

# Combating Credit Card Debt Elimination Schemes

By John W. Scott



John W. Scott is a founding shareholder in the law firm of Scott Dukes & Geisler, P.C., a Birmingham, Alabama litigation defense firm. Mr. Scott's primary practice areas involve the representation of financial services institutions in consumer litigation and class actions, businesses and management in commercial disputes, and businesses in environmental and toxic tort litigation. As to his financial services practice, Mr. Scott has defended, among others, national and community banks, credit card banks, consumer finance companies, mortgage lenders, mortgage brokers, automobile lenders, consumer finance insurers, student lenders and collection agencies, as well as consumer reporting agencies. Mr. Scott's clients include Bank of America Corporation and its affiliates and the Federal Home Loan Mortgage Corporation (Freddie Mac).

Mr. Scott has nineteen years of litigation, trial, arbitration and appellate experience. His financial services practice includes defense of Fair Credit Reporting Act and Fair Debt Collection Practices Act cases, RESPA and "yield spread premium" cases and class actions, credit life and credit disability cases and class actions, wrongful foreclosure and wrongful repossession cases, fraudulent loan practices cases, and sham debt elimination and arbitration cases against credit card banks. Mr. Scott has been named by *Chambers USA 2008* as one of the "Leaders in Their Field" in Alabama in the practice area of commercial litigation. Mr. Scott has also been selected for inclusion in the 2008 *Alabama Super Lawyers* in the practice area of civil litigation defense.

Mr. Scott obtained his B.A. degree from the University of Virginia and his J.D. from Tulane University School of Law, where he graduated *magna cum laude* and was named a member of the Order of the Coif.

## I. Introduction

Debt elimination schemes, usually rooted in the internet, continue to plague creditors and victimize debtors. As the Federal Reserve Board first warned several years ago:

These schemes are proliferating on the Internet and the organizers are charging borrowers substantial upfront fees and commissions based on the total amount of debt that can be forgiven. Members of the public are being harmed as borrowers generally pay significant amounts of money without eliminating or reducing their overall debt obligations—which of course is not in fact possible through any of these programs. Also, the cessation of legitimate loan payments increases the risk of a foreclosure or other legal action being taken against the borrower, and in addition could negatively affect a borrower's credit rating. Financial institutions may find that the use of the specious documents complicates the collection process, and may at least temporarily prevent any final action against the consumer.<sup>1</sup>

The Office of the Comptroller of the Currency also recently warned of the persistent nature of these schemes:

The Office of the Comptroller of the Currency (OCC) is aware that the volume and variety of fraudulent schemes supposedly designed to

"eliminate" debt is increasing. These schemes are being promoted via the Internet and in seminars throughout the United States. The fraudulent schemes are being marketed to ordinary people, not just the wealthy or sophisticated, including borrowers who are current on their payments and those approaching foreclosure.<sup>2</sup>

The persons perpetrating the fraudulent schemes claim that they can eliminate borrowers' various types of debt, including mortgages, credit card balances (including balances on cards issued by nonbank companies), student loans, auto loans, and small business loans.

These schemes take a number of different forms. Some appear to have originated out of anti-tax efforts,<sup>3</sup> gained traction with mortgage lending, and now have moved to credit cards.<sup>4</sup>

This article analyzes two recent and common variations of credit card debt elimination schemes, as well as a third credit card scheme that harkens back to the dubious historical roots of the anti-tax and mortgage debt elimination schemes.

There are three common threads running through these debt elimination schemes. First, the theories underlying these schemes do not make a bit of sense. While often peppered with legalese, and even statutory and caselaw citations, as well as citations to various government

2. OCC Alert 2007-55, available at [www.occ.treas.gov/ftp/alert/2007-55.html](http://www.occ.treas.gov/ftp/alert/2007-55.html).

3. See *id.*; Stuart Wolfe, *Debt Elimination Schemes*, 59 Consumer Fin. L.Q. Rep. 357 (2005). For example, one group, which labeled itself as "expert educators," offered on its website "tax freedom non-filing programs," "debt termination programs," and estate planning.

4. See generally Wolfe, *Debt Elimination Schemes*, *supra*, which focuses on mortgage debt elimination schemes; accordingly, this article focuses on credit card debt elimination schemes.

1. Federal Reserve Board, SR 04-03 (Jan. 28, 2004) (footnote omitted).

documents, the legal theories are usually nothing but a combination of legal mumbo-jumbo, mixed liberally with a dose of conspiracy theories hinting at dark forces controlling the federal government and banking system. Second, these debt elimination schemes cost individual debtors, who are often facing dire financial conditions and susceptible to these schemes, thousands of dollars and, except possibly for an occasional aberration, do not relieve anyone of any debt.<sup>5</sup> Third, these schemes cost banks and creditors untold millions of dollars in attorneys' fees, as well as other transaction costs, in combating bogus claims by debtors that their debt has been eliminated and then in going after and shutting down the scammers.

