

**BARRIERS TO THE EXERCISE OF THE  
FIDELITY INSURER'S SUBROGATION  
RIGHTS WITH EMPHASIS ON CONFLICTS  
INVOLVING FEDERAL  
FORFEITURE STATUTES**

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When a fidelity insurer pays a loss, it is subrogated to its insured's rights against those responsible for the loss. The most obvious target of a subrogation claim is any wrongdoer whose dishonest or fraudulent act caused the loss. The wrongdoer, however, sometimes cannot be found and often cannot pay. As a consequence, a great deal of the law in this area is devoted to trying to place the loss on innocent third parties who may be liable to the insured by contract or otherwise. The most common example is a subrogation claim against a bank which has honored checks which the wrongdoer forged or altered.

### SCOPE OF THIS ARTICLE

As used in this article, a barrier to exercise of the insurer's subrogation rights<sup>1</sup> is a statute, legal doctrine or defense which prevents the subrogated insurer from successfully exercising its insured's rights. The three specific areas discussed are recent cases on the Compensated Surety Defense or Superior Equities Doctrine, subrogation claims against the insured's own officers and directors, and the impact of federal asset forfeiture statutes.

### THE COMPENSATED SURETY DEFENSE REVISITED

Even in the absence of a legal assignment or a right of conventional subrogation in its Policy or Bond,<sup>2</sup> an insurer which fully compensates its insured is equitably subrogated to its insured's rights. Equitable subrogation, as its name implies, is a creature of equity to assure that a loss ultimately falls on the party who in good conscience should pay it. It does not depend on the contract between the parties or even on their desires or intentions, and almost by definition it requires the court to balance the equities of the respective litigants and determine which should bear the loss involved. In *District of Columbia v. Aetna Insurance Company*, 462 A.2d 428 (D.C. 1983) the court, quoting from *Memphis & L.R.R. Co. v. Dow*, 120 U.S. 287, 7 S.Ct. 482, 30 L.Ed. 595 (1887), described equitable subrogation as follows:

... we adopt the view that, "the right of subrogation is not founded on contract. It is a creature of equity; is enforced solely for the purpose of accomplishing the ends of substantial justice; and is independent of any contractual relations between the parties".

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1. The paper addresses conventional subrogation and legal assignments as well as equitable subrogation. See discussion of the distinctions at pages 3-4.

2. Virtually all modern insurance policies and fidelity bonds include a conventional subrogation provision and forbid the insured to do anything after discovery of the loss to prejudice the insurer's subrogation claim. If the insurer does not introduce the Policy into evidence, however, it can still fall back on the doctrine of equitable subrogation. See, e.g., *American Security Bank, N.A. v. American Motorists Insurance Company*, 538 A.2d 736 (D.C. 1988).

If a fidelity insurer relies only on equitable subrogation, therefore, there is some logical basis for the Compensated Surety Defense which denies recovery to the subrogated insurer unless it can show that its equities are superior to those of the third party against whom the claim is asserted. That is, if the Defense applies, the subrogated insurer cannot recover from an innocent third party even though its insured would prevail against the third party. The compensated surety is held not to have superior equities unless it can show that the third party was negligent or otherwise at fault in causing the loss. Since equitable subrogation is intended to place the loss on the party which in equity and good conscience should pay it, there is some logic in balancing the equities of the contending parties to determine which will ultimately bear the loss.<sup>3</sup>

There is no logical reason, however, to apply the Compensated Surety Defense or Superior Equities Doctrine to bar an insurer which is proceeding by conventional subrogation or assignment. The reasoning of courts which have reached that result simply does not stand up to rigorous analysis. For example, in *Bank of Fort Mill v. Lawyers Title Insurance Corporation*, 268 F.2d 313 (4th Cir. 1959)<sup>4</sup> the court reasoned that when the insurer paid its insured, the insured's claim was extinguished and, therefore, there was nothing for it to assign. Such reasoning would prevent any commercial assignment for consideration since payment for the assignment would "destroy" the very thing being assigned.

The leading case applying the Superior Equities doctrine to assignment or conventional subrogation is *Meyers v. Bank of America National Trust & Savings Assn.*, 77 P.2d 1084 (Cal. 1938) which held that the insurer's assignment did not give it any greater rights than it already had through equitable subrogation.

