Seizure and Return of Cryptocurrency: Existing Efforts Under California State Law

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ABSTRACT

Scam organizations steal billions of dollars each year and use cryptocurrency to launder the proceeds.[1] This article examines existing methods for cryptocurrency returns under California state law, specifically discussing a popular method that combines California's return of property laws with presumption-based asset tracing methods. First, the article touches on the epidemic of online scams and their use of cryptocurrency. Transnational criminal organizations are the most common perpetrators of these scams, rendering prosecution difficult and creating an increased need for other tools. From there, the article examines tracing in federal asset forfeiture cases. The article briefly highlights research that has thoroughly documented federal circuit splits regarding whether to permit tracing through commingled, fungible assets. Thereafter, the article discusses how California's laws differ from federal asset forfeiture by requiring proof that the property is stolen and requiring the victim to establish title to the property to obtain its return. The article examines pitfalls and potential inequities that can result if courts award title to seized cryptocurrency using different presumption-based tracing methods. Finally, the article proposes that civil in rem forfeiture proceedings provide a more structured and effective tool and suggests that the Legislature instead consider a forfeiture statute.[2]

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1. B. CHAD YARBROUGH, FEDERAL BUREAU OF INVESTIGATION INTERNET CRIME REPORT 10-11 (2024), https://www.ic3.gov/AnnualReport/Reports/2024_IC3Report.pdf.

2. *See, e.g.*, 18 U.S.C. § 981; *see also* FLA. STAT. §§ 932.701–.7062 (2018).

I. THE ONLINE SCAM EPIDEMIC

Pro Publica reported in 2022 that transnational organized crime in Southeast Asia traffics victims into forced participation in scam centers.[3] The organizations force trafficking victims to victimize others in transnational fraud schemes. The fraud victims also suffer. Victims of the fraud schemes are frequently left personally and financially devastated, and some even commit suicide.[4]

Through deceptive or abusive tactics, these sophisticated organizations obtain and then use knowledge about the victim, their family, their friends, and their finances. The scams can be quite convincing. The organization may use fake websites or other online methods to establish legitimacy. The scammers may pretend to be law enforcement, obtain and recite bank account balances or other confidential information, or spoof a real telephone number. When the victim seeks return of their property, the scammers may get more money by demanding the payment of taxes or even by imitating a scam recovery service. The organization may have multiple people working as fake law enforcement,

3. Pro Publica noted that "[w]orkers from around Asia are tricked into going to Cambodia, Laos or Myanmar for seemingly well-paid jobs that instead trap them inside scam sweatshops run by Chinese criminal syndicates. Those who resist directives to engage in online fraud face beatings, food deprivation or worse." Cezary Podkul, *Authorities Raid Alleged Cyberscam Compounds in Cambodia*, PROPUBLICA (Oct. 3, 2022), https://www.propublica.org/article/pig-butchering-scams-raided-cambodia-apple-trafficking.

4. Teele Rebane & Ivan Watson, *Killed by a scam: A father took his life after losing his savings to international criminal gangs. He's not the only one*, CNN (June 20, 2024), https://www.cnn.com/2024/06/17/asia/pig-butchering-scam-southeast-asia-dst-intl-hnk/index.html.

banks, scam recovery companies, or other roles at the same time. As long as they believe that new forms of abuse or deceit will succeed, they may continue to try whatever will convince the victim to send more money.

Cryptocurrency's underlying technology lends itself to laundering stolen proceeds. Transfers are immediate and irreversible. Victims send their money to an address or smart contract that places it under the scam organization's control. Scammers may instruct victims to use a crypto ATM or cryptocurrency exchange service to convert their fiat money into cryptocurrency. Mules may accept victims' fiat currency and convert it into cryptocurrency for the organization. Once the victim's money is in cryptocurrency and under the control of the scam organization, the organization begins the process of transferring and laundering the proceeds, often while the victim believes the money is safe and continues to send funds. Easy automation and decentralized services can create quick transactions that obfuscate the origins of illicit proceeds, all while avoiding a financial system's anti-laundering checks and controls.

The problem is widespread. The National Money Laundering Risk Assessment noted that fraud "continues to be the largest driver of money laundering activity in terms of the scope of activity and volume of illicit proceeds, generating billions of dollars annually."[5] Researchers estimate that transnational organized crime stole and laundered over $75 billion via cryptocurrency from 2021 to 2024.[6] Some individual California scam victims lost millions, such as a seventy-one-year-old California man who lost $2.1 million.[7] Overall, California saw 96,265 victims report over $2.5 billion lost to scams in 2024, ranking first among states for both number of victims and overall loss amount in the FBI's annual Internet Crime Report.[8] Approximately 20% of the California complainants (19,508) specifically referenced cryptocurrency in their complaints. Those complaints accounted for approximately half of the overall fraud loss amount ($1.3 billion). The problem got worse in the recently released 2025 report. California saw 116,414 victims report over $3.7 billion lost to scams in 2025, again ranking first among states for both number of victims

5. U.S. DEP'T OF TREASURY, 2024 NATIONAL MONEY LAUNDERING RISK ASSESSMENT 4 (2024), https://home.treasury.gov/system/files/136/2024-National-Money-Laundering-Risk-Assessment.pdf.

6. John M. Griffin & Kevin Mei, *How Do Crypto Flows Finance Slavery? The Economics of Pig Butchering* (Feb. 29, 2024), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4742235 [https://dx.doi.org/10.2139/ssrn.4742235]

7. Poppy McPherson & Tom Wilson, *Crypto scam: Inside The Billion-Dollar 'Pig-Butchering' Industry*, REUTERS (Nov. 23, 2023), https://www.reuters.com/investigates/special-report/fintech-crypto-fraud-thailand/; *see also* Stephanie Sierra, *Bay Area Investor Loses $1.2m In Crypto Scam As Fraud Cases Triple Across CA*, ABC (July 27, 2022), https://abc7news.com/crypto-scam-pig-butchering-fbi-silicon-valley/12077745/.

8. YARBROUGH, *supra* note 1, at 20-21.

and overall loss amount.[9] Again approximately 20% (20,878) of the complaints referenced cryptocurrency but accounted for over $2 billion of the loss.[10]

Tracing, locating, and returning those proceeds can be part of law enforcement efforts to combat transnational scam organizations,[11] along with education and disruption efforts to prevent further victimization. Many California victims are losing funds to organized criminal groups. These groups collect and then commingle victims' funds in massive and complex patterns using cryptocurrency. Efforts to recover the cryptocurrency held by such organizations present a new twist to old problems. When should the government be able to trace fungible property to combat obfuscation efforts? What should be the standards of proof for such actions? What presumptions are permissible for meeting those standards? What should the government do with seized fraud proceeds?[12] An effective answer requires understanding how scam organizations launder fraud proceeds and either the ability to apply existing laws and methods or the creation of new laws.

II. FRAUD AND MONEY LAUNDERING OF CRYPTOCURRENCY

To best understand the movement of scam proceeds in cryptocurrency, one should use the classic money-laundering framework of placement, layering, and integration. Placement is the process of putting "dirty" funds into the financial system. During the scam, the scammer often convinces the fraud victim to put the dirty funds into a cryptocurrency form under the organization's control. Though now under the launderer's control, the cryptocurrency is still clearly traceable to the victim's transaction, so the criminal organization needs to layer the dirty funds.

Layering is the second stage of the model, where the launderer obfuscates the origin of the dirty funds by moving them in complex financial transactions that make it difficult to link the funds to their criminal origin. The organization can employ several techniques. Classic methods include commingling,

9. JOSE A. PEREZ, FEDERAL BUREAU OF INVESTIGATION INTERNET CRIME REPORT 27-30 (2025), https://www.ic3.gov/AnnualReport/Reports/2025_IC3Report.pdf.

10. *Id.* at 56-57.

11. Cyrus Favriar, *'Pig Butchering' Scam Victim to Get Money Back from Binance, Law Enforcement Says*, FORBES (Jul. 1, 2022), https://www.forbes.com/sites/cyrusfarivar/2022/07/01/pig-butchering-crypto-scam-victim-to-get-money-back-from-binance-law-enforcement-says/; *see also* Cyrus Favriar, *Cryptocurrency Scam Victim Who Lost Over $1 Million to Get Over $100,000 Back, Prosecutor Says*, FORBES (Oct. 22, 2022), https://www.forbes.com/sites/cyrusfarivar/2022/10/22/cryptocurrency-scam-victim-who-lost-over-1-million-to-get-over-100000-back-prosecutor-says/; *see also* Eric Johansson, *Meet the prosecutor who claws back millions from crypto scams: 'I've had grown men crying on the phone to me'*, DLNEWS (June 3, 2023), https://www.dlnews.com/articles/regulation/meet-erin-west-the-prosecutor-who-hunts-for-crypto-scammers/.

12. These are questions courts have struggled with in various contexts for some time. *See, e.g.*, Austin W. Scott, *The Right to Follow Money Wrongfully Mingled with Other Money*, 27 Harv. L. Rev. 125 (1913).

aggregating, and splitting funds through different accounts. Cryptocurrency-specific methods include using mixers that combine transactions to make outputs more difficult to trace, using a centralized exchange or decentralized smart contract to exchange one cryptocurrency for another, or even using cross-chain swaps and bridges to switch blockchains and/or cryptocurrencies.

The final stage of the model is integration. During integration, the funds become available as a clean asset for the organization's use in the legitimate economy. Integration transactions often provide a legitimate explanation for the origin of the funds. Organizations can convert cryptocurrency back into clean fiat currency, real property, or other tangible assets through false transactions with knowing collaborators or legitimate sales to actual purchasers. However, cryptocurrency itself has become a part of the modern economy. Therefore, integration does not require conversion to fiat currency. The transactions that provide a legitimate "clean" origin story can use cryptocurrency. If an organization performs both obfuscation and integration using only cryptocurrency, the organization can obtain clean cryptocurrency income or investment returns without ever having to involve other financial systems.[13]

A. Cryptocurrencies That Store and Exchange Value Like Bank Accounts Are Fungible

Currency in a bank account is fungible, meaning that every unit of currency is indistinguishable from every other unit. For example, assume that a bank account receives five deposits of one dollar and then the owner of the account spends one dollar by sending it to another account. There is no way to link the spent dollar to a single deposit because all five dollars in the account are the same and cannot be differentiated from one another. The fungible nature of currency stored in a bank account is a useful feature for money laundering. Cryptocurrencies can also be fungible, but not all cryptocurrencies operate in that manner.