## II. Sham Arbitration Awards

### A. Nature of the Scheme

In this scheme, credit card holders attempt to terminate or eliminate their credit card debt through the use of bogus arbitration awards issued by bogus arbitral forums. The awards typically purport either to hold the debt to be invalid, and uncollectible, or make an award of damages to the card holder in an amount equal to (or sometimes even greater than) the debt, thus establishing an offset that supposedly eliminates the debt.

The arbitration award scheme usually begins with credit card holders finding these services through the internet or attending "debt elimination" or "debt termination" seminars. These outfits sell themselves on claims such as "guaranteed credit card debt elimination." For example, one program made the following rather extravagant legal claims:

...Through binding arbitration you are given an award in your favor. There are many legal reasons for it. The attorneys handle all of the

procedures, paperwork, and arbitration appearances on your behalf. You need not be present for any of it. You then receive [a] judgement good in all 50 states against your credit card companies absolving you of the debt. This process has been on going for many years and is 100% legal and 100% guaranteed.

\* \* \*

Our program has been used with literally thousands of credit card accounts and it has stopped hundreds of millions of dollars from being collected. During the nine years this program has been available, no one has had to pay as much as one penny on any credit card or debt collector account.<sup>6</sup>

So why hasn't the public heard more about this wonderful debt elimination system? This answer is provided as well:

The majority of the stock in the prominent newspapers and television stations is owned by the eight families who own the Federal Reserve.

Most people do not realize that the Federal Reserve is not part of our government. They are no more federal than Federal Express. The Federal Reserve is a private, foreign corporation owned by eight very wealthy families, such as the Rockefellers and Rothchilds, just to name a few. These eight families own the media...They control the news that goes out over the Associated Press (AP) and United Press International (UPI). Obviously, they are not going to permit the media to

educate the public as to what really goes on in the banking business.<sup>7</sup>

Once the credit card holder signs up with and pays the debt elimination company (often with a credit card<sup>8</sup>), the debt elimination company produces form documents that purport to procedurally and substantively permit the credit card holder to arbitrate his or her "dispute" with the credit card bank through the auspices of a number of fly-by-night arbitral forums established to effectuate this scam. The cost for this type of service typically runs into the thousands of dollars for the debtor. One company, for example, charges \$1,995 for its "standard" program, which covers five credit cards, plus \$200 for each additional credit card. Separate arbitration fees, which must be paid to the arbitral forum, run hundreds of dollars more per credit card. Finally, to purportedly have the resulting arbitration award filed with a court for "certification as a judgment" will cost several hundred dollars more per award.<sup>9</sup>

To set the groundwork for the arbitration, the debt elimination company sends the form documents, on behalf of the credit card holder, to the credit card bank giving the bank a notice of a "dispute" regarding the particular account. The bases for these "disputes" rest on a number of less-than-sound legal arguments. For example, one internet-based company produced a "Notice of Dispute," in the credit card holder's name, based upon a "no consideration" argument, *i.e.*, that the bank never lent any money to the

5. See, e.g., *MBNA America Bank, N.A. v. Boddala*, 949 So. 2d 935 (Ala. Civ. App. 2006) (en banc trial court judge entered judgment affirming the debtor's bogus arbitration award against a credit card bank; the Court of Civil Appeals vacated the judgment on procedural and jurisdictional grounds).

6. Quotations taken from written promotional material for the Debt Termination Program offered through [www.capitalpromotion.com](http://www.capitalpromotion.com). Another company claimed that "[s]ince its inception in March 1998, 6756 credit cards have been wiped out totaling \$53,321,012.00." CCDebt101, available at [www.credent101.com/faq.php](http://www.credent101.com/faq.php).

7. Debt Termination Program, available at [www.capitalpromotion.com](http://www.capitalpromotion.com).

8. One company in the "FAQ" section of its website stated:

Q. If I use a credit card to pay for your program, and then terminate my credit card debt, isn't that the same as getting the program for free?

A. Yes!

TA Financial Group, available at [www.tafinancial.net/dfaq.html](http://www.tafinancial.net/dfaq.html).

9. One distraught credit card holder, when it became apparent that the arbitration awards would not be automatically converted into judgments by a court and that the credit card banks were fighting the bogus awards, emailed the debt elimination company: "Would someone PLEASE make contact with me so I know what to do? Have I been scammed out of \$10,000 or are these arbitration awards legitimate?" The court vacated the bogus arbitration awards and the card holder eventually filed bankruptcy.

credit card holder. This theory asserts that under our system of fractional reserve banking, the credit card bank does not extend credit to the card holder, but rather uses the card holder's good name and credit rating to create more money for itself. Thus, the theory goes, the bank actually owes the card holder money:

Our written account agreement is predicated on the basis that you would be lending money to me; however, in fact, that is not the case since you have advanced me no consideration for the debit charges that you have placed on my account. I have heretofore made payments to you on this account in spite of the fact that you advanced no consideration to me. What I have learned is that you used my application to create new money for yourself. In doing this, you concealed from me the fact that you were using my credit to increase the value of your own portfolio at my expense. My account was never a debit on your books of accounting according to generally accepted accounting principles (GAAP).

