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Notes

The Real Party Under Rule 17(a): The Loan Receipt and Insurers’ Subrogation Revisited

Suppose Jones is reading the latest issue of Exercise Today in her home in Minnesota, when she comes across an advertisement for the Uniflex Fitness Machine. Deciding she must own one, she calls the toll-free number to place an order. After taking her name and address, the voice at the other end of the telephone informs her that shipping will be arranged through Bob’s Shipping and Hauling based in Wisconsin. The voice then asks Jones if she would like to insure the shipment through America’s Largest Insurance Company. She answers affirmatively.

Weeks later, the Uniflex Fitness Machine arrives. Jones acknowledges receipt by signing the bill of lading. Upon opening the crate, she discovers the equipment is damaged. She submits a claim to America’s Largest. America’s Largest investigates the claim and discovers that Bob’s Shipping was negligent in handling the crate. Jones is not interested in recovering in tort from Bob’s Shipping; she just wants to receive her policy proceeds from America’s Largest. By paying on the policy, America’s Largest is subrogated to Jones’ claim against Bob’s Shipping; consequently, America’s Largest has standing to sue Bob’s Shipping for damaging Jones’ machine. When subrogation was first incorporated into the common law, America’s Largest could bring suit in Jones’ name so the complaint would read Jones v. Bob’s Shipping and Hauling.1 Under modern real-party-in-interest statutes, however, such as Federal Rule of Civil Procedure 17(a), America’s Largest must bring suit in its own name so the complaint reads America’s Largest Insurance Co. v. Bob’s Shipping and Hauling.2

1. See infra note 8 and accompanying text.
2. See FED. R. CIV. P. 17(a) (providing that “[e]very action shall be prosecuted in the name of the real party in interest”); infra note 10 and accompanying text.

In federal court, jurisdiction over this hypothetical case would be based on diversity of citizenship because Jones and Bob’s Shipping are citizens of different states. See 28 U.S.C. § 1332(a)(1) (1988); see also id. § 1332(c) (stating that
America's Largest prefers bringing suit in Jones' name to avoid any prejudice jurors may have against large insurance companies. To achieve this result under Rule 17(a), America's Largest and Jones enter into a loan receipt agreement, under which the payment due Jones on the policy is characterized as a loan. The loan is repayable only from amounts Jones recovers from Bob's Shipping, and America's Largest conducts the suit against Bob's Shipping for her. In other words, Jones recovers as if America's Largest had paid on the policy in the usual fashion, but because America's Largest technically loaned Jones the money, subrogation is not involved and the complaint will read Jones v. Bob's Shipping and Hauling.

This hypothetical illustrates the use of loan receipt agreements, which insurers commonly use to avoid bringing suit in their own names. Federal circuit courts disagree whether monies transferred under loan receipt agreements are loans, in which case the insurer need not be joined as a party in a subsequent lawsuit, or payments, in which case the insurer is subrogated to the rights of the insured and must be joined as a real party in interest in a subsequent lawsuit. The case law does little to reconcile this conflict, and indeed, creates confusion in this area of law.

This Note analyzes the various approaches used by courts in determining what effect should be given to the loan receipt device. Part I examines subrogation, Rule 17(a), and federal loan receipt case law. Part II critiques the analysis of the cases addressing the validity of loan receipts, and exposes the flaws in those decisions that have upheld the validity of the loan receipt. The Note concludes that the loan receipt agreement is invalid as a device to avoid joinder under Rule 17(a), except in

"a corporation shall be deemed a citizen of any State by which it has been incorporated and of the State where it has its principal place of business"). If America's Largest is incorporated in Wisconsin or has its principal place of business there, it lacks diversity of citizenship in its suit against Bob's Shipping. See id. § 1332(a)(1), 1332(c). This situation suggests another use of the loan receipt: to create diversity jurisdiction. By bringing suit in Jones' name, America's Largest could take advantage of Jones' Minnesota citizenship. For a more detailed discussion of the effect of the loan receipt on diversity jurisdiction, see Comment, The Loan Receipt and Insurers' Subrogation—How to Become the Real Party in Interest Without Really Lying, 50 Tul. L. Rev. 115, 123-24 (1975).

3. See infra notes 53, 67 (providing examples of loan receipt agreements).
5. See infra note 60.
the traditional context of insurer's contingent liability where
the insurer has a valid purpose for avoiding joinder other than
avoiding perceived jury prejudice against insurance companies.

I. LOAN RECEIPT AGREEMENTS AND THE REAL
PARTY IN INTEREST

A. Subrogation

At common law, when an insurer paid money to its insured
in satisfaction of an insurance claim, the subrogee (insurer)
could not bring suit against a party liable to its insured.6 Subro-
gation developed as an equitable doctrine7 that allowed the in-
surer to bring suit on its insured's claim against the wrongdoer
in the name of the insured.8

Real-party-in-interest statutes changed this process by
prohibiting parties lacking equitable interests to sue.9 If the in-
surer has already paid the insured's claim, only the insurer has
an interest in recovering from the wrongdoer. Thus, the in-
surer is the real party in interest.10 Under these statutes, when

6. Note, Subrogation: Proper Party Plaintiff in Action Against Tort-Fea-
7. Id. at 463. Some commentators argue that insurer subrogation is not
an appropriate equitable remedy. One writer points out that insurers receive
windfalls because insurance premiums are not reduced based on anticipated
Oxford J. Legal Stud. 416, 418, 422 (1985). He then outlines a statute
designed to abolish subrogation in most areas of insurance. Id. at 417, 436-38.
Another commentator argues that health insurers should be denied subroga-
tion in personal injury cases. Procaccia, Denying Subrogation in Personal In-
jury Claims: A Needed Change of Direction, 15 WM. & MARY L. REV. 93, 116
(1973). Courts should allow accident victims to recover from both the insurer
and the tortfeasor because a single insurance recovery only rarely achieves ac-
tual indemnity. Id. at 94.
L.Q. REV. 171, 171 (1949); see also 18 G. Couch, R. Anderson & M. Rhodes,
Couch Cyclopaedia of Insurance Law § 74:389, at 824 (rev. 2d ed. 1983) (al-
uding to "the common-law requirement of suit by the subrogated insurer
in the name of the injured claimant"). The insurer may still bring suit in the
name of the insured in jurisdictions lacking real-party-in-interest provisions
For a more detailed treatment of the history of subrogation, see Note,
supra note 6, at 463-66.
9. See, e.g., Fed. R. Civ. P. 17(a); see also Note, supra note 6, at 464-65.
(1949); 3A J. Moore & J. Lucas, Moore's Federal Practice ¶ 17.09[2-1]
(1959); 6A C. Wright, A. Miller & M. Kane, Federal Practice and Proce-
dure §1546 (1990). As one insurance expert explains:
Under modern statutes abolishing the distinction between law and eq-
a wrongdoer injures an insured, the insurer typically pays the
insured under the terms of the insurance policy. The insurer
then must use its own name if it elects to sue the wrongdoer on
its insured's claim.\textsuperscript{11}

B. \textbf{RULE 17(a)}

Federal Rule of Civil Procedure 17(a) is the federal real-
party-in-interest statute.\textsuperscript{12} It requires that "[e]very action shall
be prosecuted in the name of the real party in interest."\textsuperscript{13} Con-
sequently, in the typical situation in which an insurer pays pro-
cceeds to its insured under an insurance policy without
executing a loan receipt agreement, Rule 17(a) requires the in-
surer to sue in its own name.\textsuperscript{14}

\textsuperscript{11} Aetna, 338 U.S. at 381.
\textsuperscript{12} Rule 17(a) reads:

\begin{quote}
Every action shall be prosecuted in the name of the real party in interest. An executor, administrator, guardian, bailee, trustee of an
express trust, a party with whom or in whose name a contract has
been made for the benefit of another, or a party authorized by statute
may sue in that person's own name without joining the party for
whose benefit the action is brought; and when a statute of the United
States so provides, an action for the use or benefit of another shall be
brought in the name of the United States. No action shall be dis-
misssed on the ground that it is not prosecuted in the name of the real
party in interest until a reasonable time has been allowed after objec-
tion for ratification of commencement of the action by, or joinder or
substitution of, the real party in interest; and such ratification, join-
der, or substitution shall have the same effect as if the action had
been commenced in the name of the real party in interest.
\textsuperscript{13} \textit{Fed. R. Civ. P. 17(a)}.
\textsuperscript{14} \textit{Id.}
\end{quote}
Rule 17(a) helped to merge "law and equity by adopting


In Stouffer, the U.S. District Court for the Eastern District of Pennsylvania presented the typical argument for allowing ratification. See Stouffer, 88 F.R.D. at 337. The court looked to the purpose of Rule 17(a) as explained in the advisory committee notes and concluded that the main purpose behind Rule 17(a) is to protect the defendant from subsequent litigation. Id. Because ratification protects the defendant from subsequent litigation, the court reasoned that joinder of the insurer was unnecessary. Id.