Cryptocurrencies exchange value by transferring units of the cryptocurrency from an original owner to a new owner via a transaction secured by cryptography. Many cryptocurrencies store transaction information on a decentralized blockchain, which is a distributed ledger that records the transactions across computers in a way that is permanent, secure, and immutable. Many blockchains are public and the history of all transactions can be examined. Determining whether a given cryptocurrency is fungible requires examining technically how the cryptocurrency stores and transfers value.

The most well-known cryptocurrency, Bitcoin, is not necessarily fungible. Transfers do not occur via a single data structure of account numbers with associated balance information. Instead, Bitcoin uses unspent transaction outputs

13. The more legitimate cryptocurrency transactions become for real-world financial exchange, the less important it is to make a timely integration back into the fiat currency system.

("UTXO"). Each user sending a transaction must identify all existing UTXOs to be spent as inputs and provide the correct unlocking script for each of those UTXOs. The transaction spends the input UTXOs, so they no longer exist as UTXO because they are listed on the blockchain as inputs to a transaction. However, the transaction also creates new UTXOs that are available to spend and are also associated with the same transaction. Therefore, the transaction data recorded on the blockchain links transaction outputs to the previous transactions that created the transaction inputs. Because Bitcoin requires the user (or more commonly their wallet software) to define which existing UTXOs will be spent, there is a technological link that can be followed.[14] For this reason, commingling bitcoins by sending them to the same "address"[15] does not necessarily complicate tracing in the same manner as depositing two dollars into the same bank account.

However, many other cryptocurrencies store data about value and value exchange using a ledger of addresses and balances, just like banks store account balance information. Cryptocurrencies that store balances in this manner are fungible, like fiat money. For example, Ethereum's native cryptocurrency, called Ether, stores addresses and associated balances as part of the state of the Ethereum Virtual Machine ("EVM"). An Ethereum address is a unique identifier for receiving and sending Ether on the Ethereum blockchain. There is a single format. Each private key controls one single Ethereum address, which is a hash of the public key associated with that private key. The EVM maintains a single data structure that tracks the Ether balance associated with each address, adding to the value when Ether is received in a transaction and subtracting when Ether is spent in a transaction. Therefore, an Ethereum address is comparable to a bank account.

Similarly, Ethereum supports specialized digital coins, called tokens. While Ether is a native coin created and governed by the code that runs the Ethereum blockchain, tokens are additional cryptocurrencies created on top of the existing Ethereum blockchain. Tokens are created and governed by code that a user deploys onto the blockchain as a "smart contract." Smart contracts consist of public, permanent, and immutable code, as well as mutable data storage in the

14. While the output UTXOs are linked to the input UTXOs by their selection for the transaction, there is not necessarily any logical significance or meaning to the connection. This is because "[d]ifferent wallets use different strategies when choosing which inputs to use in a payment, called *coin selection*." ANDRES M. ANTONOPOULOS & DAVID A. HARDING, *How Bitcoin Works*, *in* MASTERING BITCOIN 20 (2024) (emphasis in original). The links in a UTXO tracing do not necessarily show that the user selected a specific coin for that particular transaction, because usually software does it without input.

15. A Bitcoin "address" is a unique identifier used to receive and spend Bitcoin. Every Unspent Transaction Output ("UTXO") is locked and must be provided the appropriate unlocking script to spend the UTXO. Bitcoin users generate the unlocking script for UTXOs locked to a particular "address" by using the private key and the rules related to that address format. Different address formats have been added to Bitcoin over time. There is not a single address that contains all the UTXOs spendable with a user's private key, like a bank account number.

EVM. For a fungible token, the contract maintains a list of all Ethereum addresses and their associated token balances, just like a bank account.

Understanding the code that transfers Ether or fungible tokens is like understanding the wire transfer process for dollars. The process is defined, but coin selection is arbitrary because currency in an account is fungible. For example, Tether ("USDT") is a fungible token on the Ethereum blockchain.[16] When sending a Tether token, the sender submits a transaction that calls the Tether smart contract address and then passes the recipient address and amount to transfer as variables. The EVM processes the transaction and it succeeds or fails. If the transfer succeeds, then the USDT smart contract will have updated the relevant balances for the sender and recipient in its data storage. If the transaction fails, then the USDT smart contract balances remain as they were. The transfer function does not link the transaction to any previous deposit transactions because it only updates balance information.

Because USDT is fungible, each time a user sends tainted USDT, the tainted USDT becomes commingled with all other USDT at the receiving address. If the receiving user sends multiple transactions of USDT out of their address after receiving tainted USDT, which transaction contains the tainted USDT is not defined by the technology. This is true for all truly fungible cryptocurrencies on Ethereum. Like bank accounts, tracing fungible tokens on the Ethereum blockchain necessarily includes some degree of choice as to which transaction or movement of funds contains tainted funds.

B. Fungible Currencies Can be Traced Using Presumption-Based Methods

This section discusses several presumption-based methods for bank account tracing, which can be applied to cryptocurrency tracing on account-based cryptocurrencies like Ether or USDT. Presumption-based tracing methods are derived from inventory control methods or other logical principles. These methods include "proceeds-in, first out," (PIFO) "first-in, first-out" ("FIFO"), "last-in, first-out" ("LIFO"), the pro rata rule, as well as the lowest intermediate balance rule ("LIBR").[17] Each of these methods uses a different presumption for tracing through an account containing commingled funds. Neither the American Institute of Certified Public Accountants nor the Association of Certified Fraud

16. Researchers estimate that Tether ("USDT") has been most popular with transnational organized crime scammers, followed closely by ether ("ETH"), and Circle ("USDC"). Griffin & Mei, *supra* note 6, at 16.

However, Tether made headlines in 2023 by burning and reissuing USDT at addresses associated with fraud. Shaun Waterman, *U.S. Prosecutors Call Huge Cryptocurrency Fraud Seizure a 'Game Changer'*, NEWSWEEK (Dec. 7, 2023), https://www.newsweek.com/us-prosecutors-crypto-fraud-seizure-tether-binance-scams-currency-pig-butchering-1849885. Unsurprisingly, the same researchers saw increasing use of the decentralized DAI stablecoin starting in 2023.

17. Joel Glick, *Tracing Commingled Funds*, BERKOWITZ POLLACK BRANT (Nov. 10, 2023), https://www.bpbcpa.com/tracing-commingled-funds-by-joel-glick-cpa-cff-cfe-cgma/.

Examiners has specific best practices for determining the asset tracing method to apply to a given set of facts.[18]

Presumption-based methodologies work in different ways and will often yield different results depending on which is chosen. These different outcomes are driven by the presumptions underlying the methodology. For example, the FIFO method presumes that the first funds deposited into the account are the first funds spent. If there are two deposits of $100 each, followed by a withdrawal of $100, that withdrawal constitutes 100% of the first depositor's funds. Alternatively, LIFO presumes that the most recent funds deposited into the account are the first to be spent. If there are two deposits of $100 each, and a withdrawal of $100, that withdrawal constitutes 100% of the second depositor's funds. The pro rata rule assigns withdrawals proportional to the deposits before the withdrawal. If there are two deposits of $100 each and a withdrawal of $100, that withdrawal constitutes 50% of the first depositor's funds and 50% of the second depositor's funds.[19]

FIFO tracing requires the tracer to determine the balance at the time of the deposit. LIFO tracing does not require calculating the balance but does require accounting for subsequent deposits. Either can become complicated in accounts with a lot of activity. "Drugs-in, first out," also known as "proceeds-in, first out" ("PIFO") is another common presumption-based method. It is easier than FIFO or LIFO.

PIFO is like LIFO, except it disregards any other deposits entering the account and follows the first transfer exiting the account after the tainted deposit. For example, assume a $100 deposit of tainted funds, such as drug sales proceeds or fraud proceeds, followed by a $100 deposit of other funds irrelevant to the investigation, followed by two $100 withdrawals into two different accounts. After the withdrawals, which account contains the tainted funds? PIFO concludes that the first $100 withdrawal contained all the tainted funds, while LIFO attributes that withdrawal to the subsequent, most recent deposit, concluding instead that the second withdrawal contained all the tainted funds.

LIBR is an entirely different method with its own presumption. LIBR presumes that legitimate funds are spent before tainted funds so the full amount of tainted funds remains in the account until all of the account's legitimate funds are spent. Accordingly, if there are two deposits of $100 each, one tainted and one not, followed by a withdrawal of $100, then LIBR concludes that the tainted funds remain in the account because they assume they withdraw untainted funds first. The LIBR rule can be applied with or without a concept of replenishment

18. Jordan Sandberg, *Following the Money: Forensic Accounting Tracing Methods & Best Practices*, HKA (Mar. 13, 2024), https://www.hka.com/following-the-money-forensic-accounting-tracing-methods-amp-best-practices/.

19. This rule rapidly creates a high degree of complexity and is not commonly used in actual tracing.

which means that new untainted funds can be used to restore the tainted funds' balance.[20]

Can California law enforcement use these methods to return cryptocurrency to scam victims using California's return of property law?[21] Using presumption-based tracing to identify commingled funds as stolen property parallels the use of such methods in federal asset forfeiture to identify commingled funds as traceable fraud proceeds. However, only some federal courts approve the use of such methods for asset forfeiture. Accordingly, this article discusses the well documented circuit split regarding the permissibility of tracing evidence in federal asset forfeiture proceedings. It then discusses the differences created by applying the same methods to California's return of property law.