Under this particular program, the "Notice of Dispute" was followed by an "Initial Claim" form, setting forth four purported "claims" against the credit card bank, as follows:

THE NATURE OF THE DISPUTE:

(1) Claimant received no consideration from Respondent. See the Federal Reserve Publications: Two faces of Debt, Federal Reserve Bank of Chicago, page 19 states "...a depositor's balance also rises when the depository institution extends credit—either by granting a loan to or buying securities from the depositor. In exchange for the note or security, the lending or investing institution credits the depositor's account or gives a

*check that can be deposited at yet another depository institution. In this case, no one else loses a deposit. The total of currency and checkable deposits—the money supply—is increased. New money has been brought into existence by expansion of depository institution credit. Such newly created funds are in addition to funds that all financial institutions provide in their operations as intermediaries between savers and users of savings," and Modern Money Mechanics, Federal Reserve Bank of Chicago, page 7 states, "Loans are made by crediting the borrowers account, i.e., by creating additional deposit money":*

- (2) Violations of the Truth In Lending Act, specifically 15 U.S.C. Section 1666(I), and Regulation Z, Sections 226.12(c) and 226.13(c),...
- (3) Claimant's account has been reported to credit bureaus as a negative report, however *the debt has not been substantiated as a valid debt owed by the Claimant*; and is therefore a violation of the Fair Credit Reporting Act, specifically 15 U.S.C. § 1681s-2,....
- (4) Respondent used Claimant's credit without Claimant's knowledge or consent and without benefit to Claimant. As a result thereof, Respondent has been unjustly enriched in an amount equal to or greater than the disputed account's credit limit.<sup>10</sup>

The credit card holder also, as part of this scheme, makes a claim for monetary relief against the credit card bank, usually either for the outstanding balance on the credit card account or the credit limit, whichever is greater.

Once the credit card holder has established his or her "dispute" and "claims" with the credit card bank, the matter moves on to the dispute resolution stage, usually through an attempted modification of the arbitration provision in the credit card agreement. Credit card arbitration clauses typically require dispute resolution through the American Arbitration Association, the National Arbitration Forum, or JAMS/Endispute. Under a typical debt elimination scheme, however, the dispute supposedly goes not to one of these well-recognized, nationally-known arbitration forums, but to a fly-by-night outfit formed to effectuate the debt elimination scheme. In other words, the dispute goes to an arbitrator who will, in accordance with the promises of the debt elimination company, issue an arbitration award in the credit card holder's favor and against the credit card bank.

This purported card agreement modification is accomplished by sending the credit card bank a unilateral notice supposedly altering the terms of the arbitration clause found in the credit card agreement, along with a check for a nominal sum as "consideration" for the contract modification. For example:

Enclosed please find my check in the amount of ten dollars (\$10) that serves as consideration for several modifications in our credit card

10. (Continued from previous column)

America located in Bridgeport, Alabama. The "no money lent" theory has also arisen in the context of mortgage debt elimination schemes, not surprisingly without much apparent success. See, e.g., *Alcorn v. Washington Mut. Bank, F.A.*, 111 S.W.3d 264, 266 (Tex. Ct. App. 2003) (borrowers "took the position that, when they executed and delivered the home equity note to Long Beach Mortgage Company, the note did not evidence a debt from them to the mortgage company, but instead 'created money' belonging to them that they do not owe to anyone. This is a legally erroneous concept that is apparently based on [borrowers'] misinterpretation of some information they discovered in a publication by the Federal Reserve System."). *Demmler v. Bank One, NA*, 2006 WL 640499, slip. op. at \*3-4 (S.D. Ohio March 9, 2006) (finding "no consideration" argument "patently ludicrous").

10. Bold, capitalization, underlining and italics in original. These particular "Notice of Dispute" and "Initial Claim" forms, as well as the form letter set forth below unilaterally purporting to change the arbitration forum, were submitted in several hundred credit card arbitrations carried out by Arbitration Forum of (Continued in next column)

agreement. Regardless of any other provisions in our agreement to the contrary as to how it may be modified or changed, by accepting this payment from me you agree that my selection as to the arbitrator of any disputes, the choice of law and venue, shall be binding upon us. I am specifically rejecting any prior dispute methods and designation or selection of arbitrator(s) contained in our agreement. In this regard, we both waive any right to litigate any claims between us. You agree to binding arbitration through one of the three following neutral arbitration services of my choosing:

Arbitration Forum of America, Inc.,  
P.O. Drawer 1006, Bridgeport, Alabama 35740-1006

National Arbitration Council, Inc.,  
P.O. Box 234, O'Brien, FL 32071

Solomon Arbitration Group, Inc.,  
2905 N. Montana Avenue, Suite #209, Helena, MT 59601

I trust that we want any dispute resolved expeditiously and that you will find this agreeable to you and if so you may process the enclosed check as confirmation that you agree to these changes in our agreement, to take effect immediately. If I have not heard back from you to the contrary within the next twenty-five days, or if you cash this check, or simply hold on to it without cashing or returning it to me, such will constitute acceptance of these terms by you.