The Stouffer court addressed only part of the advisory committee notes. After discussing the purpose behind allowing a reasonable time to join the real party before dismissing the action, the notes continue:

Modern decisions are inclined to be lenient when an honest mistake has been made in choosing the party in whose name the action is to be filed—in both maritime and nonmaritime cases. The provision should not be misunderstood or distorted. It is intended to prevent forfeiture when determination of the proper party to sue is difficult or when an understandable mistake has been made.

FED. R. CIV. P. 17(a) advisory committee note (1966) (emphasis added) (citations omitted). Whenever an insurer uses ratification to avoid suit in its own name, the insurer is not within the ambit of the advisory committee notes' "honest mistake" as to who is the real party in interest. A leading commentator on the federal rules concurs in this analysis. 6A C. WRIGHT, A. MILLER & M. KANE, supra note 10, § 1555, at 415 (the last sentence of Rule 17(a) applies only when "necessary to avoid injustice"). Wright, Miller and Kane criticize the Stouffer interpretation of "ratification," noting that the reference to 'ratification' in Rule 17(a) seems to be a carryover from the original draft of the sentence added in 1966, which was to apply only to certain maritime proceedings, and probably was intended to adopt the procedure in salvage actions by which nonparties seek their share of the recovered property. Nonetheless, some federal courts have interpreted the word to validate an arrangement by which the real party in interest authorizes the continuation of an action brought by another and agrees to be bound by its result, thereby eliminating any risk of multiple liability.

Id. at 417 (citing Southern Nat'l Bank, 317 F. Supp. at 1186-88; Urrutia Aviation, 406 F.2d at 770).

Some courts have paid attention to the advisory committee's intention to limit the scope of permissible substitution and relation back. See Crowder v. Gordons Transps., Inc., 387 F.2d 413, 418-19 (8th Cir. 1967) (allowing relation back when a reasonable basis existed for plaintiff's mistake in initially bringing the action in the name of the administratrix); cf. Pace v. General Elec. Co., 55 F.R.D. 215, 217, 219 (W.D. Pa. 1972) (allowing ratification rather than joinder of the insurers as real parties in interest when the defendant's motion was not seasonably made).

Commentators and courts have not addressed what seems to be the central issue within ratification: whether the ratification agreement can be revealed to the jury. If an insured is prosecuting an action for the benefit of its insurer pursuant to a ratification agreement, the complaint should presumably read Insured ex rel. Insurer v. Wrongdoer. Cf. Ingram ex rel. St. Paul Fire &
the rule of equity that the plaintiff should be the party with the
substantive right sought to be enforced." One policy reason
for adopting the rule in equity rather than the rule at law is
to recognize the equitable interest of the subrogee. The in-
surer should be forced to bring suit in its own name because
once it pays the insured, only the insurer has an interest in re-
covering the money paid. Suit in the name of the insurer thus
avoids the legal fiction that the insured always maintains a pec-
uniary interest in recovery from the alleged wrongdoer.

Commentators often cite two other policies supporting
Rule 17(a). The requirement that every action be prosecuted in
the name of the real party in interest enables the defendant to
avail itself of all evidence and defenses it would have against
the real party in interest. It also ensures finality of judg-
ment. These policy reasons appear in the Advisory Committee

Marine Ins. Co. v. Magnolia Petroleum, 112 F. Supp. 430, 431 (M.D. Tenn. 1953) (stating that in the absence of the loan receipt as an exhibit, the suit would proceed as an ordinary subrogation action). This would reveal the iden-
tity of the insurer as the real party in interest and thus make ratification a moot alternative to joinder or substitution. The last sentence of Rule 17(a) is more logically consistent under this interpretation. If the insurer controls the litigation, and if both the insurer and the insured have a pecuniary interest in the outcome of the litigation, the insurer should be joined. If the insurer con-
trols the litigation and only the insurer has a pecuniary interest in the outcome, the insurer should be substituted. Finally, if the insured controls the litigation but the insurer also has a pecuniary interest in the outcome of the litigation, the insurer could ratify commencement of the action. As long as the ratification agreement is reflected by appending "ex rel. Insurer" to the plain-
tiff insured's name, joinder, substitution, and ratification all will result in ident-
fication of the real party in interest. Thus, ratification would not be a loophole to avoid Rule 17(a).

15. Comment, supra note 2, at 118; see also 6 C. MILLER, CYCLOPEDIA OF
FEDERAL PROCEDURE § 21.09, at 462 (rev. 3d ed. 1988) (stating that Rule 17(a) is "a literal rescript of" former Federal Equity Rule 37, which required every action to be brought in the name of the real party in interest); Kessner, Federal Court Interpretations of the Real Party in Interest Rule in Cases of Subro-
gation, 39 Neb. L. Rev. 452, 453 (1960) (stating that "adoption of the rule was an acceptance of the equity doctrine that he who has the right is the person to pursue the remedy").

16. See supra text accompanying note 6.

17. See 3A J. MOORE & J. LUCAS, supra note 10, ¶ 17.09(2.—1), at 17-77
n.2.

18. E.g., Celanese Corp. of Am. v. John Clark Indus., 214 F.2d 551, 556
(5th Cir. 1954); 6 C. MILLER, supra note 15, § 21.10, at 463.

19. Finality of judgment — the protection of defendant from multiple suits arising from a single cause of action — is not relevant to this Note because "[w]here the insured, after receiving money from the insurer under a loan receipt transaction, recovers in an action from the alleged wrongdoer, the insurer is barred from bringing an independent action against the wrongdoer." 16 G. COUCH, R. ANDERSON & M. RHODES, supra note 8, § 61:87, at 161-62; see
on Rules' Notes to the 1966 Amendment to Rule 17(a).\textsuperscript{20}

Application of Rule 17(a) is complicated by the necessity of deciding whether to apply state or federal law in determining the real party in interest.\textsuperscript{21} This is a matter of some controversy.\textsuperscript{22} Although determination of the real party in interest is

\textit{also} Montana v. United States, 440 U.S. 147, 154 (1979) (stating that when a non-party assumes control of a party's litigation, the non-party is precluded from relitigating the claims litigated in the first action).

\textsuperscript{20} In explaining why "[n]o action shall be dismissed on the ground that it is not prosecuted in the name of the real party in interest until a reasonable time has been allowed . . . for . . . joinder . . . of [the] real party in interest[,]"

FED. R. CIV. P. 17(a), the advisory committee alluded to the policy behind adoption of the real-party-in-interest rule:

In its origin the rule concerning the real party in interest was permissive in purpose: it was designed to allow an assignee to sue in his [or her] own name. That having been accomplished, the modern function of the rule in its negative aspect is simply to protect the defendant against a subsequent action by the party actually entitled to recover, and to insure generally that the judgment will have its proper effect as res judicata.


\textsuperscript{21} See Erie R.R. v. Tompkins, 304 U.S. 64, 78 (1938).

\textsuperscript{22} Of course, federal courts must apply the appropriate state law to decide substantive issues, but procedural issues can be resolved by federal law. \textit{Id.} Thus, the issue is whether determination of the named plaintiff is a procedural or a substantive issue. The federal courts in the following cases involving loan receipts decided that determining the real party in interest is a substantive issue, and, accordingly, applied state law: Keystone Shipping Co. v. Home Ins. Co., 840 F.2d 181, 183 n.6 (3d Cir. 1988); McNeil Constr. Co. v. Livingston State Bank, 300 F.2d 88, 90 n.5 (9th Cir. 1962); Tyler v. Dowell, Inc., 274 F.2d 890, 894 (10th Cir.), \textit{cert. denied}, 363 U.S. 812 (1960); Childers v. Eastern Foam Prods., 94 F.R.D. 53, 55 (N.D. Ga. 1982); Stouffer Corp. v. Dow Chem. Co., 88 F.R.D. 336, 337 (E.D. Pa. 1980); See v. Emhart Corp., 444 F. Supp. 71, 73-74 (W.D. Mo. 1977); White Hall Bldg. Corp. v. Profaxray Div. of Litton Indus., 387 F. Supp. 1202, 1204 (E.D. Pa. 1974), \textit{aff'd} \textit{without opinion sub nom.} Quaglia v. Profaxray Div. of Litton Indus., 578 F.2d 1375, \textit{and aff'd without opinion}, 578 F.2d 1377 (3d Cir. 1978); Northern Assurance Co. of Am. v. Associated Indep. Dealers, 313 F. Supp. 816, 818 (D. Minn. 1970); Rosenfeld v. Continental Bldg. Operating Co., 135 F. Supp. 465, 470 (W.D. Mo. 1955); see \textit{also} E. Brooke Matlack, Inc. v. Walrath, 24 F.R.D. 263, 268 (D. Md. 1959) (recognizing that the real party in interest is determined by state law). In other cases involving loan receipts, the federal courts determined the real party in interest based, at least in part, on federal procedural law. \textit{See infra} note 60.