The result in *Meyers* has been criticized by commentators and rejected by more recent decisions from other states. O'Malley, "Subrogation against

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3. There are, of course, also logical arguments against applying the Compensated Surety Defense to even equitable subrogation claims, and a number of States have rejected it outright. See, for example, *Standard Accident Insurance Co. v. Pellacchia*, 104 A.2d 288 (N.J. 1954) and *Federal Insurance Company v. Toiyabe Supply Co.*, 409 P.2d 623 (Nev. 1966). Other courts have questioned its applicability in cases governed by the Uniform Commercial Code which has, in effect, already balanced the equities involved and established a clear, bright line allocation of the risk of loss. See, for example, *Cumis Insurance Society, Inc. v. Girard Bank*, 522 F. Supp. 414 (E.D. Pa. 1981) and the concurring opinion in *National Union Fire Insurance Company of Pittsburgh, Pa. v. The Riggs National Bank*, 5 F.3d 554 (D.C. Cir. 1993). On the other hand, recent proposed amendments to the UCC introducing comparative negligence concepts somewhat undercut the later argument.

4. The Fourth Circuit purported to follow South Carolina law, but the later case of *South Carolina National Bank v. Lake City State Bank*, 164 S.E.2d 103 (S.C. 1968) casts doubt on the *Bank of Fort Mill* holding.

Banks on Forged Checks” 51 *Cornell Law Quarterly* 441 (1966) states at pp. 458-459:

Where there is a firm and apparently irrevocable commitment to the paid surety defense, such as in California, the reluctance to permit avoidance of the defense by a contract of assignment is understandable. And yet, it is unquestioned that the right possessed by the insured against the bank is legally assignable to anyone. In view of this fact, it is difficult to comprehend why a distinction is made in some jurisdictions to the effect that a paid surety must take the assignment subject to a defense which could not be interposed against any other assignee.

In *Liberty Mutual Insurance Company v. Thunderbird State Bank*, 555 P.2d 333 (Ariz. 1976) the Arizona Supreme Court, sitting *en banc*, reversed the trial and intermediate appellate courts. The case involved a loss caused when the Branch Manager of the Charles Bruning Company forged endorsements and cashed checks made payable to Bruning. Liberty Mutual, as the fidelity insurer of Bruning, paid the loss caused by the Branch Manager's dishonesty and took an assignment of Bruning's rights. Thunderbird was the bank in which the checks were deposited. The Arizona Supreme Court held at 555 P.2d 336-338.

In the instant case, if we followed Meyers, *supra*, Liberty's right under the assignment would be dependent upon its right as a subrogee and not as an assignee. We believe, however, that Liberty is entitled to recovery under the assignment regardless of its right as a subrogee.

Bruning initially had a valid cause of action against Thunderbird. As a general rule, any claim that would survive the death of the plaintiff may be assigned. *Employers Casualty Co. v. Moore*, 60 Ariz. 544, 142 P.2d 414 (9143) (personal injury actions do not survive and thus are not assignable). And the existence of an equitable right of subrogation is logically irrelevant to the question of whether a party may transfer, by assignment, an otherwise assignable claim.

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Having decided that the claim could be assigned and that Liberty may sue in law on the contract, it follows that Thunderbird does not have available the equitable “compensated surety defense.”

We recognize that the rule imposing liability for the face amount of a check paid over a forged endorsement upon an intermediate collecting bank is harsh, and we are reluctant to extend such liability. However, at the same time, we see no reason why Thunderbird should be relieved of its unquestioned liability merely because the principal plaintiff, Bruning, took the precaution of insuring itself against the risk of loss. Put another way, but for the contract between Bruning and Liberty, Thunderbird would clearly have been liable for the amount of the checks to Bruning; it therefore suffers no prejudice when that liability is shifted from Bruning to Liberty under the terms of the contract between those two parties.

Liberty may therefore sue as an assignee of Bruning's claim against Thunderbird, and is not required to demonstrate superior equities before it can recover.