C. Tracing Commingled Funds in Federal Asset Forfeiture

Congress passed federal civil asset forfeiture laws that allow for a complaint proceeding *in rem* against suspected property. Claimants are required to file their claims and answer the complaint. These statutes allow for civil discovery, motion practice, including summary judgment, and ultimately trial.[22] Such processes are a powerful tool in combatting money laundering of cryptocurrencies by transnational organized crime. Congress explicitly authorized forfeiture of any property derived from or "traceable to" specific criminal activities, including frauds, under a "proceeds" theory.[23] To prevail under a proceeds theory, the government must prove the funds to be seized are "traceable to" the relevant criminal activity. Similarly, if money laundering can be proven, the government can proceed under an "instrumentality" theory.[24] Under this theory, the scope of seizure expands to include any property "involved in" the money laundering, including the other monies used to obfuscate origin

20. Marylee Robinson & Jason Wright, *A Taxonomy of Tracing Rules: One Size Does Not Fit All*, STOUT (Sep. 17, 2018), https://www.stout.com/en/insights/article/a-taxonomy-tracing-rules-one-size-does-not-fit-all.

21. CAL. PENAL CODE §§ 1407–1413.

22. Shirley U. Emehelu, *A Shot in the Dark: Using Asset Forfeiture Tools to Identify and Restrain Criminals' Cryptocurrency*, 66 DOJ J. FED. L. & PRAC. 81, 94 (2018).

23. 18 U.S.C. § 981(a)(1)(C) (permitting the seizure of "Any property, real or personal, which constitutes or is derived from proceeds traceable to a violation of section [listed statutes] of this title or any offense constituting 'specified unlawful activity' (as defined in section 1956(c)(7) of this title), or a conspiracy to commit such offense.").

24. *See, e.g.*, United States v. Certain Accounts, together with all Monies on Deposit Therein, 795 F. Supp. 391, 397 (S.D. Fla. 1992); *see also* United States v. Certain Funds on Deposit in Account No. 01-0-71417, Located at Bank of New York, 769 F. Supp. 80, 84 (E.D.N.Y. 1991); United States v. All Monies In Account No. 90-3617-3, Israel Disc. Bank, New York, N.Y., 754 F. Supp. 1467, 1472 (D. Haw. 1991).

and destination.[25] Congress passed multiple forfeiture statutes,[26] including provisions specifically designed to permit the forfeiture of fungible property.[27] However, federal courts disagree about whether to permit presumption-based tracing through commingled funds in asset forfeiture actions. A 2019 law review article titled "Tracing Commingled Funds in Asset Forfeiture"[28] concluded there are currently two competing approaches that "stand opposed to each other, but few courts address the cases together, discussing their merits." The author termed the two approaches "dual presumption" and "no presumption", proposing the split be reconciled with the "single presumption" approach.

The "dual presumption" approach originates in the Second Circuit's 1986 decision in *United States v. Banco Cafetero Panama* ("*Banco Cafetero*").[29] In *Banco Cafetero*, the government sought forfeiture of several bank accounts containing drug proceeds under 21 U.S.C. § 881, which authorizes seizure of "proceeds traceable to" drug sales. The appeal challenged whether the funds seized were "traceable to" drug transactions. The government argued that funds are "traceable" if they can be traced using either a "drugs in, first out" methodology or the lowest intermediate balance rule ("LIBR"), which the government can select at their discretion. Accordingly, the government could identify an account where drug proceeds went and apply LIBR to determine whether the balance remained in that account. If the funds remained under LIBR, the government would seize those funds. However, if the funds no longer remained under LIBR, the government could then continue the trace under "drugs in, first out" and follow the proceeds to the next account or purchase, proceeding until reaching an asset to seize.

The Second Circuit accepted the government's right to select either path based on the probable cause standard and the fact that probable cause can exist for two competing inferences at the same time.[30] The *Banco Cafetero* Court explained:

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25. 18 U.S.C. § 981(a)(1)(A) (permitting the seizure of "Any property, real or personal, involved in a transaction or attempted transaction in violation of section 1956, 1957 or 1960 of this title, or any property traceable to such property."); *see generally* Neal B. Christiansen & Julia E. Jarrett, *Forfeiting Cryptocurrency: Decrypting the Challenges of A Modern Asset*, 67 DOJ J. FED. L. & PRAC. 155, 168 (2019).

26. *Compare* 21 U.S.C. § 881, *with* 18 U.S.C. § 981 (permitting the seizure of fungible, real, and personal property).

27. United States v. Contents in Acct. No. 059-644190-69, 253 F. Supp. 2d 789, 793 (D. Vt. 2003) (explaining that "Congress enacted 18 U.S.C. § 984 to deal with the problem of traceability for cash and other fungible property."); *see generally* 18 U.S.C. § 984(a)(1).

28. Sean Michael Welsh, *Tracing Commingled Funds in Asset Forfeiture*, 88 MISS. L.J. 179, 218 (2019).

29. United States v. Banco Cafetero Panama, 797 F.2d 1154, 1154 (2d Cir. 1986).

30. *Id.* at 1160–61 ("In almost all cases, once the Government has shown probable cause to believe that a person has sold drugs and has deposited the proceeds of a drug sale into a bank account, there will be probable cause to believe that the bank account contains "traceable proceeds" of the sale (if the balance has not fallen below the amount of the deposit) *and* probable cause to believe that a withdrawal contains such "traceable proceeds" (if the withdrawal exceeds the deposit).").

> [T]here is a plausible argument to be made *either* that the account contains the "traceable proceeds" of the tainted deposit (so long as the balance has not fallen below the amount of the tainted deposit) *or* that any withdrawal (in excess of the tainted deposit) contains the "traceable proceeds" of such a deposit. Which approach reflects reality in any particular case will depend on the precise circumstances. For example, if a depositor placed a $175 check from his automobile insurer in payment of a damage claim into an account that contained $100 from a drug sale and the next day paid a $175 bill for car repairs, a fact-finder would be entitled to conclude that the $175 withdrawal did not contain "traceable proceeds" of the drug transaction but solely the "traceable proceeds" of the insurance payment, with the tainted deposit remaining in the account. Obviously few cases will present facts that neatly match untainted deposits with withdrawals, and the real question therefore becomes which side bears the risk of the inevitable uncertainty that will arise in most cases. Congress has answered that question in the Government's favor by assigning it a lenient burden of proof in obtaining forfeiture of "traceable proceeds" of drug transactions.[31]

Accordingly, in federal asset forfeiture proceedings following *Banco Cafetero*, once the government established probable cause, using either method, or both, the burden shifted to the claimant to prove they are an innocent owner of the seized funds.[32] In dicta, *Banco Cafetero* anticipated the difficulty the fungible nature of property would present to a claimant attempting to prove innocent ownership under a preponderance standard, explaining, "No doubt uncertainty caused by the fungibility of money will make it difficult and in many cases impossible for claimants to satisfy this burden. But it is precisely the function of burden of proof rules to determine which party loses where evidence is lacking or at best ambiguous."[33]

The contrasting "no presumption" approach rejects presumption-based tracing and originates in the Third Circuit's 1996 decision of *United States v. Voigt*.[34] *Voigt* decided to apply the preponderance of the evidence standard to a criminal forfeiture action.[35] The case involved a situation where "proceeds had been commingled with other funds, and … those funds were further 'diluted' by numerous intervening deposits and withdrawals."[36] *Voigt* held that tracing commingled assets is unworkable given the preponderance of the evidence

31. *Id.* at 1159–60.

32. *See, e.g.*, United States v. Real Prop. 874 Gartel Drive, Walnut, Cal., 79 F.3d 918, 923 (9th Cir. 1996) (explaining that the statute required only a showing of "probable cause that the defendant property was involved in the alleged underlying offense, following which the burden shifts to the claimant to establish by a preponderance of the evidence that the defendant property is not subject to forfeiture."); *see, e.g.*, United States v. Sellers, 848 F.Supp. 73 (E.D. La. 1994) (finding a grand jury indictment sufficient for a forfeiture showing because it is necessarily made with probable cause).

33. *Banco Cafetero*, 797 F.2d at 1161.

34. United States v. Voigt, 89 F.3d 1050, 1082 (3d Cir. 1996).

35. *Id.* at 1082; *see generally* 18 U.S.C. §§ 1982 & 1956.

36. *Voigt*, 89 F.3d at 1084.

standard of proof.[37] However, *Voigt* permitted the government to seek substitute property because the criminal forfeiture laws included explicit substitute assets provisions.[38] Following *Voigt*, the Third, Fifth, and Eleventh Circuits reject *Banco Cafetero* and do not permit presumption-based tracing through commingled funds.[39]

Congress enacted the Civil Asset Forfeiture Reform Act ("CAFRA") in 2000, changing the standard of proof for civil asset forfeiture from probable cause to a preponderance of the evidence.[40] *Banco Cafetero* had relied on the nature of probable cause[41] as its justification, explaining that two mutually exclusive scenarios can both have probable cause at the same time. *Voigt*, by contrast, is consistent with the logic that two mutually exclusive options cannot simultaneously be "more likely than not." Despite the enactment of CAFRA, the Second, Sixth, and Ninth Circuits continue to follow *Banco Cafetero*.[42]

The "single presumption" approach proposes permitting the government to use any single accounting method, so long as it is consistently applied.[43] This

37. *Id.* at 1087 (explaining the view that tracing is impossible based on the preponderance standard, "Where the property involved in a money laundering transaction is commingled in an account with untainted property, [], the government's burden of showing that money in the account or an item purchased with cash withdrawn therefrom is 'traceable to' money laundering activity will be difficult, if not impossible, to satisfy. While we can envision a situation where $500,000 is added to an account containing only $500, such that one might argue that the probability of seizing 'tainted' funds is far greater than the government's preponderance burden (50.1%), such an approach is ultimately unworkable."); *but see* United States v. Stewart, 185 F.3d 112, 129 (3d Cir. 1999) (permitting tracing and forfeiture where the tainted funds were directly deposited into an account and it is an "account that has been frozen from the time of the illegal transfer but that also contains untainted money.").

38. *Voigt*, 89 F.3d at 1088 (holding that the government may use substitute assets when directly forfeitable property is unavailable).

39. Welsh, *supra* note 28, at 213-14 (explaining that "The Third Circuit's opinions . . . have been adopted expressly by the Fifth and Eleventh Circuit Court of Appeals. The Tenth Circuit and one of its district courts have expressed support for *Voigt*, but have come short of adopting the approach because they have not had the chance to consider such a case."); *see, e.g.*, In re Rothstein, Rosenfeldt, Adler, P.A., 717 F.3d 1205, 1213 (11th Cir. 2013) (finding "The sheer volume of financial information available and required to separate tainted from untainted monies in this case leads us to the conclusion that it is far more appropriate to apply the Third Circuit's rule in *Voigt* than the exception to that rule it lays out in *Stewart*.").