\textit{Keystone Shipping} illustrates the essential problem with the line of federal cases applying substantive state law. After noting that the \textit{insurers} are actually the real parties in interest, the federal district court looked to Pennsylvania law, which allowed suit in the name of the insured under a loan receipt. \textit{Keystone Shipping}, 940 F.2d at 183 n.6. The court concluded that Pennsylvania "insurance" law controlled; that is, suit in federal court would be in the name of the insured. \textit{Id.}

The \textit{Keystone Shipping} court did not actually apply Pennsylvania insurance or substantive law. Once the federal court acknowledges that the insurers are the real parties in interest, a state court's decision to allow prosecution
based on substantive state law, the determination of the party in whose name the action should be brought is a matter of federal procedural law.23 The right to subrogation thus arises in the name of the insured is a matter of state procedural law, not state insurance law. See, e.g., Robertson v. White, 113 F.R.D. 20, 23 (W.D. Ark. 1986); 6A C. Wright, A. Miller & M. Kane, supra note 10, § 1544, at 345. In other words, when state law gives one party a cause of action in the name of another party, federal courts recognize the cause of action but use federal law to determine the procedural issue of the party in whose name the action should be brought.

No state law should substantively provide that the insured is the real party in interest, because the insured retains no pecuniary interest in the litigation after issuance of a loan receipt. A state court's decision to allow the insurer to sue in the name of the insured is, therefore, inherently procedural. Even if state law does recognize the insured as the real party based on some non-pecuniary interest, the insurer's pecuniary interest would presumably require that the federal suit be in the names of both insured and insurer. Cf. United States v. Aetna Casualty & Surety Co., 338 U.S. 366, 381-82 (1949) (holding that in cases of partial subrogation — when the insurer has paid only part of the claim — suit should be in the name of both insured and insurer).

Distinguishing the federal procedural issue from the state substantive issue can sometimes produce astonishing results. In a 1983 case, the U.S. District Court for the Middle District of Alabama held that the insured was the real party in interest based on earlier Fifth Circuit decisions purportedly applying Alabama state law upholding loan receipt validity. Industrial Dev. Bd. v. Brown & Root, Inc., 99 F.R.D. 58, 59 (M.D. Ala. 1983) (citing Ketona Chem. Corp. v. Globe Indem. Co., 404 F.2d 181, 184 (5th Cir. 1968); Sanders v. Liberty Mut. Ins. Co., 354 F.2d 777, 778 & n.1 (5th Cir. 1968), aff'd in part without opinion, 735 F.2d 87 (11th Cir. 1986). But see infra note 66 (stating that Ketona found no Alabama law on point); Sanders, 354 F.2d at 778 & n.1 (although an Alabama case is at the end of a string citation of federal authority, the Sanders court did not purport to apply Alabama law). Since the Fifth Circuit decisions, Alabama Rule of Civil Procedure 17(a) had been modified to provide that the insurer is the real party despite the use of a loan receipt. Industrial Dev. Bd., 99 F.R.D. at 59. The district court determined that Alabama substantive law remained unchanged. The court reasoned that because the federal courts are not bound by state procedural law, the insured remained the real party in interest under Alabama law! Id. at 59-60.

Whether determination of the real party in interest should be based on federal procedural or state substantive law could be the subject of a separate Note. This Note focuses on the issue of whether courts should allow loan receipt agreements to alter the function and purpose of real-party-in-interest statutes such as Rule 17(a).

23. 6A C. Wright, A. Miller & M. Kane, supra note 10, § 1544, at 345. As Wright, Miller and Kane explain:

Finally, it should be noted that the question of who is the real party in interest should be distinguished from the question of in whose name an action may be brought. State law may provide that a particular plaintiff has a cause of action but that the claim should be prosecuted in the name of another party. In that situation the federal court will allow the claim to be asserted by plaintiff since he has a substantive right under state law, which makes him the real party in interest for purposes of Rule 17(a). In short, the question of in whose
under substantive state law, but as a procedural matter, the federal statute requires suit in the name of the party with the substantive right.24

C. DEVELOPMENT OF THE LOAN RECEIPT

In the hypothetical case of Jones, America’s Largest, and Bob’s Shipping, the loan receipt let America’s Largest gain the benefits of subrogation without bringing suit in its own name, thus circumventing Rule 17(a).25 The loan receipt evolved, however, as a device designed to remedy a very different problem.26

1. Carrier Beneficiary and Third Party Liability Clauses

Insurers developed loan receipt agreements in response to commercial practices of the 1800s. Toward the end of that century, carriers of goods began to insert “carrier beneficiary” clauses into their shipment contracts.27 These provisions made the carrier the beneficiary of the shipper’s insurance. If the carrier damaged the shipper’s goods, the payment from the insurer to the shipper would settle any claim the shipper had against the carrier.28 Because the shipper no longer had a claim against the carrier, the insurer could not invoke subrogation to recover its insurance payment from the carrier, even if the carrier was negligent.29

To illustrate these principles, return to the Jones hypothetical and suppose Bob’s Shipping inserted the following carrier beneficiary clause in the bill of lading: “In case of any damage done to the shipper’s goods for which the carrier is liable to the shipper, the carrier shall have the full benefit of any insurance

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name the action should be brought is a procedural one and should be governed by the federal rules.

Id. (footnotes omitted).
24. 6A C. WRIGHT, A. MILLER & M. KANE, supra note 10, § 1544, at 345.
25. See supra notes 1-3 and accompanying text.
26. For a more detailed discussion of the history of the loan receipt, see Comment, supra note 2, at 115-17.
27. Id. at 115 (citing R. HORN, SUBROGATION IN INSURANCE THEORY AND PRACTICE 68 (1964)).
28. Id.
29. Id. The following is a typical carrier beneficiary clause: “the carrier so liable shall have the full benefit of any insurance that may have been effected upon or on account of said goods.” See Phoenix Ins. Co. v. Erie & W. Transp. Co., 117 U.S. 312, 314, 320 (1886). The Court upheld this clause in Phoenix. Id. at 325-27.
that may have been effected upon the shipper’s goods."³⁰ Bob’s Shipping then damages Jones’ Fitness Machine. In the first case, assume Jones would rather sue Bob’s Shipping than collect the proceeds of her insurance policy with America’s Largest. In this case, the insurance is not “effected” in the sense that Jones has recovered no money under the policy. Bob’s Shipping must pay Jones’ court judgment despite its carrier beneficiary clause. America’s Largest now owes no money to Jones because Jones’ recovery from Bob’s Shipping prevents Jones from filing an insurance claim.³¹

In the normal case, however, Jones will file a claim, and America’s Largest will pay on the policy. If Jones subsequently sues Bob’s Shipping, the court will not allow her to keep any payment on the judgment.³² If she sues anyway, Bob’s Shipping will defend based on the carrier beneficiary clause in the bill of lading, asserting its right to the “full benefit of any insurance.”³³ Jones cannot maintain an action for the damages compensated by insurance.³⁴

In the usual case, Jones will not sue Bob’s Shipping once she has received the insurance proceeds. Rather, America’s Largest will subrogate itself to Jones’ claim. Under subrogation, America’s Largest has the same claim against Bob’s Shipping that Jones would have had;³⁵ that is, America’s Largest is bound by the carrier beneficiary clause on the bill of lading.³⁶ Thus, Bob’s Shipping would defend based on the carrier beneficiary clause, and America’s Largest could not recover the insurance proceeds paid to Jones.³⁷

Insurers responded to carrier beneficiary clauses by in-

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30. See supra note 29, infra note 51 (both providing other examples of carrier beneficiary clauses).
32. See National Garment Co. v. New York, C. & St. L. R.R., 173 F.2d 32, 35 (8th Cir. 1949) (stating that the insured must hold the recovery in trust for the insurer); 16 G. COUCH, R. ANDERSON & M. RHODES, supra note 8, § 61:29, at 109 (same).
33. See supra text accompanying note 30.
34. See Phoenix, 117 U.S. at 325.
35. See id. at 321; 16 G. COUCH, R. ANDERSON & M. RHODES, supra note 8, § 61:114, at 183-84; Comment, supra note 2, at 115.
36. See supra note 35.
37. Phoenix, 117 U.S. at 325; cf. 16 G. COUCH, R. ANDERSON & M. RHODES, supra note 8, § 61:114, at 183-84 (stating that the insurer has the same claim against the wrongdoer as the insured).
serting third party liability clauses in their insurance policies. These clauses provided that the insurer owed no money to an insurance policy claimant until the liability of all potentially liable parties had been determined in court. The liability of the insurer under the policy thus became contingent on the liability of third parties to the claimant.