Because credit card agreements do not allow unilateral amendments by the credit card holder, the credit card bank generally responds with a letter to the card holder rejecting the changes and affirming the terms of the credit card agreement and its arbitration clause. The bank's position regarding unilateral amendments to the credit card agreement is fully supported by the law. Generally, a party to a contract may not unilaterally

alter or amend that contract by partially fulfilling that party's preexisting obligations under the contract.<sup>11</sup> In other words, a credit card holder cannot unilaterally alter the credit card agreement by making a payment under the contract that was already due and owing.

After receiving the "dispute," the bogus arbitration forum issues an arbitration award in favor of the credit card holder and against the credit card bank. A typical sham arbitration award, this one used by Arbitration Forum of America of Bridgeport, Alabama, states as follows:

#### AWARD

Having carefully considered the evidence and the arguments of the parties on the issue; it is the decision of the Arbiter that this award is issued in favor of **John Doe**, Claimant.

Let it be known that **John Doe** prevails on all allegations. The Respondent, **Credit Card Bank** has failed to carry the burden of proof.

Further, let it be known:

1. That no known conflict of interest exists.
2. That on or before \_\_\_\_\_, 200\_, the parties entered into an agreement providing that any disputes that arise shall be arbitrated. This matter has been resolved in accordance with the Arbitration Forum of America, Inc. Rules and Procedures of Arbitration.
3. That the Claimant has filed a claim with the Arbitration Forum of America, Inc. and has served it upon the respondent.

4. That the Respondent has been served with the evidence file, including the Notice of Arbitration, Demand for Arbitration and Initial Claim by the Arbitration Forum of America, Inc.
5. That the parties have had the opportunity to present all evidence and information to the Arbitration Forum of America, Inc. and the Arbiter.
6. That after careful review of the demand and answer, together with the evidence, and after having been properly advised in the premise, the arbitration committee has unanimously adjudged this arbitration award in favor of **John Doe**, the Claimant, and against **Credit Card Bank**, the Respondent for damages, cost and fees not exceeding [outstanding balance or credit limit], which shall accrue interest at the legally mandated rate on all money thus owed to **John Doe** from this date.
7. The prevailing party, **John Doe**, is entitled to have this debt paid immediately upon demand and notification.
8. Further, it is the finding of this Committee that **Credit Card Bank** shall, within thirty (30) days, communicate to the major consumer credit reporting agencies, referencing account number XXXXXXXXXXXX, and any subsequent numbers relating to this account that all negative reports shall be expunged from the account and that the disputed amount has been resolved and credited.

Once the award has been issued, the debt elimination company usually recommends that the credit card holder file the arbitration award with a court

11. See, e.g., *Continental Ins. Co. v. Rutledge & Co.*, 750 A.2d 1219, 1232 (Del. Ch. 2000) ("A party cannot rely on a pre-existing duty as his legal detriment in an attempt to formulate a contract.") (Delaware law); 3 WILLISTON ON CONTRACTS § 7.36 at 569 ("As a general principle, when a party does simply what he has already obligated himself to do under a contract, he cannot demand any additional compensation or benefit, and it is clear that if he takes advantage of the situation and obtains a promise for more, the law in general regards it as not binding as lacking consideration.")

to convert it into a judgment. This can occur through a mass filing of awards, which happened in Jackson County, Alabama, where nearly 200 bogus awards issued by the Arbitration Forum of America were filed with the Jackson County Circuit Court before an injunction was entered stopping the filing of the awards. Or, the award can be filed on an individual basis by the card holder in different courts around the country.

**B. Judicial Responses**

Not surprisingly, courts have recognized these awards, and the underlying arbitration and debt elimination process, for the shams that they are. Courts have almost uniformly vacated sham arbitration awards presented for confirmation as judgments.