In *First National Bank of Atlanta v. American Surety Co.*, 30 S.E. 2d 402 (Ga. App. 1944) a dishonest employee forged endorsements on checks. The employer's fidelity insurer reimbursed the employer and received an assignment of the employer's rights. The court held at 30 S.E. 2d 407:

While there are many cases dealing with the doctrine of subrogation, and some confusion and conflict in the decisions of the various state and federal courts, in this State an action based on conventional subrogation of the type presented by this case, clearly established by an agreement reduced to writing or otherwise shown, in which no equitable relief in aid of the claim is prayed, is an action at law, and is not controlled by the principles appertaining to an action in equity, and the conventional subrogee in this action did not have the burden of showing the superior equity as against the defendant in order to recover.

A recent case which squarely considered the question as a matter of first impression and held that the Superior Equities Doctrine does not apply to a fidelity insurer proceeding by conventional subrogation or assignment is *National Union Fire Insurance Company of Pittsburgh, Pa. v. The Riggs National Bank*, 646 A.2d 966 (D.C. 1994).<sup>5</sup> The Court held:

We agree with the Arizona Supreme Court and are persuaded to follow the line of cases holding that the superior equities doctrine, although applicable to equitable subrogation claims, has no application in cases of conventional subrogation and assignment. Conventional subrogation and assignment are based on contractual agreements between parties and do not derive their validity from principles of equity. Where the bank would be liable to the depositor and the depositor agrees to assign or contract its rights to its insurer, we see no sound reason for allowing the bank to prevail against the insurer. Enforcing the agreement does not saddle the bank with any new or unexpected liability. Further, it will carry out the intent of the insurance contract, under which the insurer has effectively agreed to assume ultimate liability only where the law otherwise would place that liability upon the insured. Because the assignee stands in the same position as the assignor, the bank's liability with or without the assignment will depend upon its duty to the depositor.

A State by State review of the Compensated Surety Defense and its application to fidelity insurers proceeding by conventional subrogation or assignment is well beyond the scope of this paper,<sup>6</sup> but in any jurisdiction

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5. The case was certified from the United States Court of Appeals for the District of Columbia Circuit for decision on a question of controlling District of Columbia law. See 5 F.3d 554 (D.C. Cir. 1993).

6. For such a review see James A. Knox, "Subrogation Rights in Fidelity Cases" 12 *The Forum* 348 (1976). A more recent article is Gregory R. Veal, "Subrogation: The Duties and Obligations of the Insured and Rights of the Insurer Revisited," 28 *Tort & Ins. Law Journal* 69 (1992).

where the Courts will consider the competing arguments on their merits, the *Liberty Mutual v. Thunderbird State Bank* and *National Union v. Riggs* decisions should provide persuasive support for the insurer's position.

#### SUBROGATION AGAINST THE INSURED'S OFFICERS AND DIRECTORS

Negligence by the insured which contributes to an employee's successful perpetration or concealment of his or her dishonest or fraudulent scheme is ordinarily not a defense to a fidelity insurer. The courts have understandably been reluctant to allow the insurer to indirectly avoid the risk it was compensated to assume by claiming a subrogation right against the insured's allegedly negligent officers or directors who did not personally benefit from the dishonest acts.

Unfortunately, the theory chosen to reject such a claim is often the Compensated Surety Defense or Superior Equities Doctrine. These cases, therefore, appear to give credence to the argument that even a conventional subrogee or assignee has to prevail in a balancing of equities.

An example of this phenomenon is *Dixie National Bank v. Employers Commercial Union Ins. Co.*, 463 So.2d 1147 (Fla. 1985)<sup>7</sup> in which the Court stated:

We agree with appellees and hold that, in Florida in an action by a fidelity bond insurer against the directors of a bank and their insurer for the directors' negligence in failing to prevent embezzlement losses, in order to recover, the fidelity insurer is required to establish superior equities as between the fidelity insurer and the directors and their insurer where the fidelity bond insurer has obtained rights against the directors through legal or equitable subrogation and also has obtained a written assignment from the bank.

Other cases reaching similar results include, *First National bank of Columbus v. Hansen*, 267 N.W.2d 367 (Wis. 1978); *Home Indemnity Company v. Shaffer*, 860 F.2d 186 (6th Cir. 1988); and *Employers Insurance Co. of Wausau v. Doonan*, 664 F. Supp. 1220 (C.D. Ill. 1987), but compare *Manufacturers Bank and Trust Co. v. Transamerica Insurance Co.*, 568 F. Supp. 790 (E.D. Mo. 1983).