40. Pub. L. No. 106-185, Apr. 25, 2000, 114 Stat. 202; *see generally* 18 U.S.C. § 983(c)(1) (setting forth that "the burden of proof is on the Government to establish, by a preponderance of the evidence, that the property is subject to forfeiture").

41. *See, e.g.*, *Fla. v. Harris*, 568 U.S. 237, 243–44 (2013) (citing *Illinois v. Gates*, 462 US 213, 235 (1983) (differentiating that, "Finely tuned standards such as proof beyond a reasonable doubt or by a preponderance of the evidence . . . have no place in the [probable-cause] decision.").

42. *See, e.g.*, *Acct. No. 059-644190-69*, 253 F. Supp. 2d at 795 (finding that "*Banco Cafetero* remains good law in precisely the situation presented by the facts of this case."); *see generally* Welsh, *supra* note 28, at 205 (explaining that "The Second Circuit is the only Court of Appeals to expressly adopt the *Banco Cafetero* accounting methods. However, district courts in the Sixth and Ninth Circuits have followed *Banco Cafetero* exclusively."); *see also* United States v. Dillon, No. 1:16-CR-00037-BLW, 2022 WL 2105974, at *4 (D. Idaho June 10, 2022) (footnote omitted) (noting that "although district courts in the Ninth Circuit have followed *Banco Cafetero*, the Ninth Circuit has not expressly adopted LIBR (or any approach discussed in *Banco Cafetero*) in the criminal asset-forfeiture context.").

43. Welsh, *supra* note 28, at 205.

suggested "single presumption" methodology narrows the discussion and debate from uncertainty at each transaction to uncertainty at a single point up for debate. As proposed,

> [T]he Single Presumption Method yields two options in every case. For each asset, the Government would apply the LIBR through all transactions and determine how much of the asset it seeks is forfeitable. The Government would then do the same analysis with the "proceeds first" rule, again determining how much of the asset is forfeitable. The Government would then compare the two methods and choose the better method. Instead of innumerable combinations, there are now only two. Instead of numerous choices about which method to apply at each stage, there is now only one choice after the analysis has been performed. The Single Presumption Method is easier to apply and easier for the court to test. This method removes the *mystery* of tracing and makes it easier to explain to jurors.[44]

This approach is a way to define what is "traceable." However, the "single presumption" approach is unlikely to be any more appealing to proponents of the "no presumption" view than the "dual presumption" approach, because it fails to resolve the fundamental logical fallacy that two mutually exclusive scenarios cannot both be "more likely than not." Choosing between presumptions still requires the court to select one conclusion as "more likely than not" true when another conclusion has an equally valid claim.

This section highlights the different approaches courts have taken to tracing evidence in cases involving federal asset forfeiture law. Although these differing approaches are instructive, California courts are not bound by federal precedent. California courts must also consider the historical use of tracing evidence in California law and the specifics of return of property proceedings for guidance.

III. ASSET TRACING IN VARIOUS AREAS OF CALIFORNIA LAW

Asset tracing arises in many areas of California law that seek to differentiate funds, such as money laundering prosecutions,[45] trust law,[46] bankruptcy law,[47] and divorce proceedings.[48] One common area for tracing

44. *Id.* at 245–46.

45. *See, e.g.*, People v. Bolding, 34 Cal. App. 5th 1037, 1046 (2019), *as modified on denial of reh'g* (May 24, 2019) (holding, "[T]he prosecution must demonstrate that the amount of the illegally obtained funds equals or exceeds the amount of the monetary transaction, whether or not the illegally obtained funds have been commingled with legally obtained funds . . . The prosecution need not trace every illegal dollar to the monetary instrument.").

46. *See, e.g.*, Walsh v. Majors, 4 Cal. 2d 384, 399 (1935) (explaining, "The equitable lien of the beneficiary depends upon his being able to trace the trust property into the particular property against which he seeks to enforce the trust, or a commingling with the fund upon which he asserts his lien. Some degree of identification with the property which he seeks to subject to his claim is essential.").

47. *See, e.g.*, In re Goldberg, 158 B.R. 188, 194 (Bankr. E.D. Cal. 1993), *aff'd*, 168 B.R. 382 (B.A.P. 9th Cir. 1994)

48. *See, e.g.*, In re Marriage of Prentis-Margulis & Margulis, 198 Cal. App. 4th 1252, 1281–82 (2011), *as modified* (Aug. 26, 2011), *as modified* (Sept. 9, 2011).

litigation is when a party seeks the recognition of a constructive trust. Constructive trust seeks to prevent unjust enrichment by the person upon whom the trust is imposed.[49] California law provides for the concept of constructive trust in statute, as follows:

> One who gains a thing by fraud, accident, mistake, undue influence, the violation of a trust, or other wrongful act, is, unless he or she has some other and better right thereto, an involuntary trustee of the thing gained, for the benefit of the person who would otherwise have had it.[50]

California courts hold that constructive trust is an equitable remedy, not a right. Thus, constructive trust can be defeated by a statute of limitations claim if it is not perfected in a court proceeding.[51] The case law surrounding constructive trusts explicitly requires some form of tracing, as courts interpreting constructive trusts have noted that "the remedy of constructive trust is defeated if plaintiffs are unable to trace the trust property into its succeeding transfigurements."[52]

Which tracing principles the court will permit at equity is a question inextricably linked with ensuring that the tracing principles achieve an equitable outcome in the case. The 1930 California Supreme Court case of *Mitchell v. Dunn* is instructive.[53] *Mitchell* involved an express trust. The sister trustee commingled her personal funds with trust funds belonging to her incompetent beneficiary brother. The issue for the Court was the ownership of a home that the sister purchased using a withdrawal from the commingled trust account. The Court found that the trust fund contained $9,300, consisting of about $5,400 in trust money and about $3,900 in personal money, when the sister trustee purchased the home for $3,900.[54] The sister testified that she purchased the home using her funds and had put them in the account to hide them from her then-husband.[55] The Court noted that the general rule for an express trust in equity is a presumption that the trustee acted lawfully and withdrew commingled personal funds from the trust account before trust funds.[56] The Court thus presumes "that a trustee acts honestly, and not dishonestly." Under that presumption, the home should belong to the sister-trustee. The Court, however, declined to apply the rule, explaining that"[t]he presumption is nothing more than a fiction created to

49. Heckmann v. Ahmanson, 168 Cal. App. 3d 119, 135 (1985) (explaining that "[t]he purpose of the constructive trust remedy is to prevent unjust enrichment and to prevent a person from taking advantage of his own wrong.").

50. CAL. CIV. CODE § 2224.

51. Embarcadero Mun. Improvement Dist. v. Cnty. of Santa Barbara, 88 Cal. App. 4th 781, 793 (2001) ("A constructive trust is not a substantive device but merely a remedy, and an action seeking to establish a constructive trust is subject to the limitation period of the underlying substantive right.") (citing Davies v. Krasna, 14 Cal. 3d 502, 516 (1975)).

52. *Heckmann*, 168 Cal. App. 3d at 136.

53. Mitchell v. Dunn, 211 Cal. 129 (1930).

54. *Id.* at 134.

55. *Id.* at 133.

56. *Id.* at 135.

assist the [beneficiary of the trust], not to injure him."[57] The Court found mismanagement, disregarded the presumption's use "as a shield for wrongdoing," and awarded the house, the only remaining property in the trust, to the beneficiary brother.[58]

Similarly, when adjudicating bankruptcy cases, the courts have centered on equitable treatment when deciding to embrace or reject different tracing principles. A bankruptcy judge applying California law noted that, "The issue of tracing where trust funds have been commingled with personal funds has fostered divergent rules and fact-sensitive case precedents. These rules generally favor beneficiaries and are premised on preventing unjust enrichment of the trustee."[59] Bankruptcy favors "strict" tracing because recognizing the tracing gives priority to one creditor over another despite both having similar claims while rejecting the tracing means that the assets default to all creditors pro rata.[60] "Strict tracing," requires showing that "the property subject to the constructive trust was specifically and directly exchanged for the property sought to be recognized as trust property" and any commingling renders the trust unenforceable against the commingled funds or property acquired using commingled funds.[61] Requiring "strict tracing" and declining to trace through commingled funds in bankruptcy can ensure that similarly situated creditors are treated equally regarding the remaining funds.

However, bankruptcy departs from strict tracing where it achieves equity. The judge of *In re Goldberg* opted to apply what the Court described as the "liberal" tracing method of *Mitchell.* The Court explained that the debtor would be the only one to benefit from "strict tracing" under the circumstances. Like *Mitchell,* the judge faced a binary conflict between the creditor and the debtor over a single asset. Strict tracing would have resulted in the conclusion that the debtor spent the bank's money and his own personal money remained. The bankruptcy judge wrote, "This court, like the court in *Mitchell,* will not allow Mr. Goldberg to be unjustly enriched based on argument that the only permanent investment from the commingled funds was drawn from his personal funds and the Bank's portion of the commingled funds were used for nonpermanent and untraceable personal expenses."[62] Thus the Court opted to apply a different rule because equity demanded the result.

Claims based on tracing can conflict with asset forfeiture actions. For example, in 2004, the Ninth Circuit recognized the precedence of a constructive trust over the government's right via forfeiture action in *United States v.*

57. *Id.* at 134.
58. *Id.* at 135.
59. In re Goldberg, 158 B.R. at 194.
60. *Id.* at 196.
61. *Id.* at 196.
62. *Id.* at 195; *see also* In re Advent Mgmt. Corp., 178 B.R. 480, 489 (B.A.P. 9th Cir. 1995), *aff'd*, 104 F.3d 293 (9th Cir. 1997) (explaining that, "the constructive trust will not be given effect if it is against the federal bankruptcy policy favoring ratable distribution to all creditors.").