Courts have even taken it upon themselves to either vacate or refuse to enforce these arbitration awards. In *Edward A. Seiler v. MBNA*,<sup>12</sup> the credit card holder filed a petition to confirm his arbitration award. The court, after failing to find a telephone number for the arbitral forum and although the credit card bank (MBNA) had not made an appearance in the case, advised the petitioner “that his petition presented possible fraud on the Court.”<sup>13</sup> The court further concluded that the “petition and facts presented in this matter constitute one of the more palpable efforts of an individual to abuse the process of the courts of the State of California in the [court’s] experience.”<sup>14</sup> The court denied the petition, finding “that petitioner has attempted to deceive the Court, first advancing a unilateral ‘agreement’ in the form of a letter to respondent demanding arbitration and characterizing his unilateral letter as an agreement by respondent to arbitrate, then providing the Court with a contrived award.... The lack of integrity of such patently crude, legally unenforce-

able language demonstrates a sham enterprise by the perpetrating parties.”<sup>15</sup>

Similarly, in *Sorenson v. Fleet Bank (R.I.), N.A.*,<sup>16</sup> the court refused to confirm the sham arbitration award on jurisdictional grounds. Even though Fleet Bank had not made an appearance or argument in the *Sorenson* case, the court noted that the arbitration forum, Century Arbitration Associates of Ocala, Florida, was not one of the forums mandated by the Fleet Bank credit card agreement. Accordingly, the court stated that “[b]efore reaching the legal issues of Petitioner’s Motion [to enforce arbitration award], the Court must address the dubious factual basis of Petitioner’s claim. The Court seriously questions whether Century Arbitration Associates is a legitimate entity. An internet search revealed no evidence that Century actually exists, and though Century is allegedly based in Ocala, Florida, Century’s fax number, listed on the arbitration complaint, contains a New Hampshire area code. The Court will not enforce an award obtained under such questionable circumstances.”<sup>17</sup>

In *John Ellis v. Chase Manhattan Bank, USA, N.A.*, and related cases, the credit card banks vigorously opposed the mass filing of sham arbitration awards in Jackson County, Alabama. The trial court vacated a number of bogus arbitration awards that had been issued through the auspices of the Arbitration Forum of America to credit card holders throughout the country.<sup>18</sup> After holding an evidentiary hearing, which included testimony from card holders, the court concluded:

There can be no doubt, based on the evidence presented to this Court that the entire scheme that produced the purported arbitration awards was fraudulent. Among the numerous facts compelling that conclusion

are [the] guarantee to eliminate the Cardholders’ debt, all arbitrations resulted in awards for the Cardholders, each arbitration was based on the identical alleged dispute and the only two arbitrators issuing the purported awards had no legal training, no arbitration training and no experience in the credit card business.

These awards were conclusively “procured by corruption, fraud or undue means,” there was clear and “evident partiality [and] corruption” in the arbitrators, and the arbitrators were guilty of misbehavior by which the rights of the banks were prejudiced. These awards are therefore due to be vacated pursuant to the [Federal Arbitration Act].<sup>19</sup>

In one of the few cases that have made it past the trial court level,<sup>20</sup> *MBNA America Bank, N.A. v. Bodalia*,<sup>21</sup> the Alabama Court of Civil Appeals, while vacating on jurisdictional grounds the judicial confirmation of a bogus award under Alabama’s arcane and archaic arbitration statute, expressed its opinion that the award was a sham and nullity. The *Bodalia* case involved an arbitration award procured by a credit card holder purporting to adjudicate claims arising out of the use of her MBNA credit card.<sup>22</sup> The credit card agreement with MBNA contained an arbitration clause requiring that all disputes between Bodalia and MBNA be resolved by binding arbitration conducted by the National Arbitration Forum.<sup>23</sup>

After defaulting on her payments, Bodalia sent a letter to MBNA purporting to amend the credit card agreement to require that disputes be arbitrated “through

12. Case No. CIV 434652 (Superior Ct., County of San Mateo, Cal. Dec. 23, 2003).

13. *Id.*, slip op. at 3.

14. *Id.*, slip op. at 4.

15. *Id.*, slip op. at 6.

16. 2004 WL 964265 (D. Minn. April 30, 2004).

17. *Id.* at \*1.

18. CV-04-510 (lead case), CV-04-304, CV-04-305, CV-04-436, CV-04-455, CV-04-456, CV-04-458, CV-04-459, CV-04-460, CV-04-461 & CV-04-516 (Circuit Ct., Jackson County, Alabama July 21, 2005).

19. *Id.* slip op. at 11-12.

20. It is not surprising that most of these cases involving confirmation of bogus awards are disposed of by trial courts with no subsequent appeals. Most card holders attempt to confirm their awards on a *pro se* basis and do not appeal after the trial courts vacate their awards.

21. 949 So. 2d 935 (Ala. Civ. App. 2006). See also *supra* note 4.

22. *Id.* at 936.

