

# Legislative Analysis



## ALLOW PUBLIC OFFICIAL TO CONTEST FRAUDULENT FINANCING STATEMENT

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**House Bills 5934 and 5935 as introduced**

**Sponsor: Rep. Andy Coulouris**

**Committee: Banking and Financial Services**

**First Analysis (6-26-08)**

**BRIEF SUMMARY:** The bills would create an expedited process by which a public officer could terminate a fraudulent financing statement filed against the public officer or his or her spouse and make filing a false affidavit of fraudulent financing statement a felony.

**FISCAL IMPACT:** The bills would have some fiscal implications for state and local governments. A more detailed discussion follows later in the analysis.

### **THE APPARENT PROBLEM:**

Apparently, it is not uncommon for one individual to fraudulently claim that another person owes him or her money. If an individual files a false or fraudulent financing statement in order to injure another person by falsely identifying that person as a debtor, the person's credit record can be affected.

Public Act 212 of 2004, enrolled House Bill 5148, amended the Uniform Commercial Code to, among other things, require the secretary of state to provide written notice of the filing of a financing statement filed with that office to any debtor identified in the statement, if the debtor is an individual. Public Act 212 also made it a felony for a person to knowingly or intentionally file a false or fraudulent financing statement with the secretary of state, punishable by imprisonment for not more than five years or a fine of not more than \$2,500, or both. Those falsely identified in a financing statement can file a civil action seeking equitable relief and damages, and the court can, if the filer were convicted of the violation, order the false record ineffective.

Reportedly, the civil action can take months to a year or more to complete, and the process to have the false lien removed can't be started until after the fraudulent filer was convicted. Meanwhile, fraudulent liens may remain on a person's credit record, making it difficult to qualify for loans to purchase a car or home, or even open a new cell phone account. Because of their high profile positions, judges and other public officials are very visible targets for a person who feels a public employee "done him or her wrong." Because some public officials may have multiple fraudulent financial statements filed against them, legislation has been offered to create a process by which the termination of such statements filed against public employees could be expedited.

## ***THE CONTENT OF THE BILLS:***

According to the Department of State, a "financing statement" is a statement filed to perfect a security interest and provide a public notice of a security agreement between a debtor and a secured party. The financing statement describes certain types of collateral or property used as surety for the security agreement. In general, most financial statements are filed with the office of Secretary of State; in some instances, a filing is filed with a county register of deeds.

House Bill 5934 would add a new section to the Uniform Commercial Code (MCL 440.9501a) to create an expedited process by which a financing statement naming a public officer or his or her spouse as a debtor could be terminated. "Public officer" would mean an individual who is or was employed by the state, the federal government, or a local unit of government (which would include a county, township, city, village, court, or other authority).

Affidavit of false filing. Under the bill, when a public officer or his or her spouse received a notice from a filing office that a financing statement as described above had been filed against him or her, the public officer or spouse could file an affidavit with the filing office stating that the financing statement was fraudulent. The filing office would then be required to terminate the financing statement effective on the date the affidavit had been filed. A fee could not be charged for filing an affidavit. The secretary of state would be required to adopt and make available a form affidavit to give notice of fraudulent filing statement. (Presumably, the notice referred to would be the notice required under the provisions of Public Act 212 of 2004 required to be sent by the secretary of state to individuals named in a financing statement that had been filed with the secretary of state.)

Notice of termination. A filing office would have to send notice of the termination of a financing statement to the filer of the financing statement advising the filer that the statement had been terminated. The filing office could not return any filing fee paid for filing the financing statement, even if the financing statement had been terminated.

Reinstatement of financial statement. If the filer believed in good faith that the statement had been legally filed and was not fraudulent, the filer could file an action to reinstate the financing statement. If the financing statement named an employee of the state or his or her spouse, the action would be filed in the Ingham County Circuit Court. For all others, the action would be filed in the circuit court for the county in which the public officer or spouse resided.

If the court determined that the financing statement should be reinstated, the court order reinstating the statement would be filed with the filing office. The reinstatement would be effective as notice to bona fide purchasers or creditors only after the order was filed.

However, if the court determined the financing statement to be invalid, the filer of the statement would have to pay the costs and expenses incurred by the public official or spouse in defending the action.

Penalty for filing false affidavit. An individual who filed a false or fraudulent affidavit would be guilty of a felony punishable by imprisonment for not more than five years, a fine of \$2,500, or both.

House Bill 5935 would amend the Code of Criminal Procedure (MCL 777.14g) to specify that filing a false affidavit of fraudulent financing statement would be a Class E felony against the public trust with a maximum term of imprisonment of five years. The bill is tie-barred to House Bill 5934.