$4,224,958.57 ("Boylan").[63] In *Boylan*, the government sought to forfeit money that had been repatriated after an investment fraud scheme with seventy-six known victims. The attorney for twenty-three of the victims indicated that he might file claims and requested an informal settlement of their interest. Instead, the government forfeited the funds without notifying any fraud victims. After the government obtained the unnoticed default judgment, the attorney for the twenty-three claimant victims filed a motion to set aside the default based on asset tracing that he alleged created a constructive trust entitling the beneficiaries, rather than the government, to the funds. The Ninth Circuit recognized the constructive trust under California Civil Code sections 2223[64] and 2224,[65] set aside the default judgment, and ordered the District Court to administer the funds according to the trusts established by the victims.

The United States Department of Justice disfavors such constructive trust claims in multiple victim cases. Constructive trust claims have practical difficulties and pit victims' claims against one another in what can become complicated and expensive legal proceedings. Regarding distribution of funds, the federal manual on asset forfeiture notes:

> While courts generally agree that fraud victims do not retain legal title in money paid voluntarily into a fraud scheme, some courts occasionally recognize constructive trusts in favor of victims. Under this equitable remedy, the perpetrator of the fraud holds title to the victim's funds in trust for the benefit of the victim. A constructive trust generally requires a victim to trace their money to the seized funds, which may warrant extensive discovery and evidentiary hearings. This legal theory is troublesome in forfeiture cases involving multiple victims because it can transform the forfeiture case into a cumbersome and costly liquidation proceeding in which all victims compete against each other and against the government for the seized funds. The government should generally oppose a claim of constructive trust in multiple-victim fraud cases so that the Attorney General can return the funds to the victims through the orderly remission or restoration process.[66]

The government generally prefers the pro rata distribution that occurs among fraud victims in forfeiture restorations.[67] Despite this preference and its

63. United States v. $4,224,958.57 (hereinafter *Boylan*), 392 F.3d 1002, 1004 (9th Cir. 2004).

64. CAL. CIV. CODE § 2223 (providing that "One who wrongfully detains a thing is an involuntary trustee thereof, for the benefit of the owner.").

65. CAL. CIV. CODE § 2224 (providing that "One who gains a thing by fraud, accident, mistake, undue influence, the violation of a trust, or other wrongful act, is, unless he or she has some other and better right thereto, an involuntary trustee of the thing gained, for the benefit of the person who would otherwise have had it.").

66. U.S. DEP'T OF JUST., CRIM. DIV., ASSET FORFEITURE POLICY MANUAL § 14-12 (2023), https://perma.cc/4MXL-B3T2.

67. *See* 28 C.F.R. § 9.8 (2024) (discussing the other factors considered as follows, "Pro rata basis. In granting remission to multiple victims pursuant to this section, the ruling official should generally grant remission on a pro rata basis to recognized victims when petitions cannot be granted in

application in many circuits, however, in 2011 in *United States v. Wilson*, the Ninth Circuit revisited *Boylan* and rejected the Department of Justice's explicit invitation to overrule *Boylan*'s constructive trust analysis.[68] *Wilson* noted that the timing of a constructive trust's creation is a matter of state law and that *Boylan* correctly interpreted California law regarding a constructive trust's creation at the time of fraudulent transfer.[69]

A strictly administered constructive trust can result in the most recent victim getting money back while older victims, who lost money in the same way to the same fraud, recover none. However, courts can decline to administer the trust so heavily in favor of the single fraud victim and can instead suspend tracing as the judge determines necessary to achieve equity.[70] For example, *Wilson* involved a $13 million Ponzi scheme with over fifty victims.[71] The account seized had a balance of approximately $1.5 million.[72] However, all but $300 traced to the last victim, who sent his money in just before the account was seized. Were the last victim's tracing recognized as a constructive trust, it would entitle him to everything and defeat any other victims' right of recovery. The *Wilson* court recognized the trust, but invited the District Court to administer the trust in an equitable manner that could involve disregarding the trust's claim of priority.[73] The Ninth Circuit explained that "even if the forfeited assets can be traced back to [a single victim's] investment into Wilson's fraudulent scheme, this does not necessarily move him ahead of the other victims in this case."[74] Instead, the Ninth Circuit explained that even where a constructive trust is recognized, "tracing rules can be suspended where equity so demands."[75]

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full due to the limited value of the forfeited property. However, the ruling official may consider the following factors, among others, in establishing appropriate priorities in individual cases:
(1) The specificity and reliability of the evidence establishing a loss;
(2) The fact that a particular victim is suffering an extreme financial hardship;
(3) The fact that a particular victim has cooperated with the Government in the investigation related to the forfeiture or to a related prosecution or civil action; and
(4) In the case of petitions filed by multiple victims of related offenses, the fact that a particular victim is a victim of the offense underlying the forfeiture.").

68. United States v. Wilson, 659 F.3d 947, 954-955 (9th Cir. 2011).

69. The decision conceded that some California decisions suggest that constructive trusts do not arise until they are recognized by a court but instead relied upon its own interpretation of the California law. *Cf.*, United States v. Ramunno, 599 F.3d 1269, 1274-1275 (11th Cir. 2010) (discussing that under Georgia State law a constructive trust is formed when recognized by the court, not at the time of the fraud).

70. *See, e.g.*, United States v. 13328 & 13324 State Highway 75 N., 89 F.3d 551, 553 (9th Cir. 1996) (stating in the context of an SEC forfeiture action, "As in *Cunningham*, this is a case where 'equality is equity.'" (citing Cunningham v. Brown, 265 U.S. 1, 13 (1924)).

71. *Wilson*, 659 F.3d at 949. Authorities also seized $425,000 that had been transferred from the account.

72. *Id.*

73. *Id.* at 956.

74. *Id.*

75. *Id.* (citing Cunningham v. Brown, 265 U.S. 1, 13 (1924) (finding that "[this] is a case the circumstances of which call strongly for the principle that equality is equity, and this is the spirit of the bankrupt law. Those who were successful in the race of diligence violated not only its spirit, but its letter,

In contrast to constructive trusts and equitable tracing, California's family law courts have fashioned a fact-intensive inquiry based on each case's specific facts. For example, co-mingling of marital and separate property "creates a rebuttable presumption that all the funds in the account are community property."[76] To overcome this presumption, courts evolved how they apply the "traditional family law tracing methods" of direct tracing and the "family expense" method of tracing.[77] The intricacies are beyond the scope of this article except to note that direct tracing commingled funds is based on the facts of each case and the intent of each transaction. In that context:

> [S]eparate funds do not lose their character as such when commingled with community funds in a bank account so long as the amount thereof can be ascertained. Whether separate funds so deposited continue to be on deposit when a withdrawal is made from such a bank account for the purpose of purchasing specific property, and whether the intention of the drawer is to withdraw such funds therefrom, are questions of fact for determination by the trial court.[78]

Accordingly, California family law proceedings consider the intent of the transaction at each account instead of applying maxims or presumptions. This inquiry makes sense where the mental state is known because the transaction was done or authorized by one of the parties.

These cases demonstrate that California courts recognize tracing evidence as necessary to achieve equitable results. The tracing rule applied depends upon the legal issue the tracing is being offered to resolve. However, there is no published case regarding the appropriate rule for considering a tracing in return of property proceedings. Accordingly, courts may wish to examine the parties involved in the proceeding, the equity of the default outcome, and the equity of the result to be achieved by accepting different forms of tracing evidence when deciding such cases.

IV. CALIFORNIA LAW REGARDING RETURN OF STOLEN PROPERTY

California law does not currently include a specific forfeiture statute that can be used to target transnational scam organizations without a criminal conviction, which can be challenging for many reasons. The only applicable forfeiture statutes require a criminal conviction.[79] However, convicting those persons who are criminally responsible for the conduct of a transnational scam

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and secured an unlawful preference.")). Accordingly, the Court concluded that "courts generally will not indulge in tracing when doing so would allow one fraud victim to recover all of his losses at the expense of other victims." *Id.*

76. In re Marriage of Prentis-Margulis & Margulis, 198 Cal. App. 4th 1252, 1281 (2011), *as modified* (Aug. 26, 2011), *as modified* (Sept. 9, 2011) (hereinafter *Margulis*).

77. *Margulis*, 198 Cal. App. 4th at 1281–82.

78. Hicks v. Hicks, 211 Cal. App. 2d 144, 157 (1962).

79. *See* CAL. PENAL CODE §§ 186.3, 186.11. *Cf.*, CAL. HEALTH & SAFETY CODE § 11488 (providing guidelines for forfeiture in drug crimes).

organization is not easy. The hierarchical nature of organized crime means that the most culpable actors who receive the benefit of fraud proceeds are not necessarily those directly perpetrating the scams or even those directly laundering the money. Transnational organized crime groups perpetrate their scams from foreign countries outside the reach of state courts. Those directly perpetrating scams and those laundering the money can be victims themselves, subject to coercion by members of the organization as well as corrupt state actors profiting from the activities of the organization.[80] Criminal prosecution requires identifying the perpetrator, investigating sufficiently to determine their individual culpability, and obtaining foreign cooperation to safely seize them and deliver them in custody to a California criminal court. Such investigations require strong international reach, including resources available to appropriately investigate in each jurisdiction that contains necessary evidence as well as the ability to ultimately locate the suspect and convince the relevant jurisdiction to undertake an arrest operation.

Confronted with these challenges, California prosecutors have opted to use return of property laws to try to retrieve money for fraud victims. While California law enforcement officers may use a search warrant to temporarily seize suspected stolen property,[81] California law also presumes that the person who possessed the property owned it.[82] If it can be proven that the property is stolen, however, then law enforcement may not return it because stolen property is contraband under California law.[83] Stolen property must be returned to the true owner or forfeited to the treasury if the true owner cannot be found.[84]

In some circumstances, the victim can initiate the return of stolen property without the assistance of the prosecution. They only have standing to do so, however, during a charged criminal prosecution where they are an alleged victim. The Court of Appeal explained:

> [A] third party claimant to seized property has no standing to apply for delivery of the property or to prove ownership in criminal court, until (1) the People allege that the person from whom the property was seized stole or embezzled the property, in a criminal complaint or charge (§

80. This may decrease as the availability of artificial intelligence replaces the need for as many human victims.

81. CAL. PENAL CODE § 1524 (a)(1).

82. CAL. EVID. CODE § 637.

83. People v. Superior Court (McGraw), 100 Cal. App. 3d 154, 157 (1979) (hereinafter *McGraw*) [categorizing that, "Stolen property in the hands of the thief is contraband."]; *see also* Ensoniq Corp. v. Superior Ct. (1998) 65 Cal. App. 4th 1537, 1547 (hereinafter *Ensoniq*) citing *McGraw* at p. 157 (explaining that, "only legal property may be returned to the person from whom it was taken. '[T]he People have the right to detain any property which it is unlawful to possess, and such right exists whether the property was lawfully seized or not.'") citing Aday v. Superior Court (Alameda), 55 Cal. 2d 789, 780 (1961).