Returning to the Jones hypothetical, suppose Bob's Shipping included a carrier beneficiary clause in its bill of lading. Further suppose America's Largest anticipated shipment on a bill of lading containing a carrier beneficiary clause by including the following third party liability clause in Jones' insurance policy: "America's Largest will not make payment to the insured until the liability, if any, of any and all third parties to the insured has been first determined." After Bob's Shipping damaged her Fitness Machine, Jones would file a claim. Under the third party liability clause, America's Largest could properly delay payment until Jones' suit against Bob's Shipping was settled or went to judgment. In fact, if Jones' suit is successful, Jones' recovery would extinguish the policy claim, and America's Largest would never pay on the policy.

2. Luckenbach and the Loan Receipt Agreement

Third party beneficiary clauses relieved insurers of immediate liability for goods shipped on bills of lading containing carrier beneficiary clauses. This is not the result the insurers sought. The insurers merely wanted to compensate the insured without losing their subrogation rights, and developed loan receipt agreements with that purpose in mind. Using this device, when the shipper filed a claim with its insurance company for the damaged cargo, the amount the insurer paid on the policy was considered a loan to the shipper. The shipper was obligated to repay the loan only if and to the extent it was able to

38. See, e.g., Luckenbach v. W.J. McCahan Sugar Refining Co., 248 U.S. 139, 146 (1918); infra note 52.
39. See, e.g., Luckenbach, 248 U.S. at 146. The third party liability clause in Luckenbach also provided specifically that the insurer was not liable for any goods shipped under a bill of lading containing a carrier beneficiary clause. See infra note 52. The insurer waived its claim based on this provision. Luckenbach, 248 U.S. at 140-41 (argument for petitioners).
40. Luckenbach, 248 U.S. at 146.
41. See infra note 52 (providing example of third party liability clause).
42. See Luckenbach, 248 U.S. at 146.
43. Comment, supra note 2, at 115-16.
44. Id. at 116.
recover from the carrier by suing the carrier. Because the transfer of funds from the insurer to the shipper was a loan rather than an insurance payment, the carrier's beneficiary clause did not apply. The shipper thus obtained immediate insurance compensation for its loss in the form of a loan, while retaining a claim against the carrier for the damage caused to its goods. The insurer would have its loan repaid if the shipper successfully recovered from the carrier for the value of the damaged goods.

The U.S. Supreme Court upheld use of the loan receipt to promptly compensate the insured without losing the insurer's subrogation right in Luckenbach v. W. J. McCahan Sugar Refining Co. In Luckenbach, the W. J. McCahan Sugar Refining Company shipped a cargo of sugar from Puerto Rico to Philadelphia aboard the Julia Luckenbach, chartered by the Insular Line. The cargo was damaged, but the shipper had full insurance coverage through the Federal Insurance Company. The bills of lading contained carrier beneficiary clauses, however, and the shipper's insurance policy, containing a third party liability clause, did not cover shipments on such bills of lading. The Federal Insurance Company paid on the policy anyway, using a loan receipt.

45. Id.
46. See id. at 116-17.
47. 248 U.S. 139 (1918).
48. Id. at 144.
49. Id.
50. Id. at 145-47.
51. The bills of lading contained the following carrier beneficiary clause, giving the carrier the full benefit of the shipper's insurance:
   In case of any loss, detriment or damage done to or sustained by said goods or any part thereof for which the carrier shall be liable to the shipper, owner or consignee, the carrier shall to the extent of such liability have the full benefit of any insurance that may have been effected upon or on account of said goods.
   Id. at 145-46.
52. The insurance policy contained a third party liability clause providing that the insurer did not have to pay on the policy until the carrier's liability had been determined:
   Warranted by the assured free from any liability for merchandise in the possession of any carrier or other bailee, who may be liable for any loss or damage thereto; and for merchandise shipped under a bill of lading containing a stipulation that the carrier may have the benefit of any insurance thereon.
   Id. at 146.
53. Id. at 147. To promptly reimburse the shipper and to avoid losing the right of subrogation, the insurer paid on the policy in accordance with the following loan receipt agreement:
The Court held that payments under loan receipt agreements are legitimate loans rather than payments of insurance, noting that whether the transfer of money operates as a payment is determined ordinarily by the intention of the parties to the transaction.64 The *Luckenbach* Court considered loan receipts the ideal solution to the problem posed by carrier beneficiary clauses. Delivering the opinion of the Court, Justice Brandeis praised the ingenuity of businesspersons in devising an arrangement "which is consonant both with the needs of commerce and the demands of justice."55

Insurers noted the Supreme Court's unqualified approval of the loan receipt agreement and sought other ways to make use of the loan receipt.56 One natural use for the loan receipt

Received from the Federal Insurance Company, [$2,304.16], as a loan and repayable only to the extent of any net recovery we may make from any carrier . . . on account of loss to our property . . . due to damage on S/S Julia Luckenbach . . . and we agree to enter and prosecute suit against said . . . carrier . . . on said claim with all due diligence at the expense and under the exclusive direction and control of the said Federal Insurance Company.

Id.

54. *Id.* at 149-51.

55. *Id.*


The following cases involve the use of loan receipts in other contexts or by parties other than insurer and insured: Moore v. Subaru of Am., 891 F.2d 1445, 1450 (10th Cir. 1989) (holding that loan receipts are not valid loans when used to avoid setoff against settlement); Symons v. Mueller Co., 526 F.2d 13, 16 (10th Cir. 1975) (holding that loan receipts do not circumvent rule prohibiting indemnity between joint tortfeasors); Willamette-W. Corp. v. Columbia Pac. Towing Co., 466 F.2d 1390, 1393 (9th Cir. 1972) (holding that loan receipts are invalid to circumvent waiver of subrogation rights in contract); Augusta Broadcasting Co. v. United States, 170 F.2d 199, 200 (5th Cir. 1948) (holding that insured remains sufficiently interested after executing a loan receipt to bring action under Federal Tort Claims Act); Aetna Ins. Co. v. United States, 162 F. Supp. 442, 442 (Ct. Cl. 1958) (per curiam) (holding that loan receipt payment is payment on the policy for tax statute); Oliver B. Cannon & Son, Inc. v. Fidelity & Casualty Co., 519 F. Supp. 668, 677 (D. Del. 1981) (holding loan receipt valid when attorney "loaned" services); Independent School Dist. No. 454 v. Statistical Tabulating Corp., 359 F. Supp. 1095, 1098-99 (N.D. Ill. 1973) (holding loan receipt valid between corporation and school district); American Dredging Co. v. Federal Ins. Co., 309 F. Supp. 425, 428-29 (S.D.N.Y. 1970)

Received from the Federal Insurance Company, [2,304.16], as a loan and repayable only to the extent of any net recovery we may make from any carrier . . . on account of loss to our property . . . due to damage on S/S Julia Luckenbach . . . and we agree to enter and prosecute suit against said . . . carrier . . . on said claim with all due diligence at the expense and under the exclusive direction and control of the said Federal Insurance Company.

Id.

54. *Id.* at 149-51.

55. *Id.*


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arose in the context of insurer subrogation.

D. **LOAN RECEIPTS AND RULE 17(a)**

Insurers were dissatisfied that Rule 17(a) required them to bring suit against the wrongdoer in their own names. Insurers believed a jury would be prejudiced against a plaintiff insurance company. The loan receipt provided an ideal solution to the dilemma posed by insurers bringing suit in their own names. The insurer would still pay the policy proceeds, but in the form of a loan, to be repaid only out of any recovery the insured may receive from the wrongdoer. As in the case of the shipper and carrier, the insured would bring suit in its own name against the wrongdoer. If the loan receipt is upheld as a valid loan in this context, the insurer avoids joinder as the real party in interest under Rule 17(a).