23. *Id.*

an arbitration service of [her] choice only."<sup>24</sup> Bodalia later designated the National Arbitration Council, Inc. (NAC), as the arbitration service of her choice.<sup>25</sup> As "consideration" for the purported modification of her credit-card agreement, Bodalia enclosed a check in the amount of \$10.00. MBNA cashed the check.<sup>26</sup>

Bodalia subsequently sent MBNA a written demand for arbitration and filed a claim for arbitration with NAC.<sup>27</sup> In her demand for arbitration, Bodalia did not dispute any particular charges, but asserted that MBNA had failed to lend her money as required by the credit card agreement.<sup>28</sup> According to Bodalia's theory, payments that MBNA made to merchants for goods and services were not advancements of credit, but the creation of new money that had never existed.<sup>29</sup> Bodalia, in her arbitration demand, alleged she did not owe MBNA any money and, in fact, MBNA owed her money that it had allegedly failed to lend to her.<sup>30</sup>

The court noted that although the correctness of the NAC arbitration award was not before it, Bodalia's arbitration argument was without legal merit.<sup>31</sup> "Bodalia's theory is known in the credit industry as the 'vapor money' or 'no money lent' theory, and it is commonly used to avoid legitimate debts."<sup>32</sup> The court also held that Bodalia's purported "amendment" to the credit card agreement was not effective to modify the terms of the agreement.<sup>33</sup> Finally, the court held it appeared that the NAC

proceeding "did not comply with the minimum standards of due process."<sup>34</sup>

In addition to having courts vacate bogus awards, banks have been successful in shutting down the bogus arbitration forums themselves. *Citibank (South Dakota), N.A. v. National Arbitration Counsel, Inc.*,<sup>35</sup> provides a good example of this strategy. In the *Citibank* case, the court granted the banks' summary judgment against a bogus arbitration company, National Arbitration Council, Inc. (NAC). The court concluded that the NAC's "arbitration 'procedure' and 'awards' constitute nothing more than a sham."<sup>36</sup> The court found in favor of the banks on their claims for tortious interference with their contractual agreements with their credit card holders by the NAC, as well as their claims against the NAC for violation of Florida's Deceptive and Unfair Trade Practices Act.<sup>37</sup> The court permanently enjoined the NAC, and its principal, from conducting any further arbitration involving the banks' credit card holders, and vacated all arbitration awards rendered by NAC against the banks.<sup>38</sup> Credit card banks have used similar strategy and claims to pursue and shut down the internet-based debt elimination companies behind these schemes.

34. *Id.* at n.3. See also *AmSouth Bank v. Soltis*, 2005 WL 3601460 (Tenn. App. Dec. 29, 2005) (affirming, on procedural grounds, trial court's entry of summary judgment in favor of the bank and against card holders who sought to have bogus arbitration awards confirmed, and also commenting on the bogus nature of the awards).

35. 2006 WL 2691528 (M.D. Fla. Sept. 19, 2006).

36. *Id.* at \*5.

37. *Id.* at \*7-8. The *Citibank* decision contains a good analysis of the arguments and claims that banks have against these arbitration outfits, as well as the questionable nature of the arbitration awards.

38. See also *Chase Bank USA, N.A. v. Dispute Resolution Arbitration Group*, 2006 WL 1663823 (D. Nev. June 9, 2006) (granting a preliminary injunction against the arbitration forum); *MBNA America Bank, N.A. v. Cice & Wagenblast, P.C.*, 2005 WL 2709281 (N.D. Ind. Oct. 20, 2005) (denying the arbitrators' motion for judgment on the pleadings against the credit card bank seeking dismissal of the bank's claims relating to sham arbitrations based upon concept of arbitral immunity). A number of credit card banks in the Jackson County, Alabama, litigation referenced above also obtained injunctive relief against the Arbitration Forum of America, effectively putting it out of business.

Various governmental agencies, including the Federal Reserve Board, the Federal Trade Commission, and the Justice Department have also taken an interest in shutting down these bogus debt elimination schemes.

### III. Variations on a Theme 1: Sham Truth-In-Lending Act Arbitrations

Under this scheme, the credit card holder, after signing up with and paying a debt elimination company, attempts to take advantage of the arbitration provision in the credit card agreement as written. The scheme starts with the card holder sending to the credit card bank a form "Billing Error Notice" generated by the debt elimination company. The card holder, pursuant to the arbitration clause in the credit card agreement, then demands arbitration under the auspices of the designated arbitral forum, alleging a claim against the credit card bank for Truth in Lending Act (TILA)<sup>39</sup> violations based upon the purported billing errors in the monthly credit card statements.

The Billing Error Notice scheme rests on the premise that not all of the statutorily required TILA disclosures were made to the card holder prior to the opening of the credit card account. The Billing Error Notices usually cite the TILA, its subchapter, the Fair Credit Billing Act,<sup>40</sup> and the TILA's corresponding implementing regulatory framework, Regulation Z.<sup>41</sup> The card holders, based on these Billing Error Notices, then file arbitration claims against their credit card banks asserting that every posting on every monthly periodic statement was an actionable billing error under the TILA and Regulation Z.

A typical Billing Error Notice states, on behalf of the credit card holder, somewhat obtusely, his or her "beliefs" as to the nature of the purported billing errors:

My belief that the statement contains Billing Errors under 15 U.S.C. § 1666(b)(1), (2) and (5) is based upon my belief that you failed to give all the proper disclosures required by law to me prior to opening this account, and additional disclosures since then.

