny Family Trust v. World Savings Bank FSB*, 2005 WL 106792 (N.D. Ca), the court, in making the decision to assess attorneys' fees against the attorney who brought the action, notified the State Bar of California as well as the United States Attorneys Office that "[g]reater bad faith would be hard to imagine. Plaintiffs and their counsel have employed a smokescreen to burden various lending institutions and impose upon them litigation costs in hopes of extracting settlements." In addressing the validity of the "vapor money" scam, the court also stated that "[P]laintiffs 'vapor money' theory has no basis in law. It has been squarely addressed and rejected by various courts throughout the country for over twenty years."

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New Case Alert

Amx Enterprises, Inc. v. Bank One, N.A., No. 01-04-01035, 2006 WL 947774 (Tex. App. -- Houston [1st Dist.] filed 4/13/2006)

In an opinion issued on April 13, 2006, the First District Court of Appeals in Houston, Texas held that a plaintiff in a check conversion case may not recover more than the face amount of the check. Specifically, the court rejected claims for interest, attorneys fees and consequential damages. The court also provided strong language upholding preemption of common law causes of action. [View the full opinion.](#)

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New Legislation

§ 276.002. Garnishment of Financial Institution

Effective September 1, 2005, the Texas Legislature amended the garnishment procedure as it affects financial institutions. Prior to the amendment, financial institutions were subject to the same risk of default in a garnishment action as other garnishees. Under Texas law, a garnishee who fails to answer a writ of garnishment can be held liable for the full amount of the underlying judgment regardless of the amount of proceeds held by the garnishee. Now, a creditor who seeks to obtain a default judgment in a garnishment proceeding against a financial institution is limited to the dollar amount that the garnishor is able to prove that the bank held on account for the debtor. [See Texas Finance Code § 276.002.](#)

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