Whether the loan receipt is a valid loan or merely a payment disguised as a loan usually has been the central issue in cases determining the validity of the device when used to circumvent Rule 17(a). Lower federal courts have aligned themselves on both sides of the issue of loan receipt validity.

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(holding that loan receipt cannot alter right of pro rata contribution between co-insurers).

This Note addresses only insurers' use of loan receipts to avoid bringing suit in their own names.

57. **Note, supra note 6, at 466.**

58. **Id. at 466.** Jury prejudice against insurance companies is often judicially recognized. *E.g.*, White Hall Bldg. Corp. v. Profexray Div. of Litton Indus., 387 F. Supp. 1202, 1206 (E.D. Pa. 1974), aff'd without opinion sub nom. Quaglia v. Profexray Div. of Litton Indus., 578 F.2d 1375, 1377 (3d Cir. 1978). In the absence of compelling empirical evidence, both the existence and the effect of jury prejudice is debatable. Juries are familiar with insurance. Rather than being prejudiced against plaintiff insurers, juries may even be aware that the defendant is also, "in reality," an insurance company. See Kennedy, **Federal Rule 17(a): Will the Real Party in Interest Please Stand?**, 51 MINN. L. REV. 675, 686 (1967) (noting that modern juries may assume defendants are insured). For a more thorough discussion of the effect of jury prejudice, see *infra* text accompanying notes 131-40.

59. **Comment, supra note 2, at 122 n.38** (citing Note, **Insurance—The Loan Receipt**, 35 WASH. L. REV. 190, 193 (1960)).


The courts in the following cases found loan receipts valid: Luckenbach v.
1. Early Federal Court Decisions: Mechanically Applying Luckenbach

Prior to the adoption of the Federal Rules of Civil Procedure in 1938, use of loan receipts to circumvent Rule 17(a) was, of course, not a problem. After Rule 17(a) became effective, a series of circuit court cases upheld the validity of loan receipts when used by insurers suing the wrongdoer in the name of the insured. These courts typically cited Luckenbach without offering any other supporting rationale. The last in this series of cases, Ketona Chemical Corp. v. Globe Indemnity


62. Between the Luckenbach decision in 1918 and adoption of the Federal Rules of Civil Procedure in 1938, parties did advance the argument that the insurer was the real party. E.g., Wittig v. Canada S.S. Lines, Ltd., 95 F.2d 428, 429-30 (W.D.N.Y. 1933). The federal courts rejected this argument based on Luckenbach. See, e.g., id.

63. See supra note 60 (citing federal court of appeals cases dating from 1940 to 1968).

illustrates how the federal courts automatically approved loan receipts used to circumvent Rule 17(a). The Fifth Circuit held that the insured, Ketona, was the real party in interest under Rule 17(a), without offering any supporting rationale and without even citing Luckenbach.

2. Federal Courts Rejecting Loan Receipt Use to Circumvent Rule 17(a)

In 1969, the D.C. Circuit decided City Stores Co. v. Lerner Shops, Inc. and created a split among the circuit courts on this issue for the first time. The City Stores court held that the loan receipt was a sham agreement designed to evade Rule 17(a), Ketona involved a dispute over the Comprehensive General Liability Policy that Globe Indemnity Company issued to Ketona Chemical Corporation. A Ketona employee sought recovery for personal injury sustained while loading a tank car with ammonia. Id. at 182-83. The Fifth Circuit affirmed the lower court judgment in holding that Globe's policy did not cover the employee's injury. Id. at 182.

Ketona had also purchased insurance from Underwriters at Lloyd's of London. Pursuant to a loan receipt agreement, Lloyd's defended the suit and paid Ketona's portion of the settlement. Id. at 183. The entire holding is as follows:

We hold that under [Federal Rule of Civil Procedure 17(a)], Ketona is the real party in interest and the proper party plaintiff. Sanders v. Liberty Mut. Ins. Co., 354 F.2d 777 (5th Cir. 1965). See 18 G. COUCH & R. ANDERSON, COUCH Cyclopedia of Insurance Law § 61:72 (2d ed. 1959); Annotation, Insurance: Validity and Effect of Loan Receipt or Agreement between Insured and Insurer for a Loan Repayable to Extent of Insured's Recovery from Another, 13 A.L.R.3d 42 (1967). The single Alabama case which has dealt with the question of the validity of a loan receipt transaction is McKenzie v. North River Ins. Co., 257 Ala. 265, 58 [So. 2d] 581 (1951), and it is not in point.

Id. at 184.

410 F.2d 1010 (D.C. Cir. 1969). In this case three companies, including Lerner Shops, sued City Stores for losses sustained in a fire allegedly caused by City Stores' negligence. Id. at 1011. Their insurance companies had already compensated the three companies, using either the following or a substantially similar loan receipt agreement:

RECEIVED FROM Lumberman's Mutual Casualty Company [§27,890.18], as a loan and repayable only to the extent of any net recovery we may make from any person or persons, corporation or corporations, on account of loss by fire to our property on or about September 7, 1963 or from any insurance effected by such person or persons, corporation or corporations.

As security for such repayment, . . . we agree to enter and prosecute suit against such person or persons, corporation or corporations on account of said claim for said loss, with all due diligence, at the expense and under the exclusive direction and control of said Lumberman's Mutual Casualty Company.

Id. at 1011 & n.1.
and therefore insurance companies should be made parties plaintiff, as the real parties in interest.\textsuperscript{68} The court distinguished \textit{Luckenbach} as a situation in which the insurer's liability was contingent rather than absolute.\textsuperscript{69} The court appeared to argue that, due to the third party liability clause in \textit{Luckenbach}, the contingency of the carrier's liability must be resolved to determine the insurer's liability.\textsuperscript{70} City Stores, the insured, admitted in oral argument that \textit{Luckenbach} involved contingent, not absolute, liability, but contended that subsequent federal cases expanded the holding of \textit{Luckenbach} to cover situations of absolute liability.\textsuperscript{71} The D.C. Circuit was unimpressed with the other federal cases that cited \textit{Luckenbach} as supporting the validity of loan receipt agreements, because they lacked any other supporting rationale.\textsuperscript{72}

After noting that the insurer sought to avoid suing in its own name for fear of jury prejudice, the court deemed this "an unworthy motive, if not an improper and illegal purpose,"

\begin{itemize}
  \item \textsuperscript{68} \textit{Id.} at 1015.
  \item \textsuperscript{69} \textit{Id.} at 1013.
  \item \textsuperscript{70} \textit{Id.}
  \item \textsuperscript{71} \textit{Id.} at 1014.
  \item \textsuperscript{72} \textit{Id.} The court was frank in expressing its disdain toward the other federal decisions:
    \begin{itemize}
    \item We might be impressed by [the] assertion [that federal cases since the \textit{Luckenbach} opinion have enlarged its holding] if in the subsequent federal decisions the courts had reached their conclusions through sound and independent reasoning. But, almost without exception, the district and circuit court cases cited by the appellees upheld the use of the loan receipt where the liability of the insurer is absolute base their holdings upon the \textit{Luckenbach} case, without any process of reasoning of their own to justify their expansion of its ruling. This clearly indicated, we think, that the cases cited by the appellees, and others of similar import, were based upon a misapprehension of the true holding of the \textit{Luckenbach} decision.
    \item During the half century since it was written, that case has been often cited by federal district and circuit courts, and almost as often has been misunderstood. As we have shown, it does not hold that an insurer whose liability is absolute may pay the claim of an insured and avoid the consequences of subrogation by calling the payment a loan and taking a loan receipt from the insured. Consequently, it does not support the subsequent federal cases which so hold.
    \item Our consideration of this case of first impression is not aided by the federal cases cited by the appellees which, as we have said, do little more than cite the \textit{Luckenbach} case to support their expansion of its holding. Decisions of district courts and other courts of appeals are, of course, not binding on us and are looked to only for their persuasive effect. If they fail to persuade by the use of sound and logical reasoning, they will not be followed, no matter how great their number.
    \item \textit{Id.} (footnote omitted).
  \end{itemize}
\end{itemize}
which sought to frustrate the enforcement of Rule 17(a). The court determined that loan receipts are not true loans because they lack an unconditional promise to pay at some certain time, they do not provide for interest, and the insured sells the insurance company the right to use the insured's name with the only consideration to the insured being a possibility of earlier payment. The court considered irrelevant the parties' intention that the loan receipt be construed a loan because the real purpose was "a bold and bald evasion of a federal rule of practice and procedure." It also noted that some earlier courts had upheld loan receipts because the defendant had not shown that it would be prejudiced by the denial of joinder of the insurer as the real party in interest. In rejecting this rationale, the court stated that the burden is on the plaintiff to show why the defendant is not entitled to the benefit of Rule 17(a).