39. 15 U.S.C. §§ 1601 *et seq.*

40. *Id.* § 1666.

41. 12 CFR §§ 226.1, *et seq.*

24. *Id.* at 937.

25. *Id.*

26. *Id.*

27. *Id.*

28. *Id.*

29. *Id.*

30. *Id.*

31. *Id.*

32. *Id.* at n. 2.

33. *Id.* at n.1.

Because you failed to provide these disclosures, the account could not legally be opened and I should not be responsible for the payment of interest, fees or other finance charges.

These TILA arguments have about as much merit as the "no money lent" argument outlined above. These Billing Error Notices consistently fail to specify what the disclosure deficiencies were or are. Furthermore, the TILA requires two types of disclosures, initial disclosures prior to the time the account is opened,<sup>42</sup> and disclosures with each monthly billing statement.<sup>43</sup> A reading of the statutory definition of "Billing Error," found in the TILA, however, makes clear that even if there is a lack of initial disclosure, by definition it is not a Billing Error.<sup>44</sup> Moreover, card holders have argued that carrying a finance charge over more than one billing period constitutes an extension of credit under the TILA, thus requiring additional disclosures. This is refuted by the fact that finance charges are *incident* to the extension of credit but are not themselves extensions of credit triggering the TILA's disclosure requirements.<sup>45</sup>

Two interesting differences in these arbitrations, as opposed to the sham "no money lent" arbitrations, lie in the fact that they have been brought by a number of lawyers on behalf of the credit card holders, and, as noted, the scam utilizes the legitimate arbitration companies identified in the credit card agreements. Because these TILA disclosure violation claims have been submitted to and decided by legitimate arbitrators, the credit card holders have not been successful in obtaining awards by asserting these types of claims against

the credit card companies, and this particular scam appears to be on the wane.<sup>46</sup>

#### IV. Variations on a Theme 2: Use of a Strawman

Another variation of the credit card scheme that has shown up on the internet promises to eliminate credit card debt through the filing of a UCC-1 financing statement and related documents. This appears to be a variation of the mortgage lending scam where a borrower's property is put into a "trust" owned by a "strawman." The mortgage scam in turn apparently has its genesis in the anti-tax movement.

An example, apparently being touted by the some of the same people behind one of the arbitration schemes, is one internet site claiming:

The program is a 100% legal, proprietary process designed to close your credit card accounts and cancel your unsecured debts without you having to pay the balances. The process is accomplished first by you filing a UCC-1 application and becoming a Creditor rather than a Debtor, and then, with a series of letters, an administrative injunction is accomplished....your consultant will provide you with the appropriate guidance and suggestions each step of the way.

The program implements information from the Federal Reserve, the Fair Debt Collection Practices Act, federal banking regulations, The Uniform Commercial Code, and expertise in contracts and the legal system to help achieve

your goals. Individuals who have implemented this strategy have experienced unprecedented success.

This scheme appears premised upon the theory that, through the filing of a UCC-1 financing statement, the debtor becomes the "owner" of his or her own debt.

By filing the UCC-1 and other papers, you become the holder in due course [sic] with your STRAWMAN. All the debts you have are to your STRAWMAN which the government created without your knowledge. As explained in the material you have read, you are now in the first position instead of the government and the bank and anyone else who has a "lien" on you. Once filed they no longer have jurisdiction. You do not dispute that your STRAWMAN owes the bill on those credit cards, you agree, but since you are now holder in due course, and not them, you can instruct them to discharge the balance of debt as you are excusing the debt to your artificial person. When you implement the strategies of our program, the creditors will have no other course, as dictated in the laws of Commerce, to accept your rightful place as the person in first position who can take back the "loan" that was "given."

Your credit report will suddenly show that you have a zero balance for that, or those, credit card(s), and you may expect a nice letter from the bank(s) thanking you for discharging your debt to them.

As with other schemes, the rationale behind the "strawman" approach is somewhat murky and not grounded in reality. One federal court tried to decipher the strawman theoretical underpinnings, finding its origins in the "redemptionist" or "sovereign citizen" movement:

Redemptionists assign an imaginary account number to some sort of direct treasury account,

42. 15 U.S.C. § 1637.

43. *Id.* § 1667(b).

44. *Id.* § 1666(b). Moreover, the TILA has a one-year statute of limitations for claims arising from allegedly deficient initial disclosures, making most claims based upon initial disclosures academic. *Id.* § 1640(e).

45. See *id.* § 1605(a); Household Credit Servs., Inc., v. Pfennig, 541 U.S. 232, 236 (2004) ("finance charge" is an amount incident to the extension of credit).