84. *See, e.g,.* CAL. PENAL CODE §§ 1409-1410 (1872) (discussing return of stolen property to victims of theft); *see also Ensoniq*, 65 Cal. App. 4th at 1549–50 (discussing the rules of the special proceedings to do so); *see generally* CAL. CIV. PROC. CODE § 23 (governing special proceedings generally).

> 1408); (2) the People have proven that the property was stolen or embezzled by obtaining a conviction of theft or embezzlement (§ 1409); or (3) the People have proven by a preponderance of the evidence in a special proceeding that the person from whom the property was seized stole or embezzled it.[85]

Once a criminal charge is filed, any victim alleged in the complaint possesses a statutory and constitutional right to ask the judge presiding over the criminal proceedings to timely return their stolen property.[86] However, there are some limitations. For example, the return of property must not prejudice the State, meaning that the property may only be returned once it is no longer needed as evidence. Additionally, in these cases,[87] the victim must convince the criminal court presiding over the proceedings that the property belongs to them; specifically, the victim must provide "satisfactory proof of his ownership of the property. . . ."[88]

Where no criminal charges are filed, the Court of Appeal has made clear that the prosecution can still determine that the property is stolen and pursue returning it to the owner. Courts created a special return of property proceeding because the relevant statutes contained no legislative guidance on how to proceed in the absence of a criminal case.[89] Accordingly, in *People v. Superior Court ("McGraw"),* the Court of Appeal fashioned a procedure for a fair hearing, stating, "[t]he People would be required to prove the property was stolen by a preponderance of the evidence, as in all determinations of ownership. All relevant evidence on the issue would be admissible."[90] Thus, at the special hearing, the standard to prove that the property is stolen is higher than the standard to issue the search warrant.

The Court of Appeal has also held that deciding whether to bring a proceeding seeking to prove that property is stolen is a matter of prosecutorial discretion.[91] In *Ensoniq v. Superior Court* ("*Ensoniq*"), the Court addressed allegedly stolen property's disposition following the prosecutor's declination to

85. *Ensoniq*, 65 Cal. App. 4th at 1550.

86. CAL. PENAL CODE § 1408 (1872); *see also* Cal. Const. art. I, § 28(b)(14). The filing of a complaint is necessary and courts have held that "a search warrant issued upon grounds that there is probable cause to believe that the property to be seized was stolen or embezzled does not state an allegation which would enable a third party to make an application for delivery of the property under section 1408." *Ensoniq*, 65 Cal. App. 4th at 1548.

87. The same principles apply to post-conviction claims submitted pursuant to Penal Code section 1409, although at that point the theft conviction is available in support of such applications.

88. CAL. PENAL CODE § 1408.

89. *McGraw*, 100 Cal. App. 3d at 159 (finding that, "no statute or case authority for the appropriate procedure to follow to make the initial determination of whether property seized in the execution of a search warrant is in fact stolen property.").

90. *Id.*

91. *Ensoniq*, 65 Cal. App. 4th at 1551 (explaining "the discretionary power of the district attorney also extends to decisions regarding whether to object to the court's disposal of property seized pursuant to warrant.").

file charges regarding theft of trade secrets.[92] The Santa Clara County prosecutor who declined to file charges stated that he did so because the defendant did not act with the required *mens rea*. The prosecutor further specified the decision did not mean the District Attorney determined whether the defendant or the victim was the rightful owner of the allegedly stolen trade secrets.[93] Thereafter, both parties filed motions to receive the property. The defendant filed a motion for return of the property pursuant to Penal Code sections 1536, 1539, and 1540.[94] The victim corporation, Ensoniq, filed a motion for return of the allegedly stolen property pursuant to Penal Code section 1407 et seq. The Court set a hearing to resolve the competing motions.

At the ownership hearing, the District Attorney stated, "We do not take a position on that matter" and described the prosecution as a neutral third party in a dispute between the victim and the defendant regarding the allegedly stolen property.[95] Ensoniq asked that it be permitted to present the evidence at the special proceeding.[96] However, the trial court found that the victim had no standing, and instead ordered the District Attorney to present the evidence at the special proceedings to determine the true owner over the District Attorney's objection.[97]

The Court of Appeal overturned that order. It held that the trial court correctly determined that the victim lacked standing to object to the return of the property or to present evidence to establish their claim but erred in ordering the prosecution to do so on behalf of the victim.[98] The Court explained,

It is within the discretion of the district attorney to oppose such a motion if the district attorney believes that the property should be detained by the People because its possession is unlawful, or if the district attorney believes the property was stolen or embezzled. It is also within the district attorney's discretion to decide not to oppose a motion for return of property because the People cannot prove that the property is stolen or otherwise illegal.[99]

The *Ensoniq* decision noted that it sought to draw a distinction between the criminal return of property statutes that dispose of a *res* seized by a criminal warrant and various civil claims related to theft and conversion that might be asserted between the parties. The Court of Appeal explained,

> [W]e think it was never intended that the district attorney should be compelled to participate in an evidentiary hearing regarding a motion to return seized property when no criminal proceedings are pending, and the district attorney cannot prove the seized property is stolen. We do

92. *Id.* at 1544.
93. *Id.*
94. *Id.*
95. *Id.* at 1545.
96. *Id.* at 1545-46.
97. *Id.*
98. *Id.* at 1551–54.
99. *Id.* at 1551.

> not think that the criminal courts are available for the purpose of shortcut solutions to intellectual property disputes. ¶ However, we emphasize that our ruling today has no effect upon any civil remedies which may be asserted by either Ensoniq or Dattoro.[100]

Taken together, *McGraw* and *Ensoniq* establish that when the prosecution declines prosecution or is unable to file criminal charges related to property obtained by a search warrant that is allegedly stolen, the prosecution must decide whether they can meet the preponderance of the evidence standard to prove the *res* is stolen or return it. If the prosecution succeeds in rebutting the presumption and proves that the *res* is stolen, that results in denial of the return of the stolen property.

These California decisions detail how to resolve the conflict between the original possessor's interest and the prosecution's claim that property is stolen.[101] However, if the court denies return to the original possessor, it still must consider the related question of who should receive the stolen property. Published decisions do not address the resolution of conflicts at this stage of the proceeding. The relevant statutes contemplate that the true owner files an application, that establishes proof of ownership or title to receive property from the court, for return of the stolen property.[102] They do not set forth how to resolve competing claims from multiple victims to own the same property.

A. Finding that Seized Cryptocurrency is Stolen Property

The first issue the court must decide, if it is contested, is resolving the conflict between the person from whom the property was taken and the government agency refusing its return. Because the possessor is the presumed owner, the prosecution must present a prima facie case the property is stolen. In setting forth the standard, the Court explained,

> Due process requires that the determination of whether the seized property is stolen must be the result of a fair hearing. Evidence Code section 637 provides that the "things which a person possesses are presumed to be owned by him." Such a presumption assumes the existence of the presumed fact "unless and until evidence is introduced which would support a finding of its nonexistence, in which case the trier of fact shall determine the existence or nonexistence of the presumed fact from the evidence and without regard to the presumption." . . . Thus, the subject property is presumed to be owned by the real parties in interest until the state has presented evidence which would support a finding that real parties did not in fact own the property.[103]

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100. *Ensoniq*, 65 Cal. App. 4th at 1554 (n. omitted).

101. *See e.g.* Lawrence v. Superior Court, 21 Cal. App. 5th 513, 523 (2018) (holding that the prosecution must establish the original possessor's interest is illegitimate and the property is stolen before the court can consider the claim of any other alleged owner that the property belongs to them).

102. CAL. PENAL CODE §§ 1408-1410; *see generally* CAL. EVID. CODE § 115 (stating, "Except as otherwise provided by law, the burden of proof requires proof by a preponderance of the evidence.").

103. *McGraw*, 100 Cal. App. 3d at 159.

Under *McGraw*, the Court must begin the proceeding by assuming that cryptocurrency belongs to the owner of the account from which it was taken. The prosecution must introduce evidence to rebut the presumption by proving the cryptocurrency is stolen property.

Proving the illegitimacy of the seized cryptocurrency can be accomplished without the use of presumption-based tracing. Identifying the owner is not necessary to establish that cryptocurrency is stolen. For example, police can recover a cache of stolen jewelry from a fence or stolen auto parts at a chop shop, and similar scenarios exist in cryptocurrency. The circumstances of the recovery indicate that the property is stolen, even if police have yet to identify the true owner.

Suspicion that the original possessor is laundering or holding the cryptocurrency for a transnational scam organization can be corroborated with evidence derived from the customer records at the exchange about the original possessor, such as identity documents, geolocation of the login history, device information, and analysis of the other transaction activity within the account. Police can further corroborate with evidence about the blockchain transactions at accounts that interact directly and indirectly with the original possessor's account, including the extent of the connection to victim accounts, the patterns of transaction activity in intermediary wallets, and the existence of other suspicious transactions into and out of the original possessor's account. Police can use these records to build a profile of the account that is consistent with participation in money laundering and receipt of laundered funds. Such evidence should be sufficient to overcome the presumption and weigh in favor of finding the property is stolen in the absence of a legitimate explanation.

Once the presumption is overcome, the court balances the prosecution's showing of illegitimacy against the original possessor's explanation and any evidence that corroborates it. When considering the original possessor's corroboration, the court may also consider that the original possessor is best situated to produce evidence. Money moves for a reason, and a legitimate owner should at the very least be able to explain and corroborate the reasons for transactions involving their own account. However, the stronger the prosecution's showing, the more convincing and comprehensive the evidence of legitimacy should be to obtain return of the seized property. The court then decides the motion using the ordinary preponderance standard.