Then-Circuit Judge Warren Burger dissented, seeing no compelling reason why the parties' private agreements should not be given effect. He saw nothing improper in seeking to have the jury evaluate the case without regard to insurance coverage. Judge Burger explained that the purposes of Rule 17(a) are to enable the defendant to avail itself of all evidence and defenses it has against the real party in interest and to ensure finality of judgment. Although the majority emphasized the improper purpose of the plaintiff to circumvent Rule 17(a) for fear of jury prejudice, Judge Burger considered the defendant's purpose improper in substituting the insurer as plaintiff to take advantage of any possible jury prejudice. Furthermore,

73. Id. at 1013.
74. Id. at 1014-15.
75. Id. at 1015.
76. Id.
77. Id.
78. Id. at 1015-16 (Burger, J., dissenting).
79. Id. Judge Burger further argued that "there may well be some public policy served in having the triers decide the issue uninfluenced by the circumstance that 'a large insurance company' will pay the bill." Id. at 1015.
80. Id. at 1016.
81. Id. Judge Burger argued that in Celanese Corp. of Am. v. John Clark Indus., 214 F.2d 551, 556 (5th Cir. 1954), the Fifth Circuit recognized defendant's improper purpose in trying to substitute the insurer as plaintiff. City Stores, 410 F.2d at 1016. The majority responded that the Celanese improper purpose argument applied equally to the insurer's improper purpose in trying to remain anonymous. Id. at 1015 n.3.

Insurers are not always so concerned about anonymity. In fact, some insurers routinely execute loan receipts but then attempt to sue in their own names; in these cases the device is thus merely a way of insuring their subrogation rights. See, e.g., C. Itoh & Co. v. M/V Hans Leonhardt, 719 F. Supp. 419,
Judge Burger would have given effect to the parties' intention that the loan receipt be construed as a loan despite the loan receipt's purpose of circumventing Rule 17(a).\(^{82}\)

The Sixth Circuit followed the City Stores analysis and determined that loan receipts were invalid in the 1974 case of Executive Jet Aviation, Inc. v. United States.\(^{83}\) In that case, an insurer used a loan receipt to compensate its insured for damage to the insured's airplane.\(^{84}\) The court distinguished Luckenbach as a case in which liability was contingent, explaining that the insurer would have incurred liability only if the insured could not recover from the carrier.\(^{85}\) If the insurer had paid the shipper before the court determined the carrier's liability, the carrier beneficiary clause would absolve the carrier of any liability. Although the loan receipt in Luckenbach had some indicia of a true loan, the court concluded that the transfer of monies in Executive Jet was not a true loan because the terms of the alleged loan did not require payment of a definite sum at a definite time and did not assess interest charges, the amount loaned equaled the amount of the insurance policy, and the insurer controlled the lawsuit just as it would in the case of ordinary subrogation.\(^{86}\) The court rejected earlier federal authority as lacking in reasoning, and instead sided with City

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\(^{83}\) 507 F.2d 508 (6th Cir. 1974). In this case, an aircraft owned by Executive Jet crashed on takeoff due to engine failure caused by ingestion of a large number of seagulls roosting on the runway. \textit{Id.} at 510. A group of British insurance companies paid Executive Jet, using a loan receipt. Executive Jet then filed suit against the United States, alleging FAA air traffic controller negligence by not warning the pilot of the existence of seagulls on the runway. \textit{Id.} at 510-11. The court chose not to decide whether the effect of the loan receipt is governed by federal or state law, because Ohio considered monies transferred under loan receipts to be payments under the policy, and the court felt the federal rule should be the same. \textit{Id.} at 511.

\(^{84}\) \textit{Id.} at 510.

\(^{85}\) \textit{Id.} at 512.

\(^{86}\) \textit{Id.}
3. Recent Federal Cases Supporting Loan Receipts in Rule 17(a) Cases

The courts of appeals resumed rubber stamping *Luckenbach* after the brief hiatus in *City Stores* and *Executive Jet*. In 1975, the Tenth Circuit decided *R. J. Enstrom Corp. v. Interceptor Corp.*,

holding the loan receipt valid. The court considered *Luckenbach* dispositive on the issue of loan receipt validity, deciding that the insured was the real party in interest for purposes of Rule 17(a). It noted that most federal courts have followed *Luckenbach*. As to whether the loan receipt constitutes payment, the court considered the issue one of state subrogation law, not federal procedural law. Because the relevant state law upheld the validity of loan receipts as loans, the court determined the insurers were not subrogated on the claim; that is, the insurer did not have to bring suit in its own name because it had not made a "payment."

The Eleventh Circuit similarly did not address the reasoning of *City Stores* and *Executive Jet* when it decided *Frank Briscoe Co. v. Georgia Sprinkler Co.* in 1983. Although the parties in *Frank Briscoe* did not dispute the prosecution of the

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87. *Id.* at 512-13. In *Potomac Electric Power Co. v. Babcock & Wilcox Co.*, 54 F.R.D. 486 (D. Md. 1972), Babcock supplied steam generating units to Pepco. *Id.* at 488-89. The units failed, and Pepco recovered from its two insurers (executing a loan receipt agreement), before bringing suit against Babcock. *Id.* The district court held that loan receipt agreements are not bona fide loans. *Id.* at 489.

The court further concluded that both insurers were indispensable parties under Rule 19, even though this required the court to then dismiss the action because joinder of the missing insurance company would have resulted in lack of complete diversity of citizenship. *Id.* at 491.


89. *Id.* at 1219.

90. *Id.*

91. *Id.*

92. *Id. But see supra note 22 and accompanying text (discussing whether state or federal law governs).*

93. 713 F.2d 1500 (11th Cir. 1983). *Frank Briscoe* was under contract to construct a federal government building. The company entered into a subcontract with Georgia Sprinkler for installation of a fire-prevention system. Georgia Sprinkler's sprinkler system leaked, causing damage to the building. Frank Briscoe's insurer paid Frank Briscoe, executing a loan receipt agreement. *Id.* at 1501.
suit in the insured’s name, the court upheld the validity of the loan receipt in a footnote lacking any supporting rationale, but simply citing *R. J. Enstrom* and *Ketona*.95

The most recent case to address loan receipt validity is the federal district court case of *Acro Automation Systems, Inc. v. Iscont Shipping Ltd.*96 Acro Automation Systems (Acro) bought laser welding equipment from a manufacturer in Israel and hired Bekins High Technologies International (Bekins HiTech) to arrange shipment from Israel to Acro in Milwaukee.97 After being handled by several shippers, the equipment arrived in damaged condition. Acro submitted a claim to its insurer, Insurance Company of North America (INA), for the cost of the goods less the salvage value.98 Instead of paying the insurance proceeds outright, INA “loaned” the money to Acro under a “loan and trust receipt.”99 Acro then sued Bekins HiTech for damages in the amount paid to Acro under its insur-

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95. The footnote reads:

Where an insurance company as subrogee has paid an entire loss suffered by the insured it is the only real party in interest and must sue in its own name. United States v. Aetna Casualty & Sur. Co., 338 U.S. 366, 380-81 (1949). When a loan receipt is utilized, however, the insured retains a sufficient interest so as not to displace him as the real party in interest under [Federal Rule of Civil Procedure 17(a)]. [R.J. Enstrom Corp. v. Interceptor Corp., 520 F.2d 1217 (10th Cir. 1975); Ketona Chem. Corp. v. Globe Indem. Co., 404 F.2d 181 (5th Cir. 1968); American Chain & Cable Co. v. Brunson, 157 Ga. App. 833, 278 S.E.2d 833 (1981)].

96. Id. at 1502 n.1.


98. Id. at 414.

99. Id. at 414. Acro paid $400,000 for the equipment, which had a salvage value of $147,890; thus Acro lost $252,110 and claimed this amount as damages. Id.

1990]
The U.S. District Court for the District of Maryland upheld the validity of the loan receipt agreement in *Acro*. The court undersigned undertakes to execute such documents as may be necessary to carry out the purpose hereof.

100. *Id.* at 420.

101. *Id.* at 414.