Fidelity insurers ought to recognize that they are not going to prevail against their insured's negligent but honest officers or directors and not bring such claims. In their zeal to dismiss the claims, courts are tempted to make bad law, or at least bad *dicta*, which will come back to haunt the insurers in other, meritorious cases.

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7. The case was certified for decision on questions of Florida law by the U.S. Eleventh Circuit Court of Appeals. See 759 F.2d 826 (11th Cir. 1985).

FEDERAL ASSET FORFEITURE AND  
THE SUBROGATED FIDELITY INSURER

The obligatory starting point for discussions of federal asset forfeiture is *Exodus* 21:28, “if an ox gore a man or a woman, that they die, the ox shall be surely stoned, and its flesh shall not be eaten.” This passage embodies the concept that the instrumentality of the wrongful act is itself guilty and forfeited. Neither the estate of the victim nor the State received the flesh of the ox, and the net result was a religious atonement by the ox with the desirable side effect of giving owners of oxen a reason to prevent their animals from goring people.

The Kings of England, never ones to overlook sources of revenue, made two improvements to the Biblical scheme. First, the assets of certain criminals were forfeited to the Crown or to the criminal’s lord. Second, all of the selected criminals’ property was forfeited not just the chattel or real property used in the commission of the offense.

The American colonists disliked the King’s forfeiture scheme and particularly the forfeiture of all of a person’s real and personal property to the Crown upon his or her conviction of treason. As a result, the Constitution at Art. III, § 3, cl.2 prohibits forfeiture for treason “except during the life of the person attainted.” Forfeiture was nevertheless used as a means to enforce the custom laws (a crucial source of federal government revenue prior to the income tax) and to hamper piracy and the slave trade.

The theory of civil forfeiture remains that contraband or property used in commission of a crime is itself guilty. The fact that the owner of the property may be entirely innocent is not relevant to the guilt of the property. In *Calero-Toledo v. Pearson Yacht Leasing Co.*, 416 U.S. 663, 94 S.Ct. 2080, 40 L.Ed. 2d 452 (1974) the Court rejected a constitutional challenge to forfeiture of a leased boat and rationalized that:

To the extent that such forfeiture provisions are applied to lessors, bailors, or secured creditors who are innocent of any wrongdoing, confiscation may have the desirable effect of inducing them to exercise greater care in transferring possession of their property.

The Civil forfeiture action is theoretically *in rem* against the guilty property. As applied to goods on which custom duties were evaded or a boat used in smuggling, for example, there is a logic to this theory. In recent years, however, federal asset forfeitures have expanded tremendously to the point that the United States Court of Appeals for the Second Circuit in *United States v. Statewide Auto Parts, Inc.*, 971 F.2d 896 (2nd Cir. 1992) concluded:

We continue to be enormously troubled by the government’s increasing and virtually unchecked use of the civil forfeiture statutes and the disregard for due process that is buried in those statutes.

The political explanation for this expansion is that asset forfeiture is perceived as a key element in combating drug dealing, money laundering and related crimes. Congress and even the Courts are going to show little sympathy for civil due process arguments presented by drug dealers or those they have corrupted. Congress has consistently expanded the reach of asset forfeiture to the point where it has become a significant source of revenue for federal law enforcement agencies.

The crimes for which at least some type of federal asset forfeiture is available, however, now include mail and wire fraud affecting a financial institution, bank fraud, and loan application fraud. Virtually any conduct which gives rise to a Financial Institution Bond loss could be made the predicate of an asset forfeiture. For example, 18 U.S.C. § 981 provides for the civil forfeiture of any property:

... which constitutes or is derived from proceeds traceable to a violation of section ... 1344 of this title or a violation of section 1341 or 1343 of such title affecting a financial institution.<sup>8</sup>

Section 1344 of Title 18 is the Federal Bank Fraud statute and states:

Whoever knowingly executes, or attempts to execute, a scheme or artifice—

- (1) to defraud a financial institution; or
- (2) to obtain any of the moneys, funds, credits, assets, securities, or other property owned by, or under the custody or control of, a financial institution, by means of false or fraudulent pretenses, representations, or promises;

shall be fined not more than \$1,000,000 or imprisoned not more than 30 years, or both.

The property subject to forfeiture is no longer limited to something used in commission of the crime. In many cases, the proceeds of the crime or property traceable to those proceeds can be forfeited.<sup>9</sup> There would probably be a basis to seize virtually any significant asset owned by the dishonest employee or bond principal.

