

SUBJECT: Penalties for fraudulent filing of financing statement

COMMITTEE: Financial Institutions — committee substitute recommended

VOTE: 7 ayes — Marchant, Carona, Elkins, Giddings, Grusendorf, Gutierrez, Patterson

0 nays

2 absent — Hudson, Romo

WITNESSES: For — James O. Boyd, U.S. Department of Agriculture, Office of the General Counsel; W. George Ellis, U.S. Department of Agriculture, Rural Economic and Community Development (FMHA); Karen M. Neeley, Independent Bankers Association of Texas

Against — None

DIGEST: CSHB 73 would authorize civil lawsuits and criminal penalties for a person who intentionally or knowingly files a financing statement that is groundless or contains forged or false statements. The owner of the property could request release of the fraudulent financing statement and could recover the greater of \$5,000 or actual damages, court costs and reasonable attorney's fees in a civil action.

Filing a fraudulent statement would be a Class A misdemeanor (maximum penalty of one year in jail and a \$4,000 fine) or a state jail felony (maximum penalty of two years in state jail and a \$10,000 fine) if the actor's intent was to defraud or harm another.

The bill would take effect September 1, 1995.

SUPPORTERS SAY: CSHB 73 would close a loophole in the law that might allow a vindictive person to file a fraudulent financing statement without suffering any penalty. Penal Code sec. 37.10 creates penalties against those who present a governmental record with knowledge of its falsity; however, it is unclear whether a financing statement would be considered a "governmental record" by the courts. A financing statement (UCC-1 under the Uniform

Commercial Code) perfects a security interest in collateral (property) used by the debtor to secure a loan from the creditor. These financing statements can only be released voluntarily by the creditor or through judicial order.

Falsified filing statements create many problems for the property owner. For example, potential buyers of property search county records before purchase and in a fraudulent case might find a financing statement securing a \$7 million loan, creating a cloud on the title and suspicion about whether the property can really be sold. The seller of the property would have to show that the filings were fraudulent and obtain a judicial release at considerable expense. Even if a release is later filed, the original filing evidencing the \$7 million note might create problems for the owner when trying to obtain loans.

Recently an organization whose members advocate that people need not repay loans from financial institutions and as a result often suffer foreclosures on their land, have engaged in a nationwide campaign to file fraudulent financing statements against people involved in foreclosures and investigations against them, including judges, lawyers, auctioneers for a bank, surveyors for a bank, FBI investigators and others. A few of this group have been convicted on federal charges, including conspiracy to injure and impede an officer of the United States, for their fraudulent filings against U.S. bankruptcy judges and trustees in Texas.

Although these fraudulent filings occurred in Texas, only federal laws, not state law, protected the victims. County clerks in Texas usually have no discretion to decide whether or not to file a financing statement as long as the form is filled out correctly, and it is unclear whether a financing statement would be protected as a government record. CSHB 73 would protect the integrity of the filing system and Texas property owners from vindictive fraudulent financing statements, and the potential for awarding \$5,000 in civil damages would provide a good deterrent against fraudulent financing in the first place.

OPPONENTS
SAY:

Tort law already allows a person to sue another person for damages caused by fraudulent misrepresentation, so CSHB 73 would needlessly add another layer of laws to the books. In addition, CSHB 73 would allow the plaintiff to receive at least \$5,000 in damages even if actual damages were much less. This would be inappropriate since a fraudulent filing rarely causes significant damages. In fact, a fraudulent filing by its very nature cannot create a cloud on a title and therefore would not hinder a person from selling property or acquiring a loan. The potential criminal punishment of two years in state jail would also be unduly harsh for filing a questionable document no matter what the motive.

NOTES:

The committee substitute clarified that to be civilly or criminally liable a person would have to have filed the fraudulent financing statement knowingly or intentionally and not just by mistake. The substitute also allows the property owner to request from the court specific relief such as the release of the financing statement.