The court denied Bekins' motion to add INA as the real party in interest, holding that the loan receipt agreement, intended to circumvent Rule 17(a), did not frustrate the policies of the Rule. *Id.*

The court also discussed the validity of the carrier's limitation of liability clause in the bill of lading, which reduced the damages recoverable to $1.25 per pound or, in this case, only $24,000. The court first noted that the Interstate Commerce Act permitted limitation of liability, but the shipper must deliberately choose to limit liability. *Id.* at 415-16. Acro did not choose to limit the carrier's liability because it did not sign the limitation of liability agreement in the bill of lading, and Bekins Van Lines did not deliver the bill of lading prior to shipment of the laser welding equipment. *Id.* at 416-17. By accepting the equipment and paying, Acro did not deliberately choose to limit the carrier's liability because the bill of lading recited a flat fee rather than a choice of rates, when one rate would have been with the limitation of liability and the other without. *Id.* at 418-19. Finally, in an alternative holding, the court noted that the limitation of liability could apply only to Bekins Van Lines, because Bekins Forwarding and Bekins HiTech did not hold the ICC license that permits carriers to take advantage of the section of the Interstate Commerce Act providing for limitation of liability. *Id.* at 419.

At first glance, the limitation of liability agreement in *Acro* seems similar to the carrier beneficiary clause in *Luckenbach*. The limitation of liability agreement, however, does not affect the substantive rights of the parties in the same manner as a carrier beneficiary clause. Under the carrier beneficiary clause, an insurance payment from the insurer to the shipper effectively extinguished the claim of the shipper against the carrier. *See supra* note 29 and accompanying text. Under a limitation of liability agreement, the carrier limits its liability to an amount based on the weight of the goods shipped rather than the value of the goods damaged. *E.g., Acro*, 706 F. Supp. at 414. Thus, if the insurer pays the shipper the amount of the damaged goods, the insurer becomes subrogated only to the limited claim based on the weight of the goods shipped. *See* 16 G. COUCH, R. ANDERSON & M. RHODES, *supra* note 8, § 61:116, at 186. In this situation, executing a loan receipt agreement does not help the insurer recover the full value of the damaged goods from the carrier, because the carrier's liability is not contingent on whether the shipper is insured. The carrier is liable to the shipper (or to the insurer as the shipper's subrogee) only for the limited amount based on the weight of the goods shipped.

The court decided *Acro* without mentioning *Potomac Elec. Power Co. v. Babcock & Wilcox Co.*, 54 F.R.D. 486 (D. Md. 1972). In 1972 the U.S. District Court for the District of Maryland firmly asserted in *Potomac* that "[a] payment [under a loan receipt agreement] conditioned on such control by an insurance company and its attorneys of a subsequent suit hardly amounts to a bona fide loan so as to avoid the requirements of Rules 17 and 19." *Id.* at 489. At that time, the court opposed loan receipt agreements so vigorously that it required joinder of the insurer even though the case then had to be dismissed for lack of diversity jurisdiction. *See supra* note 87. Yet in *Acro*, the court felt compelled to uphold the loan receipt agreement "[b]ecause to hold otherwise
first looked to Ketona, R. J. Enstrom, Frank Briscoe, City Stores, and Executive Jet to determine the state of the law. Because the circuits were split and the Fourth Circuit had not ruled on loan receipt validity, the court examined the policy behind Rule 17(a).102

The Acro court reiterated the two often-cited purposes of Rule 17(a): to enable a defendant to avail itself of all defenses and evidence it has against the real party in interest, and to ensure finality of judgment.103 The court noted that the defendants had not suggested they had defenses against INA that they could not assert against Acro.104 Furthermore, the defendants could conduct discovery against INA. The court noted also that the Supreme Court had decided in Montana v. United States105 that “[w]hen a non-party assumes control of a party’s litigation, the non-party is precluded from relitigating the claims litigated in the first action.”106 Because INA had full control of the litigation under the terms of the loan receipt agreement, INA would be bound by the decision rendered to Acro. The court thus found no violation of the policy behind Rule 17(a) in not substituting INA as the real party in interest.107

Finding no compelling policy reason to apply Rule 17(a), the court enforced the contractual intent of Acro and INA as expressed in the loan receipt agreement.108 According to the court, because the issue of insurance was “concededly irrelevant,” the plaintiff should be protected from any disclosure to the jury of the insurer’s role as the real party in interest.109 The Acro court concluded that the defendant’s purpose in seeking joinder of an insurance company must be to prejudice the jury.110


103. Id.; see supra notes 18-20 and accompanying text.
107. Id. at 420-21.
108. Id. at 421.
109. Id.
110. Id. (citing City Stores Co. v. Lerner Shops, Inc., 410 F.2d 1010, 1015-16 (D.C. Cir. 1969) (Burger, J., dissenting)); see supra text accompanying notes 79-82. The defendants in Acro also moved that INA be joined under Fed. R. Civ. P. 19(a) as a person to be joined if feasible. The court noted that the advisory committee note states that the purpose of Rule 19(a) is to ensure finality
II. LOAN RECEIPT AGREEMENTS SHOULD NOT AFFECT THE REAL PARTY IN INTEREST

A. LIMIT LUCKENBACH TO ITS FACTS

The loan receipt evolved from the interaction of insured, carrier, and insurer.111 Under a carrier beneficiary clause, the insurer effectively loses its subrogation right.112 If the insurer pays on the policy, that payment nullifies the shipper's claim against the carrier, and therefore the insurer has no subrogated claim. Insurers responded by including third party liability clauses in insurance policies, which made the insurer's liability on the policy contingent upon prior determination of the liability of any third parties to the insured.113

To illustrate this point, return to the hypothetical case of Jones, Bob's Shipping, and America's Largest. Suppose Jones' policy with America's Largest contained a third-party liability provision. Under this provision, America's Largest could properly delay payment until Jones' suit against Bob's Shipping was settled or went to judgment. In this hypothetical, Jones would certainly appreciate payment under a loan receipt, allowing her the immediate recovery one expects from insurance. Jones also would probably never insure with America's Largest again if it continued to issue policies with third party liability provisions.

With this in mind, one discovers the importance of distinguishing Luckenbach from cases in which a party used loan receipts to circumvent Rule 17(a), such as City Stores and Executive Jet.114 The loan receipt in Luckenbach had a valid purpose; the insurer was able to promptly compensate the shipper without losing its right to subrogation. When the loan receipt is used in contexts that do not involve the contingent liability created by third party liability clauses, however, the loan receipt is deceptive. It no longer serves the business purposes that Justice Brandeis praised;115 it serves only the interest of the insurer in not bringing suit in its own name. Thus, Luckenbach should be limited to cases involving insurance policies expressly stating that payment is contingent upon prior de-

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111. See supra notes 1-5 and accompanying text.
112. See supra text accompanying note 29.
113. See supra text accompanying note 38.
114. See supra text accompanying notes 68, 86.
115. See supra text accompanying note 55.
termination of any third parties' liability to the insured for damages related to the insurance claim.

B. PROCEEDS RECEIVED UNDER LOAN RECEIPTS ARE NOT VALID LOANS

The courts in City Stores and Executive Jet argued convincingly that loan receipts are not loans because they do not provide for definite payment at a definite time, nor for interest.\footnote{116} The other courts do not answer these concerns, nor do they explain what the insured receives as consideration for entering into the agreement, the third factor the City Stores court cited as characteristic of a true loan.\footnote{117}

Examination of the typical loan receipt agreement, as in the original hypothetical, reveals that the insured receives no consideration for entering into the agreement. Although executing the loan receipt agreement purportedly frees the insured of the expense of litigation by giving the insurer control of the subsequent lawsuit,\footnote{118} the insurer gains this control and assumes this expense through subrogation even in the absence of any agreement.\footnote{119} Through the loan receipt, the insurer gains the right to bring suit in the name of the insured, while the insured receives nothing to which it was not already entitled. In the usual case, the insurer is liable on the insurance policy, and the insured is entitled to prompt payment whether or not it agrees to enter into a loan receipt agreement.

In Luckenbach, the insurer was not liable until the carrier's liability was determined.\footnote{120} The insured benefited from entering the loan receipt agreement because it received prompt payment to which it was not otherwise entitled.\footnote{121} The insurer benefited by gaining control of the insured's litigation against

\footnote{116} See supra text accompanying notes 75, 86. Similar criteria for loan validity are used in tax cases involving disputes whether money transfers from individuals to corporations are valid loans or actually capital investments. See, e.g., Scriptomatic, Inc. v. United States, 397 F. Supp. 753, 759 (E.D. Pa. 1975), aff'd, 555 F.2d 364 (3d Cir. 1977); Santa Anita Consol. v. Commissioner, 50 T.C. 536, 550 (1968).


\footnote{118} For examples of loan receipts giving the insurer control of the subsequent litigation, see supra notes 53, 67.

\footnote{119} See supra note 8 and accompanying text; supra text accompanying note 86.