The Government, and to a lesser extent a claimant, can choose among administrative, civil and criminal forfeiture. Each has its own procedures and controlling law, but each also has certain elements in common. First, the Government seizes the property and holds it while the merits of the

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8. A list of 32 additional criminal statutes is omitted from this quotation. Sections 1341 and 1343 are the mail and wire fraud statutes which allow federal criminalization of virtually any commercial crime since the mail or telephone lines are inevitably used in some way.

9. See 18 U.S.C. § 981 quoted above. *United States v. 92 Buena Vista Ave*, \_\_\_ U.S. \_\_\_, 113 S.Ct. 1126, 122 L.Ed.2d 469 (1993) discusses the steady expansion of categories of property subject to forfeiture.

dispute are resolved. The seizure can be *ex parte* and, in exigent circumstances, through governmental self help.

Second, in judicial forfeiture proceedings the evidentiary and procedural burdens on the Government are minimal and those on a rival claimant are onerous. Once the Government demonstrates probable cause<sup>10</sup> to believe the property is subject to forfeiture, the burden shifts to the claimant to demonstrate by a preponderance of the evidence that the property is not forfeitable. In *United States v. Daccarett*, 6 F.3rd 37 (2nd Cir. 1993) the Court stated:

Judge Weinstein observed that the structure of the civil forfeiture states is “inherently unfair to claimants.”... While we also might question the wisdom of forcing the owner of the seized property to prove the property is “innocent”, rather than making the government prove the property is “guilty”, the constitutionality of congress’s allocation of the burdens of proof in forfeiture cases has been upheld... . We therefore stress the need for courts to ensure that what little due process is provided for in the statutory scheme is preserved in practice.

In administrative proceedings, the Government has virtually unreviewable discretion to dispose of a petition for mitigation or remission. The Courts can compel the responsible official to consider a petition on its merits but will not review the official’s exercise of discretion in ruling on it.

From the point of view of the subrogated insurer, however, the Government’s ability to seize assets quickly and retain them throughout the forfeiture proceeding is not necessarily bad. It is better to have the assets in the hands of the Government than those of the wrongdoer. The real question is whether, as a practical matter, the insurer will be able to get the assets back from the Government. This turns less on procedural niceties and more on the exceptions to the Government’s extremely broad forfeiture powers. As a practical matter, the two key aspects of forfeiture for the subrogated insurer are the “innocent owner” exception and administrative petitions for mitigation and remission.

#### THE INNOCENT OWNER EXCEPTION<sup>11</sup>

18 U.S.C. § 981 (Civil Forfeiture) provides at paragraph (a)(2):

No property shall be forfeited under this section to the extent of the interest of an owner or lienholder by reason of any act or omission established by that owner or lienholder to have been committed without the knowledge of that owner or lienholder.

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10. Probable cause is both a lenient standard and can be based on hearsay or other evidence not normally admissible.

11. For a general discussion of the innocent owner’s rights, see Michael F. Zeldin and Jane W. Moscovitz, “Innocent Third Parties in Federal Forfeiture Proceedings, What Are Their Rights”, 8 *Criminal Justice* 11 (1993).

21 U.S.C. § 881(a)(6) (Controlled Substance forfeitures) states:

...that no property shall be forfeited under this paragraph, to the extent of the interest of an owner, by reason of any act or omission established by that owner to have been committed or omitted without the knowledge or consent of that owner.

18 U.S.C. § 982 (Criminal Forfeiture) provides at subparagraph (b)(1) that property subject to forfeiture shall be governed by certain sections of 21 U.S.C. § 853 (which deals with forfeiture following convictions for certain drug offenses) including subparagraph (n)(6) which states:

If, after the hearing, the court determines that the petitioner has established by a preponderance of the evidence that—

(A) the petitioner has a legal right, title or interest in the property, and such right, title or interest renders the order of forfeiture invalid in whole or in part because the right, title, or interest was vested in the petitioner rather than the defendant or was superior to any right, title or interest of the defendant at the time of the commission of the acts which gave rise to the forfeiture of the property under this section; or

(B) the petitioner is a bona fide purchaser for value of the right, title, or interest in the property and was at the time of purchase reasonably without cause to believe that the property was subject to forfeiture under this section;

the court shall amend the order of forfeiture in accordance with its determination.