B. Using Presumption-Based Tracing to Identify the True Owner

The second issue at a return of property proceeding is disposal of the stolen property. California law provides that property seized by search warrant must be held by the law enforcement agency subject to further direction by the magistrate.[104] Upon receiving a proper application and proof of title, the

104. CAL. PENAL CODE § 1536.

magistrate orders that the stolen property be returned to its owner. [105] The law enforcement agency has a statutory duty to notify the true owner if they can determine the owner's identity, so that the owner knows that they can make the application.[106]

Many state and local law enforcement agencies structure their investigations in a manner that links the seized cryptocurrency to one single victim. The agency opens a new case every time they receive a new report that someone in their jurisdiction is the victim of fraud or a scam. The purpose of the investigation is to try to seize funds from a scam organization and return them to that victim. Using the agency's preferred method, the assigned investigator traces the victim's transactions and then applies for a search warrant to seize any cryptocurrency identified by the traces. After seizing the cryptocurrency, the agency closes the investigation and notifies the victim that they can apply to the court for return of the seized cryptocurrency. Accordingly, return of property proceedings often originate as a motion by a single victim seeking their cryptocurrency. The victim's claim is based on the tracing evidence generated by the law enforcement agency. Using this system, almost all cases appear to involve a binary conflict between the victim claimant and the original possessor.

Some cases are a binary conflict with only two possible outcomes. For example, assume a single victim reports to a law enforcement agency. Assume that there are no other victim reports with similarities available to the law enforcement agency. Finally, assume that the scam organization laundered the reporting victim's cryptocurrency in a way that makes using the blockchain to identify any other victims of the same organization impossible. Under such circumstances, the identity of the victim and the existence of the tracing will be the only information available to the victim, the law enforcement agency, and the court. Presented with a binary choice between returning stolen cryptocurrency to the only known victim or forfeiting it to the county treasury, the court may consider it more equitable to recognize the tracing as true and find the victim to be the true owner entitled to return of the property.[107] However, the act of awarding title to one among many is not necessarily a binary choice if more information is known to the victim, the law enforcement agency, or the court.

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105. CAL. PENAL CODE § 1409 (providing that "If property stolen or embezzled comes into the custody of the magistrate, it shall be delivered, without prejudice to the state, to the owner upon his application to the court and on satisfactory proof of his title, after reasonable notice and opportunity to be heard has been given to the person from whom custody of the property was taken and any other person as required by the magistrate, and on his paying the necessary expenses incurred in its preservation, to be certified by the magistrate.").

106. CAL. PENAL CODE § 1411.

107. *See generally* United States v. Henshaw, 388 F.3d 738, 741 (10th Cir. 2004) (guiding that, "There are several alternative methods, none of which is optimal for all commingling cases; courts exercise case-specific judgment to select the method best suited to achieve a fair and equitable result on the facts before them.").

Consider the case of ten law enforcement agencies that each receive a separate report from one of ten different victims. Assume each of the ten victims lost $10,000 to the same scam organization and the $100,000 total initially went into the same collection account. Assume also that the collection account forwarded $90,000 in nine withdrawals to separate accounts, so that $10,000 remains in the collection account and $10,000 is in each of the accounts that received a withdrawal.[108] There are ten known victims, one scam organization, and the scam organization has $100,000 in ten accounts.

Now assume each agency investigates the case in the manner described above and each agency uses the same tracing method. For example, every agency would follow the first withdrawal after the victim's deposit if using the PIFO method. The first agency to do a search warrant would recover the $10,000 and return it to their victim. Each of the other agencies would arrive at the same account, see that no funds remain and recover $0. PIFO tracing results in $10,000 recovered for one victim and $90,000 remaining with the scam organization. Which victim receives the $10,000 recovery depends on which agency executes their search warrant first, not on which victim has the superior claim.

The result may not be optimal, but such a system does appear capable of resolving motions on a case-by-case basis. After all, the court must select a method to award the commingled funds, and deferring to what investigators used during the criminal investigation is one way to select the tracing method. Recognizing the method used by the law enforcement agency is pragmatic and ensures that the victim cited to establish probable cause in the search warrant receives the property seized. The court's order achieves full justice for the victim identified in the warrant, awarding that victim all funds seized by the law enforcement agency investigating their case. The other victims will likely be told that no recovery by law enforcement is possible and are unlikely to obtain the detailed knowledge of tracing necessary to understand that a conflict occurred.

However, awarding all seized funds to the first victim identified by law enforcement does not achieve equity between similarly situated individuals. The nine victims with equivalent tracing claims will not view the outcome as equitable if they are provided with a detailed explanation of the outcome of the first victim's return of property hearing. What happens if a victim learns that they have an equivalent claim to the seized funds, but they could not assert their equivalent claim because the other claimant applied for return of the funds and did not provide them notice of the return of property hearing? [109] The victim who

108. Assume also that those accounts have no subsequent transactions.

109. The return of property statutes mandate notice and an opportunity to be heard for "the person from whom custody of the property was taken and any other person as required by the magistrate." CAL. PENAL CODE §§ 1408-1410. Accordingly, the court is unlikely to learn of any contradictory claims by other victims unless the court affirmatively requires the moving party to investigate and notice other potential claimant victims.

did not recover may file a civil lawsuit against the victim who recovered seeking a proportional share of the recovery, inviting litigation between victims.[110]

The decisions for the victims, law enforcement agency, and the court become more complex if multiple victims' interests are known before the return of property proceeding. For example, assume two of the victims made reports to the same agency and in quick succession. What happens when that agency traces two open cases to the exact same cryptocurrency? What does the agency say to each victim about being the true owner? Does the victim have any obligation to notice the other victim when they file their motion? What position does the law enforcement agency take regarding the distribution of the seized cryptocurrency at the return of property hearing if both victims know about the hearing date and have an equivalent claim based on their investigation? What does the court do?

PIFO tracing evidence alone cannot resolve the dispute. Each of the victims possesses an equivalent PIFO claim to "own" the same $10,000. Accordingly, the court may split the funds between the two victims.[111] However, that compromise introduces the concept of pro rata distribution based on the law enforcement agency's knowledge, a hybrid model, instead of strictly following the first victim model. The availability of pro rata sharing invites the question of whether the agency has any obligation to attempt to identify the eight other victims. Each possesses an equivalent PIFO claim to "own" the same $10,000, and the publicly available blockchain records show eight other transactions into the known collection account, suggesting that the owners of those accounts are victims. Some agencies may attempt to investigate further and identify, while others may not.

The discussion thus far has consisted of agencies using a single tracing method, PIFO. However, there are multiple tracing methods that can reach different conclusions. For example, some would argue that LIFO is better than PIFO at resolving the ten-agency hypothetical. LIFO does not merge victim claims like PIFO. Every dollar of funds seized resolves to a single victim of origin. Using LIFO for the ten-agency hypothetical would have resulted in each victim having an exclusive claim to a different $10,000. Each of the ten victims would recover their own $10,000 and the scam organization would be left with $0. This is because LIFO uses a different presumption.

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110. The Court of Appeal explained in *Ensoniq* that the award of physical custody to the victim does not preclude the original possessor from suing in civil court to seek its return. *Ensoniq*, 65 Cal.App.4th at 1550 (explaining "The order of the magistrate awarding actual possession to the third party claimant is not res judicata as to the issue of ownership, and the person from whom the property was seized may maintain a civil action against the person to whom the property was delivered. . . . ¶ Similarly, if the magistrate orders the property returned to the person from whom it was seized, the third party claimant is not barred by the magistrate's order from asserting any civil remedies against the person awarded actual possession. The limited nature of the magistrate's order is consistent with the rule that the summary remedy of a motion for return of seized property cannot be turned into a civil proceeding for conversion.") It stands to reason that the other victims may also sue the prevailing victim to see if a different court will recognize their entitlement to a proportional share.

111. This could be done evenly or proportionally based on loss.

For simplicity, this LIFO analysis assumes all ten deposits happened before any withdrawals, followed by ten withdrawals. Using LIFO, the first victim would not follow any of the withdrawals because they would all be attributed to the subsequent, more recent, deposits. Each of the next nine victims would follow a withdrawal in reverse chronological order. The last victim in time would recover the funds in the first withdrawal out of the collection account, the second to last victim in time would recover the funds in the second withdrawal out of the collection account, and so forth. The first victim recovers the $10,000 left in the collection account. The order of the search warrants would not affect the outcome of the return of property proceedings.

Courts could ensure that every cryptocurrency tracing case in every California jurisdiction has a definite, non-contradictory result by establishing a statewide standard that all courts must use LIFO at a return of property motion. California law enforcement agencies would never receive reports from two different victims that trace to the same cryptocurrency and could identify all victims and provide them notice to file a return of property hearing using the chosen method. Every motion before the court would be decided using a single rule known to all parties in advance. However, ensuring the use of a single method still requires making the choice of one victim over another where both have been equally wronged and are equally deserving of the seized funds.

FIFO also evenly divides seized funds among victims. Using FIFO in the hypothetical, all ten victims would recover $10,000, the scam organization would retain none, and the order of search warrants would also be irrelevant to the outcome of the return of property proceedings. Using either FIFO or LIFO achieves different outcomes for the ten-agency hypothetical, but both outcomes are equally fair to every victim. However, the choice between FIFO or LIFO can create equitable conflicts between similarly situated victims in real world applications. The ten-agency hypothetical is artificial because it assumes that the government recovers every dollar belonging to every victim. That almost never happens in real life. Law enforcement agencies usually seize only a portion of all laundered funds. This means that selection of either FIFO or LIFO is likely to change which victims recover and which do not.