\footnote{120} Luckenbach v. W.J. McCahan Sugar Refining Co., 248 U.S. 139, 149 (1918).

\footnote{121} Id.
the carrier without subrogation.\textsuperscript{122} These mutual benefits arguably supply consideration for the loan.\textsuperscript{123} Thus, when the insurer's liability is contingent, as in \textit{Luckenbach}, there is at least some indication of a true loan, despite the lack of any provision for definite payment at a definite time and for interest.\textsuperscript{124} Loan receipts used solely to circumvent Rule 17(a), on the other hand, lack indicia of a true loan.

C. \textbf{THE POLICIES BEHIND RULE 17(a)}

Rather than examining \textit{Luckenbach} and whether monies transferred under loan receipt agreements are truly loans, the \textit{Acro} court adopted the rationale of Judge Burger's dissent in \textit{City Stores} and rested its decision entirely on policy grounds.\textsuperscript{125} The court focused on defenses that can be used only against the real party in interest, and on the issue of finality of judgment.\textsuperscript{126} Although these are important policy considerations, there are other relevant policies. When Rule 17(a) was first promulgated, Congress opted for the rule in equity, recognizing the insurer's subrogation right, rather than the provision at law that did not recognize insurer's subrogation rights.\textsuperscript{127} Because Rule 17(a) requires suit in the name of the real party in interest, one can infer that the drafters of Rule 17(a) did not want to introduce the legal fiction that the insured maintains a pecuniary interest in the outcome of the subrogated suit.\textsuperscript{128} Decisions upholding the loan receipt have the opposite result. No one disputes that the insurer is truly the real party in interest because only the insurer stands to profit from the lawsuit.\textsuperscript{129} By allowing a private agreement to circumvent Rule 17(a), a court perpetuates the legal fiction that the insured maintains a pecuniary interest in the suit, which is contrary to the policy of Rule 17(a).

\begin{itemize}
\item \textsuperscript{122} \textit{Id.} at 147.
\item \textsuperscript{123} \textit{Cf.} Executive Jet Aviation, Inc. v. United States, 507 F.2d 508, 512 (6th Cir. 1974) (stating that when the insurer's liability is contingent there is at least some indication of a true loan).
\item \textsuperscript{124} \textit{Id.}
\item \textsuperscript{125} \textit{Acro Automation Sys., Inc. v. Iscont Shipping Ltd.}, 706 F. Supp. 413, 421 (D. Md. 1989); \textit{see supra} text accompanying notes 103-10.
\item \textsuperscript{126} \textit{See supra} text accompanying note 103.
\item \textsuperscript{127} \textit{See supra} text accompanying notes 6-8.
\item \textsuperscript{128} \textit{See supra} note 15 and accompanying text. One commentator has suggested that if insurers should not be the real parties in interest, the legislature changing the real-party-in-interest rule is preferable to the courts creating a legal fiction. Kessner, \textit{supra} note 15, at 466.
\item \textsuperscript{129} \textit{See supra} note 10.
\end{itemize}
Whether or not the policy behind Rule 17(a) is violated by not substituting the insurer as the real party in interest, the text of the Rule is violated. The Acro court, without explanation, circumvented the established interpretation of Rule 17(a) — that the insurer is the real party in interest — in favor of policy reasons that are not expressed in the text of the Rule. Somehow the court shifted to the defendant the burden of proving why it should be allowed to use Rule 17(a).130 Rule 17(a) operates to expose the fact that the insurer is the real plaintiff; thus the insurer has an improper purpose in seeking anonymity.131 Even if the equities truly were balanced between the defendant’s improper purpose in trying to expose plaintiff’s insurance and plaintiff’s improper purpose in trying to circumvent a rule of civil procedure, the logical presumption still would be in favor of the Rule, which presumably already balances these equities.

D. JURY PREJUDICE

The Acro court probably required the defendant to demonstrate why it should be allowed to use Rule 17(a) because of its concern that jury prejudice against insurance companies would cause unjust results in the underlying suit between the insurer and the carrier.132 To an impartial observer, this concern seems more important than the defendant’s interest in taking advantage of a procedural rule. The court, however, never presents empirical justification for its notion of jury prejudice. In the absence of empirical data, one is left only with common sense arguments.133

On one hand, jurors may not like insurance companies;134

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130. Acro Automation Sys., Inc. v. Iscont Shipping, Ltd., 706 F. Supp. 413, 420-21 (D. Md. 1989); see supra text accompanying note 107. But see supra text accompanying note 77 (noting that burden is on plaintiff to show why the court should not allow defendant to use Rule 17(a)).

131. See supra note 81.

132. See supra text accompanying note 110.

133. Courts that have analyzed the potential effect of jury prejudice against plaintiff insurers have concluded that it is not significant. Cf. Smith v. Earp, 449 F. Supp. 503, 506-07 (W.D. Ky. 1978) (rejecting jury prejudice argument against joinder of insurer in motor vehicle accident case because “no-fault” insurance is a matter of common knowledge); Pace v. General Elec. Co., 55 F.R.D. 215, 218-19 (W.D. Pa. 1972) (arguing that jurors are not prejudiced against insurance companies).

134. See 18 G. COUCH, R. ANDERSON & M. RHODES, supra note 8, § 78:30, at 496-97. For discussions noting that these general principles do not apply well in the case of insurer subrogation (plaintiff insurance companies), see Kennedy, supra note 58, at 714-15; Broeder, The Pro and Con of Interjecting Plain-
on the other hand, jurors probably have no great sympathy for the defendants in these cases either.\textsuperscript{135} For example, in \textit{Acro} the defendants were eleven international shipping companies,\textsuperscript{136} and the parties disputed neither the fact that the goods were damaged nor the monetary value of that damage.\textsuperscript{137} In that case, jury prejudice was unlikely to have an effect because the only choice in determining the cause of the damage was between defendant's negligence and some sort of natural disaster. Rather than acting on enmity toward the plaintiff insurer, jurors might even be sophisticated enough to know that international shipping companies are insured too.\textsuperscript{138}

As a general proposition, jury prejudice against insurance companies would seem to be more relevant when the insurance company is a defendant.\textsuperscript{139} Juries probably award excessive damages based on deep-pocket theories.\textsuperscript{140} When an insurance company sits as plaintiff, however, the issue is not whether the damages awarded will be excessive, but whether the jury will award any damages. Given insurance companies' generally conservative nature in paying claims, the insured almost certainly will have a great deal of proof for its claim. The insurer will present the same proof of damages to the jury that the insured presented to the insurer. The insurer is merely asking the jury to assign a culpable party. Again, jury prejudice against insurance companies as plaintiff must operate within a very narrow


\textsuperscript{135} For an example of a large defendant corporation asserting that the jury will be prejudiced against it, see Pace v. General Elec. Co., 55 F.R.D. 215, 218-19 (W.D. Pa. 1972). The \textit{Pace} court rejected this argument, along with the argument that jurors are prejudiced against plaintiff insurers. \textit{Id}.


\textsuperscript{137} \textit{Id}. at 415.

\textsuperscript{138} See Kennedy, supra note 58, at 686.

\textsuperscript{139} After first finding that jurors generally disfavor insurance companies, Broeder, The University of Chicago Jury Project, 38 NEB. L. REV. 744, 754 (1959), one commentator subsequently found that joinder of a plaintiff insurer actually benefited the plaintiff insured. Broeder, supra note 134, at 276-83.

\textsuperscript{140} 18 G. COUCH, R. ANDERSON & M. RHODES, supra note 8, § 78:30, at 497.
range, because even strong jury prejudice cannot overcome clear evidence. In the event jury prejudice causes injustice, the court can overturn an erroneous jury verdict under Rule 50(b).

CONCLUSION

The validity of loan receipt agreements has been an ongoing controversy in the twenty years since City Stores created a split among the circuits. The better-reasoned cases hold that loan receipts are invalid; the insurer remains the real party in interest and must bring suit in its own name. Courts should not use vague concerns about jury prejudice and the policies behind Rule 17(a) to circumvent the clear text of the Rule. Insurance companies must stand as the real party in interest unless, as in Luckenbach, there is a valid independent reason to allow the insured to be the named plaintiff. Luckenbach, the landmark case holding loan receipts valid, should be limited to its facts. The Supreme Court and the circuits that have not yet spoken on this issue should follow City Stores and Executive Jet and hold that loan receipts are invalid when used to circumvent Rule 17(a), thus generally requiring insurers to sue in their own names as real parties in interest.

E. Michael Johnson

141. Fed. R. Civ. P. 50(b) (judgment notwithstanding the verdict).