In the absence of a statutory innocent owner exception, an owner could still try to meet the Constitutional test of *Calero-Toledo v. Pearson Yacht Leasing Co.*, *supra*. which states at 416 U.S. 690 that it would be difficult to reject the Constitutional claim of an owner:

who proved not only that he was uninvolved in and unaware of the wrongful activity, but also that he had done all that reasonably could be expected to prevent the prescribed use of his property.

A fidelity insurer, of course, is unlikely to be a lienholder or itself the owner of the seized property. The insurer will have to claim by subrogation to its insured's rights and be subject to any defenses which could have been asserted against the insured's claim. The insurer will have to prove that the insured was the true owner of the seized property and did not know of or consent to the wrongful acts or did not have cause to believe the property was subject to forfeiture or did all that it reasonably could to prevent the illegal use of the property. It is important to note that there is no protection for an unsecured creditor of the wrongdoer.<sup>12</sup> The insured will have to have

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12. For an extended discussion of the impact of asset forfeiture on commercial creditors, see Steven L. Schwarcz and Alan E. Rothman, "Civil Forfeiture: A Higher Form of Commercial Law?" 62 *Fordham Law Review* 287 (1993).

ownership of the seized property or a lien on it. The further the property is removed from what was actually stolen the more difficult it will be for the insurer to prove that it is an owner or lienholder as opposed to a mere unsecured creditor.

#### ADMINISTRATIVE PETITIONS FOR MITIGATION OR REMISSION

Even the money-hungry English Kings tempered their harsh forfeiture laws by allowing the owner of the stolen property to file a writ of restitution to recover his property after it had been forfeited by the thief. Ever since 1790, the United States has provided for administrative remission or mitigation of statutory forfeitures.<sup>13</sup> The current statutory basis for administrative relief<sup>14</sup> is codified as part of the customs laws at 19 U.S.C. § 1618 which states, in part:

Whenever any person interested in any vessel, vehicle, aircraft, merchandise, or baggage seized ... files with the Secretary of the Treasury ... before the sale of such vessel, vehicle, aircraft, merchandise, or baggage a petition for the remission or mitigation of such fine, penalty, or forfeiture, the Secretary of the Treasury, ... if he finds that such fine, penalty, or forfeiture was incurred without willful negligence or without any intention on the part of the petitioner to defraud the revenue or to violate the law, or finds the existence of such mitigating circumstances as to justify the remission or mitigation of such fine, penalty, or forfeiture, may remit or mitigate the same upon such terms and conditions as he deems reasonable and just.

Both the Department of Justice and the Treasury Department have published Regulations controlling the submission of petitions for remission (a complete forgiveness) or mitigation (a reduction) of forfeitures. The Justice Department Regulations, 28 C.F.R. § 9.1., *et seq.*, establish procedures for filing petitions for remission or mitigation and state the following criteria for deciding whether to grant relief (28 C.F.R. § 9.5):

- (a) The Determining Official shall not consider whether the evidence is sufficient to support the forfeiture but shall presume a valid forfeiture.
- (b) *Remission.* The Determining Official shall not remit a forfeiture unless the petitioner establishes:
  - (1) That petitioner has a valid, good faith interest in the seized property as owner or otherwise; and

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13. *See Calero-Toledo v. Pearson Yacht Leasing Co., Supra.* at 416 U.S. 690, Note 27.

14. The other forfeiture statutes incorporate the customs authority to grant administrative relief by reference to 19 U.S.C. § 1602, *et seq.* but allow the Attorney General, Secretary of the Treasury, or Postal Service to exercise the authority for property seized by their agencies. *See, e.g.,* 18 U.S.C. § 981(d) and 21 U.S.C. § 881 (d).

(2) That petitioner had no knowledge that the property in which petitioner claims an interest was or would be involved in any violation of the law; and

(3) That petitioner had no knowledge of the particular violation which subjected the property to seizure and forfeiture; and

(4) That petitioner had no knowledge that the user of the property had any record for violating laws of the U.S. or of any State for a related crime; and

(5) That petitioner had taken all reasonable steps to prevent the illegal use of the property.