For example, assume an agency that uses FIFO seizes funds in only two of the ten accounts in the hypothetical. The agency would notify two victims that they each own $10,000 of the seizure based on the FIFO tracing done during the investigation. Those two victims would file a motion for return of property. The court would indicate that the statewide rule is LIFO instead of FIFO and order the agency to do a LIFO tracing and notice new victims. The agency would identify two different victims and notify them they each own $10,000 of the seizure based on the LIFO tracing ordered by the court.[112] The choice of LIFO

112. If one of the two accounts is the first withdrawal made after the deposits, then all eight of the non-recovering victims could also make a PIFO tracing claim but would never learn of the hearing.

over FIFO is an arbitrary one, but that arbitrary choice becomes the reason that two victims do not recover and that two different victims do recover, despite the fact that all victims are similarly situated.

Whatever method is selected, tracing can result in different outcomes for similarly situated victims for reasons that do not relate to which victim suffered a greater loss or is more entitled to compensation. In such circumstances, courts may opt to disregard tracing altogether.[113] Courts may follow the example that the Ninth Circuit set in *Wilson* and recognize a constructive trust based on one of the tracings but disregard the tracing victim's priority while administering the funds.[114] Constructive trust is an equitable remedy to prevent unjust enrichment by the person upon whom the trust is imposed.[115] Such trusts are a remedy for fraud victims,

In order to provide the necessary flexibility to apply an equitable doctrine to individual cases, these sections state general principles for a court's guidance rather than restrictive rules. [Citation.] Thus, it has been pointed out that "a constructive trust may be imposed in practically any case where there is a wrongful acquisition or detention of property to which another is entitled." [Citations.][116]

Wilson applied California law to recognize the existence of a constructive trust based on tracing from victim Richard A. Gray, Jr. to seized funds. However, *Wilson* explained that the District Court could administer the resulting trust by disregarding Mr. Gray's priority to achieve a more equitable pro rata distribution.[117] The District Court ordered the funds in the constructive trust distributed pro rata to all victims of the Ponzi scheme, explaining that "equity justifies suspension of the tracing rules; allowing the constructive trust to be administered solely on the basis of tracing fictions would allow the Petitioners to recover their losses at the expense of other victims."[118] Such pro rata distributions are fair and equitable in the sense that they treat all known victims

113. *See e.g.* Ruddle v. Moore, 411 F.2d 718, 718 (D.C. Cir. 1969) (explaining that, "When the law adopts a fiction, it is, or at least it should be, for some purpose of justice. To adopt it here is to apportion a common misfortune through a test which has no relation whatever to the justice of the case.").

114. United States v. Wilson, 659 F.3d at 954-955.

115. Heckmann v. Ahmanson, 168 Cal. App. 3d 119, 135 (1985) (explaining that "The purpose of the constructive trust remedy is to prevent unjust enrichment and to prevent a person from taking advantage of his own wrong.").

116. Martin v. Kehl, 145 Cal. App. 3d 228, 237–38 (1983).

117. *Wilson*, 659 F.3d at 956 (explaining that "even if the forfeited assets can be traced back to Gray's investment into Wilson's fraudulent scheme, this does not necessarily move him ahead of the other victims in this case.").

118. United States v. Wilson, No. CR S-08-114 LKK, 2013 WL 322583, at 3 (E.D. Cal. Jan. 28, 2013) (ordering as follows: "(4) The court FINDS that $1,700,446.63 of the seized funds are subject to Gray Petitioners' constructive trust and $74,025.48 of the seized funds are subject to Bailey's constructive trust. (5) The constructive trust funds SHALL be distributed to all victims in proportion to their losses.").

of the same fraud scheme equally, but they may require an extensive investigation to identify as many victims as reasonably possible.

Courts could seek to avoid the harshness of a LIFO only rule by recognizing the existence of a constructive trust and ordering pro rata distribution between all LIFO and FIFO claimants in every case. However, consider again the ten-agency hypothetical. The other six victims without LIFO or FIFO tracing would likely point out that they are similarly situated but for the existence of legal fiction. They lost money in the exact same way to the exact same scam organization. Accordingly, other courts might expand the distribution to the other victims known to the investigating agency who lost money to the same scam organization in the same manner.

Some courts may look at all the conflicting scenarios and reject presumption-based tracing entirely when awarding seized cryptocurrency using the return of property law. They may look to *Voigt* and insist that the claimant establish title without relying on presumption-based tracing. Meeting that standard could only be done if there is no commingling. Therefore, cases that involve money laundering by a scam organization would almost always result in a conclusion that the true owner cannot be "reasonably ascertained" and forfeit the seized cryptocurrency to the county treasury.[119]

V. CIVIL ASSET FORFEITURE OF CRYPTOCURRENCY IN CALIFORNIA: WHAT SHOULD IT LOOK LIKE?

A civil asset forfeiture statute specifying the method for returning cryptocurrency would create a uniform statewide legal standard for California law. Other jurisdictions already have a comprehensive set of rules for the seizure and return of cryptocurrency using civil asset forfeiture. Federal asset forfeiture statutes have been interpreted to cover laundered cryptocurrency.[120] Other states are also pursuing cryptocurrency forfeiture statutes.[121] For example, Connecticut just passed a cryptocurrency-specific statute.[122] However, California lacks the ability to use civil asset forfeiture for fraud proceeds being laundered by scam organizations. Today victims and their attorneys must guess how each jurisdiction will handle the return of property proceeding, because there is little statutory authority. Giving priority to a forfeiture statute would provide victims,

119. CAL. PENAL CODE § 1411.

120. United States v. Ulbricht, 31 F. Supp. 3d 540, 570 (S.D.N.Y. 2014) (finding the federal statute "broad enough to encompass use of Bitcoins in financial transactions. Any other reading would—in light of Bitcoins' sole raison d'etre—be nonsensical. Congress intended to prevent criminals from finding ways to wash the proceeds of criminal activity by transferring proceeds to other similar or different items that store significant value."); *see also* United States v. Iossifov, 45 F.4th 899, 913 (6th Cir. 2022), *cert. denied*, 143 S. Ct. 812 (2023); *see generally* 18 U.S.C. §§ 1956 (a), (c)(4).

121. Nat'l Ass'n Att'ys Gen., Crypto-Crackdown: Criminal Forfeiture of Cryptocurrencies by States (Dec. 19, 2025), https://www.naag.org/attorney-general-journal/crypto-crackdown-criminal-forfeiture-of-cryptocurrencies-by-states/

122. H.B. 6990, 2025 Reg. Sess. (Conn. 2025) (enacting a new cryptocurrency-specific forfeiture statute).

law enforcement agencies, and courts with clear guidance regarding the standard for seizure and for who receives the seized property that does not change by jurisdiction or court.

For example, the statute could explicitly state that the probable cause finding from the seizure warrant's issuance is sufficient to shift the burden to the original possessor of the seized cryptocurrency. Alternatively, the statute could use some other standard of proof, such as a preponderance of the evidence, but specify that showing cryptocurrency is traceable to a California crime or fraud is sufficient to meet that burden.[123] The challenge is to create a rule that enables the court to decide whether to permit the seizure in a rational and consistent manner on the merits. The rule should allow for seizure of illegitimate cryptocurrency but ensure return of legitimate cryptocurrency to the original possessor. The statute should provide the original possessor with opportunity to explain the source of the seized funds, and any other suspicious transactions, and require consideration of that evidence before forfeiture.

The statute can also provide a uniform rule for distributing seized assets once the court denies return to the original possessor. Restoration is an alternative to adversarial return of property proceedings where every victim competes against every other victim claiming to be the true owner of seized funds using presumption-based tracing. Restoration proceedings focus less on attempting to deconstruct commingling and more on distributing the perpetrator's assets to all identifiable victims of the relevant crimes or conspiracies. First, the government takes ownership of the crime proceeds based on specific alleged criminal activity, whether it is fraud or money laundering. Then, the government seeks to identify all victims who suffered because of the specified criminal activity or related criminal activity of the perpetrator. Finally, the government distributes the property to the victims who have been harmed, proportional to the amount of loss each victim suffered.

Though forfeiture favors pro rata distribution based on loss, it can be structured to also consider other equitable factors. For example, federal asset forfeiture rules outline the following considerations when distributing seized funds:

> Pro rata basis. In granting remission to multiple victims pursuant to this section, the ruling official should generally grant remission on a pro rata basis to recognized victims when petitions cannot be granted in full due to the limited value of the forfeited property. However, the ruling official may consider the following factors, among others, in establishing appropriate priorities in individual cases:
>
> (1) The specificity and reliability of the evidence establishing a loss;
>
> (2) The fact that a particular victim is suffering an extreme financial

123. Presumption-based tracing evidence is likely necessary to link cryptocurrency to California crime victims.

> hardship;
>
> (3) The fact that a particular victim has cooperated with the Government in the investigation related to the forfeiture or to a related prosecution or civil action; and
>
> (4) In the case of petitions filed by multiple victims of related offenses, the fact that a particular victim is a victim of the offense underlying the forfeiture.[124]

The federal approach reflects a balance between the need for a uniform rule and the ability of a detached decision-maker to depart where more desirable results can be achieved by considering other factors. Similarly, a California statute can incorporate those factors that the Legislature feels should be considered to achieve an equitable outcome.

Finally, a forfeiture statute would likely prove a more powerful tool for victims than relying on stolen property statutes. Forfeiture could provide for seizures using an instrumentality theory, like the federal forfeiture statutes. Such language would enable the seizure of all funds in the possession of any money laundering network that launders stolen cryptocurrency of California fraud victims. Use of that provision would likely result in larger seizures, distributed to more victims, than current efforts.

CONCLUSION

Some law enforcement agencies have used search warrants to seize cryptocurrency and return it to victims in the State of California using the return of property statutes. However, the return of property statutes require proof of title and thus were not intended to distribute fungible, commingled cryptocurrency that has been stolen from many victims and laundered by a transnational crime organization. Claims to be the sole owner of such property, despite the commingling, require the use of forensic techniques like presumption-based tracing. The ability of presumption-based tracing to separate commingled assets makes it a useful tool but also makes it malleable, complex, and prone to resolving return of property matters inequitably. Courts may declare a true owner based on a legal fiction subject to challenge by the other victims, or decide that it is not possible and forfeit the property. An *in rem* forfeiture statute would provide clearer guidance for law enforcement, claimants, and courts, and avoid adversarial proceedings where similarly situated victims compete against each other for ownership.

124. 28 C.F.R. § 9.8 (2024).