46. For example, one arbitrator summarily concluded: "Claimant shall receive nothing from his claims in the arbitration for the following reasons: (1) Claimant never had a good faith belief that there was a billing error actionable under applicable law. (2) Claimant never stated a billing error in its notice to Respondent in accordance with applicable law. (3) Respondent did not violate its duties or obligations under applicable law in connection with its interaction with Claimant as alleged." (emphasis in original). See also Discover Bank v. Robin L. Roberts aka Robin L. Culp, Court File No. 56-C9-06-402359 (Dist. Ct., County of Otter Tail, Minn. May 9, 2007) (rejecting card holder's "billing error" argument and granting summary judgment to the creditor in a collection suit).

advocate that this direct treasury account has a balance equal to the monetary value the government places on the life of an individual, and then charge against this direct treasury account through the use of fraudulent checks called "sight drafts" by making written demand to the Department of Treasury for payments from the account....The sight drafts appear to be real checks and business and financial institutions run the risk of cashing them before they discover the fraud....

Redemptionists believe government has no power over the live body of a person and all taxes, mortgage interest rates, and criminal convictions are against a "strawman" likeness

of that live body....Redemptionists then file UCC filings claiming their strawman is a commercial vehicle and make written demands for payment of services performed by the strawman or use of their copyrighted strawman name.<sup>47</sup>

The Texas Court of Appeals similarly rejected this type of "goobledygoon" in a credit card case. In *Cavazos v. Citibank (South Dakota), N.A.*,<sup>48</sup> the credit card holder argued that the pleadings and judgment against him spelled his name in all capital letters. As a result, the card holder argued that he subsequently filed a UCC-1 financing statement against "the fiction 'JAMES CAVAZOS' giving him a superior lien priority on that

fictitious entity's assets."<sup>49</sup> The court concluded that the card holder did not, with this argument, "present any comprehensible issue for our review."<sup>50</sup>

## V. Conclusion

These debt elimination schemes have done little, and certainly nothing legitimate, to help debtors or eliminate anyone's debt. They have been successful in picking the pockets of an unknown, but probably a large, number of needy and unsophisticated credit card holders over the past few years. Accordingly, lawyers, credit counselors, banks and creditors should continue to be vigilant and to combat these schemes as (or preferably before) they arise.

47. *Ray v. Williams*, 2005 WL 697041, slip op. at \*5 (D. Or. March 24, 2005) (citations omitted). The *Ray* court, slip op. at \*6, also noted other cases, primarily tax cases, where these types of arguments had been raised and rejected: *United States v. Hoos*, 166 F.3d 1222, 1999 WL 12741 (10th Cir.1999) (defendants convicted of corruptly endeavoring to obstruct or impede the due administration of the internal revenue laws by filing false UCC-1 financing statements listing the two IRS agents who attempted to collect defendants' back taxes as debtors); *United States v. Fulbright*, 105 F.3d 443, 452 (9th Cir.1997) (noting, in case where defendant mailed false arrest warrants to bankruptcy judge and attempted to file false UCC-1 forms, that filing a false UCC form regarding the judge is prohibited by the statutes at issue in the case—18 U.S.C. § 372 (conspiracy to impede or injure federal officers) and 18 U.S.C. § 1503 (obstruction of justice by intimidating or injuring federal officers)); *United States v. Hilgeford*, 7 F.3d 1340, 1342 (7th Cir.1993) (rejecting as frivolous argument that an individual is a sovereign citizen of a state who is not subject to the jurisdiction of the United States and federal taxing authority).

49. *Id.*

48. 2005 WL 1366179, slip op. at \*3 (Tex. App. June 9, 2005).

50. *Id.*

## District of Columbia Mortgage Disclosure Act...

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that mortgage lenders must provide a mortgage disclosure form, a copy of which appears as an Appendix hereto, to borrowers within three days of receiving a loan application for a "non-conventional mortgage loan." A "non-conventional mortgage loan" is defined as any residential mortgage loan that is not a fixed-rate mortgage loan with an amortization period of thirty years or less. The Bulletin states that the new disclosure requirement will enable a borrower to better understand the consequences of borrowing funds that might have an adjustable interest rate resulting in higher payments in the future and also to determine whether the borrower can properly afford to service the loan.

Interestingly, the Act provides that if the disclosure is physically (as opposed to electronically) given, the notice must be printed on a red sheet of paper.

The Act provides that within five days of receiving the disclosure form and accompanying definitions, the borrower may cancel the loan application and receive a refund for any monies except for a reasonable application fee. The Act states that the lender must notify the borrower of this right to cancel at the time the lender provides the disclosure form and definitions.

The Act provides that failure to provide the required disclosure form will constitute a violation under the MLBA and the District of Columbia

Consumer Protection Procedures Act (CPPA). Under the MLBA, penalties include administrative and civil sanctions as well as a right to bring an action for damages, including attorneys' fees. Under the CPPA, penalties include administrative sanctions, civil actions and private rights of action, under which a complainant may make a claim for, among other things, treble damages and punitive damages. However, significantly, there does not appear to be any assignee liability or validity of loan issues for a violation of the Act.

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