(c) *Mitigation.* In addition to having the discretionary authority to grant relief by way of complete remission of forfeiture, the determining official may, in the exercise of discretion, mitigate forfeitures of seized property. This authority may be exercised in those cases where the petitioner has not met the minimum conditions precedent to remission but where there are present other extenuating circumstances indicating that some relief should be granted to avoid extreme hardship. Mitigation may also be granted where the minimum standards for remission have been satisfied but the overall circumstances are such that, in the opinion of the determining official, complete relief is not warranted.

The Justice Department Regulations also recognize at § 9.6 that victims of the criminal activity and even general creditors can have an interest in the seized property and can qualify for remission or mitigation.

The Treasury Department Regulations, 19 C.F.R. § 171.0 *et seq.*, similarly provide guidelines for preparing a petition and information about what it should contain. They are less explicit about the criteria used to decide whether to grant relief but do state at § 171.13(g):

*Denial of relief.* The failure to furnish adequate evidence as required by this section may be a basis for denial of relief. Relief may also be denied to a petitioner who has met the applicable criteria, but with respect to whom remission would be inimical to the interests of justice.

The hallmarks of administrative relief from federal asset forfeiture are flexibility on the part of the Government, the requirement that the petitioner establish that it is innocent, was not negligent, and neither knew about nor could have prevented the criminal activity, and the complete insulation of the process from any meaningful judicial review. A claimant can choose to go to court and try to recover the property as an “innocent owner” or otherwise, but if he elects to seek administrative relief, he will not get judicial review of the result.

In actual practice, however, most of the agencies involved seem to recognize that the continued existence of the really extraordinary powers which they have under the forfeiture statutes depends on restraint in their dealing with innocent third parties. As long as the rejected claimants are criminals

or those in privity with criminals, the public and Congress are likely to continue to support forfeiture powers up to the permissible Constitutional limits. If those powers start to be used against truly innocent people, or as a revenue raising device, there is likely to be a groundswell of support for restrictions on the forfeiture weapons to the ultimate benefit of the criminals who are the intended targets.

### CONCLUSION

The subrogated insurer does not fit neatly into the innocent owner exceptions contained in the forfeiture statutes and may find minimal due process and judicial review are not particularly useful if the substantive law is stacked against its position. Heresy though it may be, the insurer is probably better off trying to work with the federal law enforcement agencies to use their extraordinary powers to seize the proceeds of the crime and assets traceable to those proceeds. The Government, after all, does not have to waste time with suits or judgments. It can seize on an *ex parte* showing of probable cause.

Once the assets are preserved, the insurer and insured can demonstrate to the federal authorities that the insured was neither culpable nor negligent and deserves return of the stolen property or the proceeds traceable to that property. If an administrative petition for remission or mitigation has to be filed, however, a claimant should be sure to make its case and provide a detailed explanation and supporting documents. There is only one real chance to make a record, and if a half-hearted letter is sent in, the agency can deny relief and close its file. The Government is under no obligation to help the claimant present its case.

Both civil forfeiture, which is conducted pursuant to the Admiralty and Maritime portion of the Federal Rules of Civil Procedure, and administrative forfeiture are replete with short deadlines which must be met on pain of losing any interest in the forfeited assets. As soon as the insurer or insured learns of any asset seizure, they need to investigate and be sure any necessary claims or petitions are timely filed. If that is done, however, there is at least a chance of a speedy, satisfactory conclusion. In a recent law review article<sup>15</sup>, the authors argue that the civil forfeiture statutes are inferior to the wonderful, equitable distributions and safeguards of the Bankruptcy Code. From the point of view of a subrogated insurer, the quick and cheap unreviewable decision of a Justice Department official is better than the endless waste of a bankruptcy proceeding in which whatever assets were available at the beginning are eaten up by the bankruptcy lawyers.

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15. Steven L. Schwarcz and Alan E. Rothman, *supra*. Note 12.

On paper, federal asset forfeiture is a real threat to the subrogated fidelity insurer since the wrongdoer's assets can almost certainly be seized by the Government before the insurer can settle with the insured and file suit. In actual practice, however, the Government has usually shown restraint and common sense when dealing with innocent claimants and the subrogated insurer may be better off in an administrative forfeiture proceeding to determine the disposition of seized assets than the alternatives of fraudulent concealment, judgment proof principals and wasteful bankruptcy proceedings.