### ***BACKGROUND INFORMATION:***

Senate Bill 1236 addresses similar issues, but takes a different tack. Among other things, the bill would allow a filing office to refuse to accept a record for filing or recording under several circumstances, including if the filing office has reasonable cause to believe the record was materially false or fraudulent or the record was intended for an improper purpose such as to hinder, harass, or otherwise wrongfully interfere with a person.

The bill has been referred to the Senate Judiciary Committee, but has not yet had a hearing.

### ***FISCAL INFORMATION:***

House Bill 5934 would have minimal fiscal impact on the Department of State. Any impact would be related to increased administrative costs stemming from the bill's requirement that the secretary of state adopt and make available a form affidavit for public officers or their spouses to use to be able to give notice of a fraudulent filing statement.

Regarding the impact to the judiciary by House Bill 5934, there would be an indeterminate, if not negligible, fiscal impact on state or local government as any fiscal impact would depend on the number of court proceedings emanating from this amendment.

The bills' impact on state and local correctional systems would depend on how they affected the numbers of felony convictions and severity of sentences. There are no data to indicate how many people might be convicted under the bills. The offense to be created by HB 5934 would be a Class E offense against the public trust. Under sentencing guidelines, the recommended range for an offender's minimum sentence for a Class E offense varies from 0 to 3 months, for which a local sanction is required, to 17 to 30 months, for which a prison sentence is required.

To the extent that the bills increased the number of offenders sentenced to prison or to felony probation supervision, the state could experience increased costs. Average appropriated costs of prison incarceration are roughly \$32,000 per prisoner per year, a figure that includes various fixed administrative and operational costs. Costs of parole and probation supervision average about \$2,000 per supervised offender per year. To the extent that more offenders were sentenced to jail, affected counties could experience increased costs; jail costs vary by county.

Any increase in penal fine revenues could benefit local libraries, which are the constitutionally designated recipients of those revenues.

### ***ARGUMENTS:***

#### ***For:***

Several Saginaw County judges have reported multiple fraudulent UCC liens filed against them by individuals sentenced in their courts. One judge reported that he was unable to finance the purchase of a new car because of the false liens and resulting havoc to his credit score that the false liens created.

Even though Public 212 of 2004 allows a person to have the false lien terminated, it requires hiring an attorney, court costs, and time to resolve. Plus, the process is only triggered if the person who filed the false lien is convicted of doing so. Because of the nature of their jobs, public officials often make easy targets for those who feel they need to get even with the "system," and so may have multiple false liens filed against them.

House Bill 5934 would create an easy, efficient, and inexpensive way for a judge or other public officer to have false liens terminated. The bill would also create a harsh penalty for filing a falsely claiming that a financial statement had been fraudulently filed: up to five years in prison and/or a flat fine of \$2,500.

#### ***Against:***

Reportedly, the bills were offered to assuage the "paper terrorism," as one judge called it, that several judges have faced in recent years by disgruntled people who had been sentenced in their courts. However, the definition of "public officer" contained in House Bill 5934 would not include judges or elected or appointed public officials. This oversight should be corrected.

Moreover, it could be difficult, if not impossible, for county register of deeds offices and the secretary of state (SOS) to recognize who is or had been at one time a state or municipal employee (or the spouse of a current or past employee) so that they would know who could lawfully file an affidavit to have the false lien terminated. Some, including the SOS, believe that requiring the liens to be automatically terminated upon receipt of an affidavit, without further investigation into the merits of the affidavit's validity, could result in many legitimate liens being terminated. Though the bill would allow a lien to be reinstated, the filer of the lien would have to mount a court challenge. Though the bill does include a felony penalty, it could be argued that if the amounts in

question were small, the temptation would be greater for the public officer or spouse to deny a legitimate claim, believing the filer to be less likely to pursue the matter in light of the additional court costs to have the claim reinstated.

Perhaps a better approach would be to blend elements of House Bill 5934 with some provisions of Senate 1236. For instance, the Senate bill would apply to all individuals, not just those who are or have been employed by the state or local governments. Further, SOS, county clerks, and register of deeds employees should be given proper training and authority to recognize and reject clearly fraudulent filings. Filings should not be terminated automatically because a person files an affidavit claiming the lien to be a fake. The filing offices should be required to make some initial investigations or collect additional documentation to verify the validity of an affidavit. Doing so would enable the penalty for filing a false affidavit to be a true deterrent, as the temptation to deny a lien would be greatly lessened.

What is clear is that a more efficient and less painful manner to thwart false liens is needed. House Bill 5934 as introduced, though, may not be the solution needed.

#### ***POSITIONS:***

A representative of the Michigan Judges Association testified in support of the bills. (6-25-08).

A representative of the Oakland County Circuit Court testified in support of the bills. (6-25-08)

A representative of the Saginaw County Clerk's Office indicated support for the bills. (6-25-08)

The Oakland County Executive indicated support for the bills. (6-25-08)

The Secretary of State Office indicated support for the bills' concept, and could support the bills with amendments. (6-25-08)

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■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.